Competition Law *insight*

Antitrust law and policy in a global market

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Competition Law insight

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UK competition law passes its MOT

The UK's competition regime gets high marks for effectiveness from the National Audit Office (NAO) in a report published on 22 March. The main shortcomings are the scant use made by the industry regulators of their competition law powers and the general lack of enthusiasm for market investigation references to the Competition Commission.

Overall, the regime is extraordinarily good value for money. For an annual outlay of £27m, the revenue from fines in recent years has averaged £78m and the saving to consumers from the deterrent effect of enforcement is estimated at nearly 25 times the outlay. To compare it with an example taken at random, a study published on 30 March found that the gross return on £5bn invested in regional development projects was 3.3 times, with a long-term potential of eight times.

Only UK competition law proper was reviewed – the Competition Act 1998 and the Enterprise Act 2002 as enforced by the Competition Commission and Office of Fair Trading, together with the regulators for communications, energy, water and rail, and as adjudicated by the Competition Appeal Tribunal.

Since 2000, the OFT has brought 43 proceedings, 24 of which resulted in a finding of infringement. This fairly modest total hides a fat tail. OFT research suggests that each of its decisions has deterred seven anticompetitive commercial agreements, five cartels or four abuses of market power by dominant companies.

By contrast, no industry regulator has yet used the anti-cartel powers under Chapter 1 of the 1998 Act. Even more strikingly, only two of their 36 abuse of dominance cases have resulted in a finding of infringement (energy and rail). Of Ofcom's 23 cases under Chapter 2, none has led to such a finding.

This record raises the question of whether the regulators' competition law powers are redundant. Their inaction is mainly due to scarcity of resources and the option of applying regulatory powers, such as altering licensing terms, to achieve the same end.

Competition law rulings have the merit of laying down precedents that ultimately reduce the caseload. The NAO takes a long-term, if idealistic, view and would like to see more case law that has been fully decided and tested on appeal.

Regulators, industry and consumers take a more practical view. They would rather have a solution now than wait the months or years that full-dress competition law proceedings take to reach a state of clarity.

This factor probably accounts for the paucity of market investigation references to the Competition Commission too. These are thorough, objective and effective, but extremely long-drawn-out. On average, they have taken 43 months from the opening of the initial market study to the fixing of the remedies or the outcome of an appeal.

Loss of control over "their" market is a factor that may also make the process unappetising to the industry regulators. However, it is not only they but also the OFT who have made disappointing use of this facility.

Initial planning assumptions allocated resources for four references a year, three from the OFT and one from a regulator. In fact, only 10 references in all have been made since 2002, nine of them from the OFT and one (railway rolling stock) from a regulator. This may be a case where excellence simply comes with too high a price tag.

Celia Hampton

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Vertical angle

The new draft vertical block exemption and vertical restraint guidelines

*by **Claire Purkiss** and **Pat Treacy****

The current vertical block exemption (Regulation 2790/1999) is due to expire in May 2010. Despite the Commission's view that the current regulation and the associated guidelines on vertical restraints (see the Commission's communication N 2000/C 291/01 of 13 October 2000) are working well overall, the Commission appreciates that certain changes in the market should be addressed, including the increased buyer power of big retailers and the growing importance of online and internet sales. The Commission published a consultation on 28 July 2009, inviting comments on proposed revisions to the exemption (the Draft Exemption) and guidelines (the Draft Guidelines). This received numerous responses.

What's new?

In summary, the proposed changes include the following:

- Amending the market share threshold to include both the supplier's and distributor's market shares.
- Narrowing the scope of the exception to one of the hardcore restrictions (article 4(b)).
- Removing the total annual turnover limit for non-reciprocal agreements between competitors (article 2(4)(a)).
- Amending the guidelines to reflect changes in legislation and case law (for example, regarding agency agreements) and to redefine active and passive selling, particularly in relation to internet sales.
- Introducing new guidelines clarifying that the block exemption does not apply to unilateral conduct; explaining when subcontracting agreements may fall within article 101(1); giving examples of exceptions from hardcore restrictions for franchise agreements and the distribution of new brands into a new market; raising the "vertical externality issue" as a positive effect of vertical restraints; stressing the importance of the nature of the agreement and the market position of the customers of the parties in assessing vertical restraints; and regarding upfront access payments and category management agreements.
- Revising the existing guidelines relating to resale price restrictions.

The most significant changes are addressed below.

The increased buyer power of big retailers

Market share threshold

Article 3 has been redrafted to provide that both the supplier and distributor under the agreement must have a market share of less than 30% for the block exemption to apply: "The exemption provided for in article 2 shall apply on condition that the market share held by each of the undertakings party to the agreement does not exceed 30% on any of the relevant markets affected by the agreement". The Commission's intention is to take account of the recent increase in the buyer power of big retailers. However, the consultation responses suggest that this change is thought by many to be unnecessary, problematic and likely to decrease legal certainty.

A particular concern is the lack of any transition period. This could mean that the new situation will impose a considerable burden on significant distributors who will need to review all existing vertical agreements in a short time period, given the imminent expiry of the existing block exemption.

Practically, it will be difficult to establish and monitor on a regular basis (at least annually) the relevant market share of downstream distributors. A supplier may have some view on its own market share, but is unlikely to be well positioned to assess the market share of downstream distributors in their respective markets. Identifying the appropriate markets may, in any event, be difficult given the broad wording: "any of the relevant markets affected by the agreement".

Another concern has been the possibility that assessing such issues would necessitate the exchange of commercially sensitive information. This may contradict existing messages from the Commission, that information exchange between the "hubs" and "spokes" in a series of vertical agreements are of potential concern, and lead to further uncertainty.

Whether the provision will address the Commission's concern is unclear. One example put forward suggests that a distributor's relevant market share may not necessarily reflect buying power (for example, local stores in rural areas). A more general comment relates to the possibility that the extension of the market share criterion may exclude companies unnecessarily from the protection of the exemption.

New guidelines relating to specific vertical restraints

The Draft Guidelines introduce provisions relating to category management agreements and also arrangements whereby upfront access payments are included in vertical agreements. No decided cases apply to such arrangements (which are block exempted up to the 30% market share threshold). However, if the market share threshold is exceeded, the Commission states that competition issues may arise, highlighting particular concerns about increased buyer power.

The Commission suggests that access payments (fees required by distributors to allow suppliers access to their systems) may result in anticompetitive foreclosure of other distributors or suppliers, or collusion between distributors. Positive effects are also discussed, including the prospect that the payments may contribute to the efficient allocation of shelf space and decrease the incentive for suppliers to free-ride on distributors' promotional efforts with poor quality products.

The potential effects on competition of category management agreements are also discussed for the first time, not having been dealt with in the previous guidelines. The Commission points out that to entrust the supplier in a vertical agreement with

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managing the marketing of a category of products (including competitors' products) may result in anticompetitive foreclosure of other suppliers or collusion between suppliers or between distributors and suppliers. However, the guidelines also suggest that such agreements may enable the achievement of economies of scale, increasing customer satisfaction.

Internet sales: passive and active selling definitions

The Commission has addressed the increasing role of internet sales at paragraphs 51-58 of the Draft Guidelines. As previously, the sending of unsolicited emails to certain individuals is regarded as active selling, while simply making a website widely accessible is not considered to be active selling unless it is specifically targeted at certain consumers. These provisions still do not give specific guidance – for example, they fail to explain the circumstances in which a website will be regarded as targeted at certain customers in a territory other than the distributor's exclusive territory. It is felt by some that language should be seen as a key indicator of such targeting, although the guidelines specifically exclude this. Others argue that the Commission should have engaged in more detail with the implications of a market in which global search engines are widely used.

The Commission has given some further examples of hardcore restrictions involving passive selling:

> "–requiring a (exclusive) distributor to prevent customers located in another (exclusive) territory from viewing its website or requiring the distributor to put on its website automatic rerouting of customers to the manufacturer's or other (exclusive) distributors' websites;
>
> "– requiring a (exclusive) distributor to terminate consumers' transactions over the internet once their credit card data reveal an address that is not within the distributor's (exclusive) territory;
>
> " – requiring a distributor to limit the proportion of overall sales made over the internet;
>
> "– requiring a distributor to pay a higher price for products intended to be resold by the distributor online than for products intended to be resold offline".

As far as these examples are concerned, it is worth noting, for example, that a blanket prohibition on rerouting may have detrimental effects. This might be the case where it is necessary to ensure that consumers are provided with the relevant safety information in an appropriate language, or to ensure that a supplier can reroute requests for aftersales care to ensure the desired level of customer service. Notwithstanding the above, the Draft Guidelines do state that an outright ban on internet sales may fall outside the prohibition in article 101(1) as long as it is objectively necessary (eg for health and safety reasons) and does not restrict competition that would take place in its absence.

Imposing particular obligations on dealers who sell using the internet may be a hardcore restriction unless equivalent criteria are applied to shop-based sales. The guidelines provide that the criteria need not be identical but should have the same objectives so as to achieve comparable results. For example, suppliers may require quality standards for the website, for advertising or for promotions as they do for a physical environment. In spite of this guidance, there are issues with applying the equivalency test: online stores are open and accessible 24 hours a day and, given the absence of the limitations inherent in operating from a shop, the range of products supplied may be more extensive online. Commentators have suggested that further guidelines are necessary.

The consultation responses generally welcome the fact that the large online platforms such as eBay or Amazon do not benefit substantially from the changes. Suppliers can still choose to limit the access of such retailers to their products. Suppliers may also require that their distributors have a "bricks and mortar" outlet before engaging in online distribution. Moreover, despite the hardcore restriction on limiting the proportion of overall sales made over the internet, suppliers may be able to require that the distributor sells an absolute amount (in value or volume) offline. The major concern, particularly among luxury brand owners, is that this may result in "alibi shops" opening merely to enable retailers to distribute the product extensively online.

On the other hand, brand owners do not benefit significantly from the proposals. They retain only limited ability to control online sales. It will undoubtedly be argued that the drafts do not adequately acknowledge that there may be legitimate reasons for restricting online sales.

Pricing and territorial protection

The "resale price restrictions" section of the Draft Guidelines has been amended. It now gives greater detail about the likely negative effects of resale price maintenance (RPM), but also acknowledges that there may be benefits. RPM remains a hardcore restriction, but the Draft Guidelines suggest that agreements containing RPM may be candidates for individual exemption under article 101(3) in certain circumstances. Particular examples are given. These include where retail prices are set in the context of a short-term, low-price campaign; or where RPM is used to encourage distributors to increase their promotional efforts to boost product demand when a new brand enters a new market.

In addition to suggesting that suppliers may be permitted to fix the distribution prices of products in a new market for a short period, the Draft Guidelines also give some comfort to distributors ensuring a "genuine entry in the relevant market". Where a new brand or an existing brand is launched on a new market, distributors tend to incur additional costs. The guidelines provide that, in order to recoup such costs, the distributor may enter into an agreement with the supplier which protects the distribution against both active and passive sales into its territory for the first two years. Some aspects of the Draft Guidelines remain unclear on this point. It has been suggested that greater clarity as to the meaning of "new brand" and "new market" would be helpful.

Conclusion

The Draft Exemption and Draft Guidelines have generally been well received. They represent a modest redrafting rather than introducing broad changes to address increased buyer power or redefine internet selling. Despite the broadly favourable response, the proposed changes to the market share threshold have been widely criticised. There is also significant dissatisfaction that, despite the greater clarity in respect of the treatment of internet sales, the proposed amendments are unlikely to address fully the concerns of brand owners.

Supermarkets and suppliers

A look at the new code of practice

by ***Bob Young****

On 4 February this year, a new groceries supply code of practice (GSCOP) came into effect, aimed at regulating relationships between major grocery retailers – effectively supermarkets – and their suppliers. The GSCOP is the brainchild of the Competition Commission and is the direct result of its report on the supply of groceries in the UK, published in April 2008.

The Groceries (Supply Chain Practices) Market Investigation Order 2009, to give it its full legal title, runs to 19 pages, including a code of seven pages and necessary boiler plate of 12. If the GSCOP works – a big if – it could eliminate the worst abuses that supermarkets have inflicted on suppliers for over a decade. Those caught by it are retailers with UK annual grocery turnover of at least £1bn: in alphabetical order, Aldi, Asda, the Co-op, Iceland, Lidl, Marks & Spencer, Morrisons, Sainsbury, Tesco and Waitrose. The CC had calculated that these collectively account for over 80% of all UK grocery sales.

Dos and don'ts

First and foremost, the code requires retailers to work to a principle of fair dealing. It then goes on to specify what retailers must and must not do.

They must:

- include the code in purchase agreements with suppliers;
- record purchase agreements in writing;
- supply information to the OFT when required;
- train staff with respect to the code and appoint a compliance officer; and
- negotiate with suppliers in good faith to resolve disputes.

They must not:

- impose, or put pressure on suppliers to accept, retrospective changes to purchase agreements;
- delay payment;
- require suppliers to contribute to retailers' marketing costs;
- demand payment for wastage or shrinkage that is not the supplier's fault;
- require suppliers to pay fees in order simply to remain suppliers;
- require suppliers to fund promotions or pay fees for particular shelf locations; or
- delist a supplier except for objective commercial reasons.

A successional code

The GSCOP is the successor to an earlier supermarkets code of practice (SCOP) which arose from another CC investigation, Supermarkets, completed in 2000. This inquiry had identified 52 abuses by retailers against suppliers, and the retailers admitted to 42 of them. The SCOP emerged in December 2001 as a potential remedy, to be managed by the OFT. However, opinion soon gathered pace that the SCOP was ineffective because even the largest brand owners feared to complain about and risk retaliation by their largest customers. As one commentator put it, even Heinz was too frightened to spill the beans.

In 2004, the OFT reviewed the effectiveness of the SCOP (OFT paper 697) but said that it could do nothing unless suppliers complained. It did, however, arrange an independent audit, published in March 2005 (OFT paper 783) and concluded that, by and large, the SCOP was working.

Yet supplier dissatisfaction with the SCOP persisted, and by May 2006 the OFT "noted that concerns had been expressed about the code's effectiveness. Those concerns essentially related to the lack of prescriptiveness of the standards in the code, and the apparent reluctance of suppliers to raise complaints under the code, perhaps out of fear of commercial reprisals." (OFT paper 845, p 89)

At that point – though not for that reason – the OFT finally conceded that it should refer the groceries market to the CC.

Courage to complain

Two years later, the CC reported, and now, almost two years after that, the GSCOP has been put into operation. In fact, the timetable is even more protracted than it might look. In its 2000 investigation, the CC had considered abuses going back to 1995. Some of the abuses now addressed by the GSCOP in 2010 have thus been going on for at least 15 years. How is that for an effective competition policy?

The willingness of suppliers to complain about abusive behaviour by supermarkets is no less critical to the success of the GSCOP than it was to the failure of the SCOP. Those who followed the CC's investigation must have noted, in Emerging Thinking (January 2007), explicit references to a climate of fear in suppliers' dealings with supermarkets. These were, in fact, echoes of similar comments made in the CC's 2000 inquiry. Yet when the CC published its provisional findings in October 2007, all references to a climate of fear had simply been airbrushed out. As a matter of process, this is bad. As a matter of substance, it is worse: reflect only that Appendix 9.9 of the CC's report refers to 151 suppliers who had identified 380 objectionable practices by retailers, all of which are excised from the published report on grounds of commercial confidentiality.

So, unless suppliers find new courage to complain, or unless some other process is devised, the new GSCOP is unlikely to be any more effective than the old and discredited SCOP.

Independent ombudsman

What could mark a significant break with what has, conspicuously, not happened over the past 15 years is the prospect that the GSCOP could be enforced by an independent ombudsman. What the CC said (with one member dissenting) was this:

> "…we will seek undertakings from grocery retailers to establish a GSCOP ombudsman to monitor and enforce

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compliance with the GSCOP, and whose functions are to include:
(a) the gathering of information and proactive investigation of retailers' records in areas subject to complaint in order to identify whether breaches of the GSCOP have occurred;
(b) the publication of guidance on specific provisions of the GSCOP where it considers that differences of interpretation exist; and
(c) the publication of an annual report on the operation of the GSCOP." (Final report, Introduction, para 47)

"In addition, we recommend to BERR [now BIS] that if we do not obtain satisfactory undertakings from the retailers creating the GSCOP ombudsman within a reasonable period, it should take the necessary steps to establish the ombudsman. We further recommend that, if this is the case, BERR should take steps to give the ombudsman the power to levy significant financial penalties on the retailers for non-compliance." (ibid, para 49)

Whereas it has the power to create the GSCOP, the CC has no authority to create a new public body. Yet, to its credit, the CC persisted with the ombudsman idea, even in the teeth of supermarket resistance. Its remedies implementation group sought over more than a year to secure the agreement of supermarkets to the creation of an ombudsman, but was unsuccessful – perhaps inevitably so.

Resistance by supermarkets to the appointment of an ombudsman was near-universal. Most opposed the idea of an ombudsman on the grounds that the OFT had already done such a good job in supervising the old SCOP. Thus, objections to needless bureaucracy and cost were voiced, together with their corollary, the need for supermarkets to continue protecting the interests of consumers. See, for example, the responses of Asda, Iceland, Tesco and the British Retail Consortium, all of which can be viewed at: *http://www.competition-commission.org.uk/ulcc-bin/htsearch/?config=COMPCOM2&sort=score&matchesperpage=20&restrict=&words=ombudsman.*

Sainsbury's was more forceful. Its submission to the CC of 27 May 2009 says that "the measures proposed were contrary to general principles of administrative fairness and natural justice…" (Introduction, p1). It objected to the "unnecessary and excessively intrusive" nature of the ombudsman's proposed appointment and the "impractical and unfair nature of the proposed measure to investigate complaints" (Introduction, p2). Sainsbury's also commented on finding the right person for the job: "it would be challenging to find a candidate for the role who meets the criteria set out by the CC, namely sufficient industry knowledge, independence from grocery retailers and suppliers, and the necessary skills and experience to conduct arbitrations." (Appointment and Conflicts, p3)

Waitrose, more emollient in its approach, agreed that an ombudsman would be unlikely to achieve more than the OFT, but said on 28 May 2009 that it would "be willing to give undertakings to create an ombudsman if the other affected retailers were willing to do the same."

Need for reinforcements

But, of course, the others were not willing, and just over two months later, on 6 August 2009, reinforcements had to be called up. The chairman of the CC wrote to Kevin Brennan MP, minister of state at BIS with responsibility for consumer affairs, saying: "The major retailers have refused to offer suitable undertakings so we are recommending that your department should set up the ombudsman, and do so as quickly as practicable."

In principle, BIS supports the idea that the GSCOP needs to be enforced. On 13 January 2010, Kevin Brennan said: "It is not a question of whether a body is needed, but exactly how that body will operate. The next step is to consult formally on its nature and role, to ensure that all interested parties can make their views heard and that informed decisions are made."

The consultation opened on 5 February and is due to close on 30 April, exactly two years after the CC reported. The BIS press release records that "there are differing views on whether government creates a new body or whether this can sit within an existing structure. …we need to consider the regulatory burden that this might impose in developing any policy proposals."

The minister's foreword makes clear that the government may not eventually apply the term ombudsman, since it "may confuse and mislead as to its role". Just so. Although the CC tends to wield the language carefully, here, paradoxically, its intentions are not captured by the OED definition, which describes an ombudsman as someone appointed to investigate complaints about public maladministration, nor by the Collins definition, which adds that an ombudsman is "without power of sanction or mechanism of appeal".

What's needed is a regulator

The right word that dare not speak its name is "regulator". The CC and the government would prefer not to utter it, since the creation of a new regulator would require new primary legislation and would fly in the face of the government's avowed aim – though one honoured more in the breach than in the observance – to reduce the burden of regulation. Yet one might ask why, if the supply of energy to consumers is controlled by an oligopoly of six giant suppliers which are regulated by Ofgem, the supply of groceries to consumers by another oligopoly should not be similarly regulated.

Consistently with that, the British Brands Group, on behalf of suppliers, urged in its submission of 28 May 2009 that the CC should actually stiffen up the wording of its ombudsman proposal, to a point which might be argued as giving him (or her) full-blown regulatory powers:

"The recognition that the ombudsman must be proactive in carrying out investigations even in the absence of a complaint from a named supplier has been fundamentally watered down in the current proposals where investigations may only be carried out on the basis of actual complaints. The ombudsman's ability to launch investigations beyond areas of specific complaint will be crucial…"

There is much still at stake and undecided. Yet the imminence of a general election has now surely frozen action on a groceries "ombudsman", and it may well not be top of the list for whichever party next gains power. So, pro tem, and possibly for longer, the supermarkets win again.

To borrow from Churchill, we are not yet at the beginning of the end; we may only be at the end of the beginning. It's not easy even to see what the end may be.

The *Enron* case

The first follow-on damages claim fails in the CAT

*by **Patrick Boylan** and **Basil Woodd-Walker****

On 21 December 2009, the Competition Appeal Tribunal delivered its judgment in the first follow-on claim for damages to reach trial, nearly seven years after section 47A of the Competition Act 1998 (the Act) made it possible for the CAT to hear such cases. The claim, brought by Enron Coal Services Ltd (Enron) sought damages from English Welsh and Scottish Railways Limited (EWS), the dominant supplier of coal haulage services in the UK at the relevant time. The claim failed as the CAT held that Enron had not proved that it would have secured the contracts (and, hence, the profits) which it claimed that EWS's abusive behaviour had prevented it from obtaining.

Infringement decision by the Office of Rail Regulation

The case arose from a 17 November 2006 decision of the Office of Rail Regulation (ORR) in which it fined EWS £4.1m for abusing its dominant position in the UK market for coal haulage by rail.

One of the ORR's findings related to unlawful price discrimination against Enron, which acted as an intermediary for the purchase of coal for industrial users. In order to provide those services, Enron had to procure coal haulage services from a rail freight provider; EWS was the dominant provider of those services.

The ORR found that between May 2000 and November 2000, EWS quoted Enron higher prices while offering significant reductions direct to Enron's customers, Edison Mission Energy (EME) and British Energy (BE). The ORR held that EWS's selective and discriminatory pricing practices placed Enron at a competitive disadvantage in its contractual negotiations with those customers.

Follow-on damages action

On 7 November 2008, Enron (by then in liquidation) issued a follow-on claim for damages under section 47A of the Act against EWS. Broadly speaking, Enron claimed that EWS:

(1) overcharged Enron in respect of separate contracts to haul coal to three power stations (two owned by EME and one owned by BE); and

(2) prevented Enron from obtaining new or extended business with new or existing customers and/or materially reduced the chance of it obtaining such business.

Strike-out of overcharge claims

In March 2009, following an application by EWS, the CAT exercised its jurisdiction under rule 40 of the CAT Rules 2003 (SI 2003/1372) (the Tribunal Rules) and struck out the claim in respect of the claimed overcharge for haulage to the EME power stations. The ORR found that, in August and October 2000, EWS had offered lower prices to EME than it offered to Enron. However, these prices were in respect of coal haulage services to be provided from January 2001. As Enron had ceased supplying EME in July 2000, there was no basis on which Enron could bring a follow-on claim under section 47A for alleged overcharges in the period from mid 1999 to July 2000.

The Court of Appeal's ruling

The CAT declined to strike out the overcharge claims in respect of the supply to the BE power station. EWS appealed this element of the decision.

EWS accepted that the ORR decision had held that it engaged in selective and discriminatory pricing practices which put Enron at a competitive disadvantage in tendering for new contracts in 2000. However, EWS contended that, properly read, the decision contained no findings that the contract prices charged under the earlier agreements made in 1999 and April 2000 were excessive and amounted to an abuse of its dominant position.

The Court of Appeal made a number of observations. First, it approved the test applied by the CAT to determine whether to reject a claim under rule 40 of the Tribunal Rules. This states that the CAT may reject in whole or in part a claim for damages if it considers that there are no reasonable grounds for making the claim, and is similar to the test for striking out a claim under rule 3.4(2)(a) of the Civil Procedure Rules. Second, and crucially for EWS's application, the court confirmed that the jurisdiction of the Competition Appeal Tribunal in follow-on damages actions is limited to determining the loss which results from a finding of infringement contained in a decision. The existence of such a finding "operates to determine and define the limits of that claim and the Tribunal's jurisdiction in respect of it" (see [2009] EWCA Civ 647 at para 30). Accordingly, it is not open to a claimant to seek to recover damages through section 47A simply by identifying findings of fact which could arguably amount to an infringement. The CAT ought to reject cases where there is no clearly identifiable finding of infringement and where it is, in effect, being asked to make its own judgment as to whether or not an infringement existed (see para 31).

The court therefore held that the CAT had been incorrect to find grounds on which an overcharge claim might arguably be founded. Either the ORR decision contained a finding of an infringement or it did not. The CAT should not have allowed the BE claims to survive merely on the basis that they

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were arguable, but should have decided whether it was clear from the decision that a finding of infringement had been made which covered the pleaded claims. The Court of Appeal held that it did not, and that both overcharge claims should be rejected as bound to fail.

Trial of the remaining issues

Following the Court of Appeal's ruling, the only allegations that remained for trial were that EWS's conduct had deprived Enron of a real or substantial chance of winning a contract to supply coal to one of EME's power stations from 2001 to 2004. On 21 December 2009, the CAT dismissed the remainder of the claim.

As a preliminary matter, Enron submitted that, on the basis of section 58 of the Act, the CAT was bound by all findings of fact made by the ORR in the course of its investigation, and not just those supporting its finding of infringement. Having analysed the relationship between sections 47A and 58, and citing the Court of Appeal judgment, the CAT rejected this argument. The wording of section 47A explicitly precludes section 58 from applying. This is not to say that the CAT disregarded the ORR's findings of fact. It confirmed expressly that it had given due weight to all the regulator's findings. Nevertheless, even if section 58 had applied, the CAT's judgment to dismiss Enron's claims on grounds of causation would not have been affected.

The CAT then considered whether the alleged loss had been caused by the abuse of dominance established by the ORR. Two issues arose. Enron had to show, on the balance of probabilities, that:

(1) but for the abuse, it would have submitted a bid to EME on the basis of terms agreed with EWS, and would then have sought to negotiate a four-year contract for the supply of coal; and
(2) but for the abuse, there was a real or substantial chance that negotiations between Enron and EME would have led to EME awarding Enron a four-year contract for the supply of coal.

Essentially, the CAT had to consider whether Enron would have won the EME tender, even if EWS had not discriminated against it.

The CAT concluded that Enron would not have been successful even if had been offered non-discriminatory haulage rates from EWS. There was evidence of a history of commercial difficulties between Enron and EME, and on key points, Enron's bid did not offer the level of service that EME sought.

Enron argued that its previous dealings with EME should not be considered in deciding whether a contract would have been concluded "but for" EWS's abuse. In its view, the question was whether a rational economic operator, not allowing previous commercial dealings to cloud its judgment, and looking for best value, would have contracted with it. The CAT rejected this argument. It emphasised the subjective nature of the but-for test: would the third party in question standing in its own shoes have concluded a contract but for the abuse? The only element which should be purged from the but-for analysis is the abuse itself.

The CAT further decided that Enron had not shown that if it had been successful in its bid to provide coal haulage, it was more likely than not that it would have sought to negotiate a more comprehensive supply of coal contract. The CAT, therefore, concluded that Enron had failed to prove that EWS's abuse of its dominant position had caused Enron to lose that contract.

Conclusion: the problems with causation and the appeal of the High Court

The CAT emphasised that it was following established principles in assessing the issue of causation and loss. The case therefore provides a salutary warning to claimants in competition damages actions about the importance of being able to show that the loss claimed has actually been suffered and, if so, was caused by the defendant's infringing behaviour. As ever in litigation, a finding of liability is only of use if a claimant can actually prove that it has suffered loss as a result.

The CAT was at pains to point out that it was aware that this was the first follow-on damages claim to reach it and would therefore be scrutinised for indicators of the CAT's approach to follow-on damages. It stressed that each case was to be judged on its particular facts and observers should therefore not make general assumptions on the basis of the outcome of this particular case. That may be true. However, the CAT was right to be concerned about the impact of this case, as there are aspects of the various judgments which will impact on the decisions of future claimants about the best forum in which to bring a damages action.

There are two issues in particular:

(1) the Court of Appeal's restrictive interpretation of the CAT's jurisdiction to hear follow-on claims; and
(2) the CAT's own restrictive interpretation of section 58 of the Act and its ruling that findings of fact from relevant regulatory decisions are binding on the High Court but not on the CAT.

Taken together, these two rulings provide another incentive for claimants to choose the High Court over the CAT as the claimant can use those binding conclusions of fact to build a case in the High Court to establish an infringement.

They are not the only incentives. The requirement, when an appeal is pending from a relevant regulator's decision, for permission to start follow-on proceedings before the CAT is in contrast to the position in the High Court where no such permission is required and where the court has been prepared, as in *National Grid* [2009] EWHC 1326 (Ch) for instance, to press ahead with pretrial steps pending the outcome of any appeals. This has led many claimants in cartel damages actions to prefer the High Court over the CAT as a forum in which to bring their claims. While the restrictive approach of the Court of Appeal and the CAT to the CAT's jurisdiction may have been correct, the outcome of this case is likely to reinforce that trend and may lead to the High Court becoming the forum of choice for follow-on claims. That cannot have been the legislators' desired outcome when establishing the CAT as a specialised tribunal to hear competition-related claims. Section 16 of the Enterprise Act allows for the introduction of regulations which would enable competition cases to be transferred to the CAT by the High Court. Perhaps now is the time for such regulations to be introduced.

Connecting flights

An analysis of granting antitrust immunity to the Oneworld alliance

*by **Nelson Jung** and **Russell Hunter****

On 13 February, the US Department of Transportation (DoT) said it intended to grant antitrust immunity to a group of airlines in the Oneworld alliance (American Airlines (AA), British Airways (BA), Iberia, Finnair and Royal Jordanian Airlines).

In the DoT's view, the proposal for enhanced co-operation would provide passengers and shippers with a range of benefits including lower fares on more routes, improved services and schedules and reduced travel and connection times, while also enhancing competition with the other airline alliances, Star Alliance and SkyTeam (each already having been granted antitrust immunity). The applicant airlines propose to resolve concerns raised by the DoT through the divestment of four slots at London Heathrow's airport to facilitate the development of new US-Heathrow services.

Background

In August 2008, AA, BA and Iberia announced plans to extend their global co-operation within the Oneworld alliance and to enter into joint business agreements regarding transatlantic flights. These agreements envisage the airlines jointly pricing, managing capacity, co-ordinating schedules and sharing revenue on certain routes, as well as linking their frequent-flyer programmes. In addition, they would also enhance their global co-operation with existing Oneworld partners, Finnair and Royal Jordanian Airlines.

The Oneworld alliance stated that its proposals will result in greater choice and more convenient schedules for customers by improving connections between international flights. The increased co-operation between Oneworld members is also intended to allow the Oneworld alliance to compete more effectively with rival alliances SkyTeam and Star Alliance, which have already been granted antitrust immunity by the DoT, albeit with certain carve-outs in relation to Star Alliance.

As the enhanced co-operation agreements (ECAs) were announced, the airlines filed for worldwide antitrust immunity from the DoT. In parallel, the European Commission is reviewing the ECAs in the context of formal proceedings under article 101 of the treaty on the functioning of the EU (TFEU) (ex article 81 EC), which it opened in April 2009.

Enhanced co-operation in the airline industry

Alliances are increasingly common in the aviation sector, as airlines seek to respond to ever-greater competition and the need for greater efficiencies. Historically, one of the most complex issues in setting up an alliance has been co-operation on transatlantic routes, mainly due to international (typically bilateral) air services agreements limiting traffic rights to provide cross-border services. Nationality clauses in such agreements restrict foreign ownership in airlines. This has prompted airlines to engage in ECAs that fall short of full mergers.

AA and BA have unsuccessfully sought antitrust immunity from the DoT twice before. The first approach, in 1997, failed due to a lack of progress in negotiations between the US and the EU aimed at liberalising the international (transatlantic) aviation market. A second attempt in 2001 was abandoned by the airlines as they were unwilling to accept onerous conditions proposed by the DoT, specifically the transfer to competitors of 224 weekly slots, or 16 daily city-pairs, at Heathrow airport in order to address the DoT's competition concerns.

The DoT's proposal to grant antitrust immunity

When the DoT issued a show-cause order granting preliminary antitrust immunity to the Oneworld alliance agreements on 13 February this year, this was described as a "kick in the teeth" to non-aligned carriers by the president of Virgin Atlantic Airlines, Richard Branson. However, the DoT considered that the likely public benefits flowing from the alliance outweighed any possible anticompetitive effects.

The US Department of Justice (DoJ) had suggested that the DoT impose slot divestures or carve-outs on certain routes to protect the public interest. The DoT rejected the DoJ's recommendation that certain routes be carved-out of the Oneworld alliance antitrust immunity. Instead, in order to address competition concerns on six transatlantic routes, the DoT required AA and BA to make available four daily slots at London Heathrow to competitors. Interested parties were given until 31 March to file objections to the DoT's show-cause order, following which the applicant airlines have 15 days to respond.

The preliminary antitrust immunity granted to the Oneworld alliance largely mirrors the immunities granted to SkyTeam and Star Alliance (in May 2008 and July 2009 respectively). However, in its latest decision, the DoT opted for slot divestments as the appropriate remedy for concerns identified on specific routes, in contrast to its decision to carve-out certain routes from the antitrust immunity granted for Continental Airlines to join Star Alliance in 2009.

Parallel review by European Commission

In addition to the DoT's review, the enhanced Oneworld alliance co-operation is the subject of parallel antitrust proceedings under article 101 TFEU by the Commission.

The Commission opened formal proceedings against AA, BA and Iberia in April 2009 and, in September 2009, sent a statement of objections to the parties. On 1 February this year, it announced that it was considering commitments under article 9 of Regulation 1/2003 offered by the parties. More specifically, the parties offered to make available slots at London Heathrow or London Gatwick airports on routes to Boston, New York, Dallas and Miami. On the London – New York city-pair, the parties also proposed to provide a competitor

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with operating authorisation at New York JFK airport. In addition, British Airways, American Airlines and Iberia undertook to provide access to their frequent flyer programmes on the relevant routes, allowing passengers of the qualified new entrants to accrue and redeem miles on the parties' frequent flyer programmes.

The parties also proposed to allow fare combinability and offer special prorated agreements regarding the routes of concern, which would enable competitors to offer tickets on the parties' flights and facilitate access to connecting traffic. Finally, the parties committed to submit data regularly concerning their co-operation, which would facilitate an evaluation of the alliance's impact on the markets over time. According to the Commission's press release, a trustee would be appointed to monitor the implementation of the proposed commitments.

On 10 March, the Commission announced that it was market testing these proposed commitments, meaning that interested parties now have until 10 April to submit their comments. Subject to any comments received, the Commission may then make the commitments legally binding under article 9 of Regulation 1/2003.

Comment

One of the striking features of the DoT's announced intention to grant antitrust immunity in this case is that the proposed remedy package is significantly less onerous than the proposal under consideration during the 2001 Oneworld alliance review. The DoT cited the open skies air services agreement entered into between the US and the EU in 2007 as a reason behind this relaxation. The open skies air services agreement lifted restrictions on transatlantic flights and opened access to Heathrow, from which previously only two US airlines and two UK airlines had been able to operate transatlantic services, thereby apparently removing much of the DoT's opposition to the proposed co-operation. It should also be noted that the EU and the US are currently negotiating a second-stage open skies air services agreement, which may improve choice for customers by further opening market access. The second-stage open skies air services agreement may also facilitate ownership of EU and US airlines by each other's investors.

In the light of these developments – and given the efforts to secure deeper regulatory transatlantic co-operation on a broad range of issues, including competition enforcement – it may not come as a big surprise that regulators on both sides of the Atlantic appear to be increasingly willing to ensure that any remedies required in the context of antitrust enforcement in the aviation industry are compatible and dovetail with each other. The timing of the DoT's and the Commission's latest positive signals regarding the Oneworld alliance and the current stage of open skies negotiations may or may not be coincidental. It is noteworthy, however, that the Commission announced that it was market-testing the commitments proposed by BA, AA and Iberia just one day before the EU transport commissioner Siim Kallas was to present the current state of play on the open skies negotiations to EU transport ministers at the meeting of the EU transport council on 11 March.

The reviews by the DoT and the Commission are being conducted against the background of a wave of consolidation in the airline sector. It is in this context that the Commission has sent a clear message that pre-existing co-operation arrangements between the relevant parties will not necessarily exempt further integration measures from a high degree of regulatory scrutiny, as was recently observed in the Commission's review of Lufthansa/Austrian Airlines and Lufthansa/Brussels Airlines. In those merger clearance decisions, the Commission considered slot divestments were necessary to allay competition concerns similar to those identified in relation to the Oneworld alliance.

(In response to the parties' submission in Lufthansa/Austrian Airlines that, as a result of their co-operation, they could not be considered as competitors, the Commission said that "this does not automatically mean that the proposed transaction cannot lead to a significant impediment to effective competition. Indeed, where extensive premerger co-operation has been replaced by a permanent structural link, the Commission has analysed the specific effects of the creation of that permanent structural link on a route by route basis (in particular on hub-to-hub routes) in order to assess the extent to which competition may be affected post-merger.")

The Commission's Oneworld review also serves as a reminder that, in the EU, by offering commitments under article 9 of Regulation 1/2003, the parties to a co-operation agreement may effectively reach a resolution which is reminiscent of the old notification procedure under Regulation 17/62 that was abolished as part of the modernisation of EU competition law in 2004. Although the article 9 commitment mechanism is not intended to operate as a backdoor approval process, it does in practice allow the Commission to consider the parties' arguments as to why their proposed co-operation does not give rise to competition concerns under article 101 TFEU once the parties put forward commitment proposals on a voluntary basis.

From the Commission's perspective, this mechanism allows for an investigation to be closed without necessarily having to undergo the lengthy and tedious process of issuing a statement of objections, let alone an infringement decision. In its recently published *Best Practices on the conduct of proceedings concerning Articles 101 and 102 TFEU*, the Commission "encourages undertakings to signal at the earliest possible stage their interest in discussing commitments" to explore the Commission's readiness to dispose of the case by means of a commitment decision. The Commission emphasises that "the main advantages of commitment decisions are a swifter change on the market to the benefit of consumers as well as lower administrative costs for the Commission" and that "faster proceedings and the absence of a finding of an infringement may be attractive". It remains to be seen to what extent the article 9 mechanism will serve as a tool to pave the way for swifter enhanced co-operation in the airline industry.

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A duty to co-operate?

The US Federal Trade Commission is trying to expand a monopolist's duty to deal with rivals

*by **Thomas F Bush****

One year into the Obama administration, US antitrust authorities are beginning to implement their stated plans to reinvigorate antitrust enforcement. The Federal Trade Commission took a significant step in December 2009, with an administrative complaint charging Intel Corporation with several forms of anticompetitive conduct designed to protect and extend a monopoly over microchips. Much of the commentary about the complaint has focused on allegations of Intel's use of loyalty discounts and bundled discounts.

The complaint also charges Intel with unlawful conduct by impairing the interoperability between its chips and complementary products manufactured by competitors. "Intel had a duty to deal and co-operate with its competitors," claims the FTC, "to enhance competition and innovation for the benefit of consumers" (para 21). By this allegation, the FTC appears to be challenging the position of the Supreme Court that a monopolist generally has no obligation to deal with, or co-operate with, its rivals. If the FTC prevails on this part of its complaint, the case could mark a significant change in the direction of the development of US antitrust laws.

The Federal Trade Commission's complaint against Intel Corporation

Intel is the world's leading manufacturer of central processing units (CPUs), which process data and control other components of personal computers and servers. With a market share in excess of 70% over the last decade, Intel possesses, according to the FTC's complaint, monopoly power for CPUs. Intel also manufacturers graphic processing units (GPUs), which process computer graphics. Intel holds a large share of the GPU market but not a monopoly. The FTC alleges that with technical advancements developed primarily by Intel's rivals, GPUs have started to duplicate many of the functions of CPUs, and Intel fears that further advancements by rival GPU manufacturers will erode the Intel monopoly in CPUs.

To ward off this threat to its current monopoly, and to attempt to achieve a new monopoly in GPUs, the FTC contends that Intel has, among other measures, adopted several tactics to deny or impair the ability of its rivals' GPUs to interoperate with Intel's CPU. Interoperability is essential for the GPU to function. Without it, the competitiveness of rival GPU manufacturers is severely undermined.

The FTC's position is that Intel had a duty to co-operate with the rival GPU manufacturers to facilitate the interoperability of their products. That duty arose, according to the complaint, from Intel's prior conduct: it had encouraged rivals to rely on its co-operation and represented to them that co-operation on interoperability would continue. Intel benefited from this conduct, because advancements in GPU technology, led by its rivals, had increased the demand for personal computers and hence for Intel's CPUs. Having nurtured the growth of these independent GPU manufacturers for its own benefit, Intel may not, says the Federal Trade Commission, turn on them once they develop into a serious competitive threat.

The *Trinko* precedent

This part of the FTC's complaint immediately recalls *V Trinko LLP* 540 US 398 (2004). Trinko was a private action charging the incumbent telephone company in the state of New York with monopolisation, in violation of section 2 of the Sherman Antitrust Act, 15 USC section 2, for its refusal to allow rival telephone companies to interconnect with its local telephone exchanges. The telephone interconnections in *Trinko* are very similar to the interoperability involved in Intel: in both cases, the alleged monopolist denies rivals access to its own services and facilities, with the effect that the rivals are less able to compete.

In *Trinko*, the Supreme Court found no Sherman Act violation, explaining that a monopolist generally has "no duty to aid competitors". Like any other business, a monopolist has the right to refuse to do business with anyone. The Court explained (id at 407-08):

> "Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing – a role for which they are ill-suited."

The Court in *Trinko* acknowledged that under "certain circumstances, a refusal to co-operate with rivals can constitute anticompetitive conduct" but added that it had been "very cautious" in recognising exceptions to the rule that monopolists have no duty to aid or deal with competitors (id at 408).

The Federal Trade Commission's Intel complaint hardly reflects caution. It recognises a duty to co-operate in circumstances that arise commonly. Manufacturers of electronic hardware frequently encourage independent firms to develop compatible accessories and software, hoping that the spread of new accessories and software will increase the demand for their primary hardware product. The recent

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proliferation of apps for smartphones is an example. For similar reasons, manufacturers of durable goods, like photocopiers, often encourage independent firms to provide spare parts and maintenance services for their products. The FTC's theory is that these activities can lay the foundation for holding the manufacturer to a duty to continue to co-operate with the independent firms after those firms develop into competitive rivals.

If that theory prevails, the duty to co-operate will have grown far beyond the exceptional cases that the Supreme Court envisioned in *Trinko*. The FTC is seeking to hold a monopolist to a duty to co-operate in circumstances where the Supreme Court almost certainly would decline to find the same duty.

Unfair methods of competition and section 5 of the Federal Trade Commission Act

As the highest court in the federal system, the Supreme Court has the final word on the meaning of federal statutes like the Sherman Antitrust Act. The Federal Trade Commission has no authority to apply the Sherman Act in a manner inconsistent with the Court's holding in *Trinko*. To assert this broad duty to co-operate in the Intel complaint, the Commission seeks to establish not a violation of the Sherman Act but of section 5 of the Federal Trade Commission Act, which authorises the Commission to prevent companies and individuals from "using unfair methods of competition" (see 15 USC section 45).

The distinction between these statutory provisions usually is not significant. In most FTC cases, the conduct that the FTC alleges to violate section 5 also would violate the Sherman Act, or one of the other antitrust statutes. In these cases, the Federal Trade Commission takes the position that any conduct violating one of the federal antitrust statutes is an "unfair method of competition," and in finding a violation of an antitrust statute, the FTC follows the interpretations of the antitrust statutes given by the Supreme Court and the Courts of Appeals.

However, the Commission has the authority to enforce section 5 against conduct that does not violate the antitrust statutes. In determining whether particular conduct is an "unfair method of competition", it may consider "public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws" (see *FTC v Sperry & Hutchison Co* 405 US 233, 244 (1972)). The Commission uses this authority very sparingly, but it plainly is attempting to exercise it with the Intel complaint.

This reliance on a broad reading of section 5 means that the outcome of the Intel proceedings will have a limited impact. Only the FTC has the authority to enforce section 5, and the FTC's only remedy for a violation is an administrative order to "cease and desist" the conduct found to be an unfair method of competition. No private rights of action are available for section 5 violations.

Consequently, Intel is not facing a risk that its competitors or customers will sue for treble damages for its alleged failure to co-operate with rival GPU manufacturers. Treble damages are available only for violations of the Sherman Act, or other antitrust statutes.

Will the alleged duty to co-operate survive?

The FTC has not yet ruled that Intel Corporation has a duty to deal and co-operate with the GPU manufacturers. The only official action by the Commission so far is to authorise the issuance of the complaint, which requires only that it has "reason to believe" that Intel has violated section 5.

Intel has answered the complaint and has specifically denied that it sought to impair the interoperability of rivals' GPUs. Intel also challenges the notion that it can be held to a duty to co-operate with its competitors. "The complaint seeks to turn Intel into a public utility," the answer asserts, adding that "the Commission has unfortunately declared that it is prepared to become a central planner of the microprocessor industry and related industries."

With the battle lines drawn, the case now proceeds to discovery and hearing. Under the current schedule, the Commission will issue its final decision in 2011, before August. In that final decision, the Commission can either affirm or reject its new theory of a monopolist's duty to co-operate.

Intel has the right to seek judicial review of any adverse Commission ruling. Notwithstanding the Commission's supposedly broad discretion to define "unfair methods of competition", the courts have subjected these cases to very close scrutiny, concerned that the Commission may be acting arbitrarily when it adopts an overly innovative concept of unfair competition and that businesses may be unable to determine when their practices cross the line of illegality.

In one prominent case – *Official Airline Guides Inc v FTC* 630 F 2d 920 (2d Cir 1980) – the court vacated a Commission finding that a monopoly publisher of airline schedules had violated section 5 by refusing to publish the connections of commuter airlines. The court cited the principle that a monopolist generally has the right to choose not to do business with another company, the same principle that would later be at the heart of the *Trinko* decision and that Intel now is asserting in its defence. The Commission could not deprive the publisher of its right to refuse to do business with the commuter airlines, the court held, without substantial evidence that the refusal serves to enhance or protect the publisher's own monopoly.

The Commission will likely face the same challenge in the event that it finds that Intel Corporation has breached a duty to co-operate with GPU manufacturers on interoperability. A court will look for substantial evidence that Intel's conduct had the purpose or effect of protecting an Intel monopoly in CPUs or of gaining Intel a monopoly in GPUs.

Hence, the duty to co-operate alleged in the Intel complaint might not survive in the long run. For the present, however, the FTC has made its position clear. Any company holding shares of markets in the United States large enough to support an arguable finding of a monopoly, or close to a monopoly, should examine the history of its dealings with competitors and potential competitors. If the history is that the company has encouraged its competitors to rely on its co-operation and support, then it might have assumed, in the eyes of the FTC, a duty to continue that support, and it faces a risk that a breach of that duty would lead to an investigation by the FTC and an enforcement action for violation of section 5 of the FTC Act.

Bringing Google to book

The proposed settlement leaves big unanswered questions

*by **David Wood****

The proposed Google book settlement raises so many legal issues that it is almost too difficult to know where to begin.

In no particular order, these include: the appropriateness of class actions to solve regulatory problems; the legitimate scope of class action settlements; the reversal of the longstanding principle of prior consent in IP law; the applicability of international IP treaties to court-backed settlements; the court-sanctioned creation of a digital library monopoly; price-fixing for digital distribution of works; and, last but not least, the impact of all this on online search and search advertising. On top of these legal issues, there are significant questions about access to knowledge, preservation of cultural patrimony and how to measure the impact of agreements relating to the worldwide web even in geographical areas where they do not formally apply.

This article focuses on two of these issues: the competition law implications of the proposed settlement and the nature of its effects in Europe and the rest of the world.

The first proposed settlement

Google began digitising books in 2004 and, since then, has scanned millions of works without obtaining licences from the relevant rights holders. These works provide the vast majority of content that is copied, indexed and offered online through Google book search.

In September 2005, a group of authors filed a US class-action copyright infringement lawsuit against Google for its book search service, and related litigation was also brought by a group of US publishers: *The Authors Guild Inc v Google Inc* Case No 05 CV 8137 (SDNY); *The McGraw-Hill Companies Inc, Pearson Education Inc, Penguin Group (USA) Inc, Simon & Schuster Inc* and *John Wiley & Sons Inc v Google Inc* Case No 05 CV 8881 (SDNY).

Fast forwarding to October 2008, a negotiated settlement was announced, subject to approval by the US District Court for the Southern District of New York.

In broad terms, the proposed settlement would have enabled Google to digitise virtually any book protected by a US copyright - including effectively every in-copyright book published in Europe (since these books are protected by US copyright law pursuant to various international treaties) – unless the relevant rights holder positively and formally opted out of the proposed settlement. Included within the scope of the settlement were "orphan works" – that is to say, works that are within their term of copyright protection but whose rights holder cannot be located.

The proposed settlement would also have granted Google the right to sell online access to these digitised works, as well as to analyse them to produce indices and to improve its internet search and search advertising algorithms. It would also have helped Google to develop new services such as language-based tools, including automatic translation services.

Department of Justice's response

The court was due to hold what is known as "a fairness hearing" in October 2009. Many third parties submitted observations in one form or another to the court. These included not only civil parties (such as authors and publishers), rivals to Google in the online world (such as Microsoft and Amazon) and industry associations (such as the Open Book Alliance) but also the US Department of Justice (DoJ) and the French and German governments. These submissions and other source materials have been helpfully gathered at *http://thepublicindex.org/*.

Unsurprisingly, the DoJ's submission provoked the most interest and had the greatest impact. It was surprisingly hard-hitting. The DoJ's statement of interest on the proposed settlement made the preliminary point that the settlement sought to resolve "matter[s] of public, not merely private, concern" that are "typically the kind of policy change implemented through legislation, not through a private judicial settlement". Further, the DoJ also concluded that the proposed settlement raised at least two "serious" competition issues.

First, the settlement would "grant Google de facto exclusive rights for the digital distribution of orphan works" and "create a dangerous probability that only Google would have the ability to market ... a comprehensive digital book subscription". This "is precisely the kind of competitive effect the Sherman Act is designed to address".

Second, the settlement appeared to restrict price competition by: (1) creating an industry-wide revenue-sharing formula at wholesale level applicable to all works; (2) setting default prices and prohibiting discounts at the retail level; and (3) placing control over the pricing of orphan works with publishers and authors whose books might compete with these orphan works. The DoJ noted that the settlement "bear[s] an uncomfortably close resemblance to the kinds of horizontal agreements found to be quintessential per se violations" of US antitrust law.

Shortly after the DoJ filed its statement, the plaintiffs filed a motion asking to delay the fairness hearing on the ground that the parties were seeking to revise the settlement to take account of the DoJ's concerns.

Revised settlement

On 13 November 2009, the parties filed a revised settlement proposal (perhaps inevitably tagged "version 2.0"). The key changes were that the revised proposed settlement would only include books that were either registered with the US Copyright Office or published in the UK, Australia, or Canada – in other words, the majority of non-English works were excluded unless they had been registered with the US Copyright Office. Other changes included increased possibilities for the commercialisation of works covered by the provision

(Continued on p15)

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(Continued from p13)
settlement through distribution channels other than Google (such as Amazon and Barnes & Noble) and the removal of the "most-favoured nation" provision whereby third parties could not be offered licensing terms which were better than those available to Google under the settlement.

As with the first version of the proposed settlement, many third parties submitted their observations on version 2.0 to the court. The DoJ repeated its earlier concerns that a class action procedure was the wrong way to decide such important issues and noted that:

- The proposed settlement would "confer significant and possibly anticompetitive advantages on a single entity – Google".
- In relation to the pricing mechanism, "it is unlawful for competitors to agree with one another to delegate to a common agent pricing authority for all of their wares".
- "There is no serious contention that Google's competitors are likely to obtain comparable rights independently".
- "Google already holds a relatively dominant market share in [the search] market. That dominance may be further entrenched by its exclusive access to content through the [proposed settlement]. Content that can be discovered by only one search engine offers that search engine at least some protection from competition. This outcome has not been achieved by a technological advance in search or by operation of normal market forces; rather, it is the direct product of scanning millions of books without the copyright holders' consent and then using [a class action procedure] to achieve results not otherwise obtainable in the market."

From various public and private statements made by European Commission officials, it is understood that while DG Competition has been watching this process with interest, it has not received any formal complaints, and has reservations about the impact in the Community of an arrangement which (at one level, at least) purports to be restricted to a US audience.

Nevertheless, the concerns raised by the DoJ clearly strike a chord with competition lawyers in Europe. Even if we have no direct equivalent of the "monopolisation" infringement, we do have extensive recent case law relating to leveraging of market power. We also have rules on price-fixing that are every bit as clear as those in the US.

Extraterritorial effects of settlement

In terms of effects, a number of reasons have been put forward as to why it is likely that effects of the proposed settlement would be felt outside the US.

First, although the revised settlement purports to exclude most European books, it would in fact allow Google to scan and profit from large numbers of European and other non-US books. For instance, the revised settlement would expressly apply to all books first published in the UK (and in Canada and Australia). Moreover, it would apply to all works first published elsewhere in Europe (and the world) if those books were at any time registered with the US Copyright Office.

Second, the revised settlement would continue to give Google a de facto monopoly over access to orphan works.

Third, the revised settlement does not prevent Google from continuing unauthorised copying and "snippet display" of European works that fall outside its scope. This means that European rights holders who are now excluded from the settlement would still face unauthorised copying of their works by Google.

Fourth, Google's position as gatekeeper to online access to books for US readers would give it an unparalleled degree of influence over the terms of access for European readers. Its control over the only comprehensive digitised library would give Google massive influence over Europe's development of digitised libraries, in terms of the amounts earned by authors and publishers, charges to consumers and other users, and the types of products and services on offer.

Finally, by enabling Google alone to offer the capability to search millions of books, the proposed settlement would have a major impact on search and search advertising markets, where Google has market shares significantly above 60% in Europe. Even if a rights holder instructed Google not to commercialise a particular book, the proposed settlement would allow Google to digitise the book, include it in its books database, and conduct research on this database – to the benefit of its search and search advertising offerings, among other things. As the proposed settlement specifically prohibits research on the database by any service that competes with Google, there is the clear risk that the revised settlement would stifle innovation and harm the internet. As a representative of Google said about the proposed settlement at a European Commission hearing held in September 2009, "it really is about the cloud" (ie internet-based computing where software, information and services are accessible anywhere on any computer).

Conclusions

It is tempting to be carried away by the prospect of greater access to knowledge and the almost supernatural promise that the proposed settlement would "breathe life into dead books". However, these benefits need to be weighed against the costs.

For IP rights as well as the implications for European cultural patrimony, this balance can only be found through the legislative process at EU or member state level. For the competition law issues, Europe has a tried and tested body of laws that are both flexible and at the same time reasonably clear and predictable.

In the light of the continued objections from around the world, there is a likelihood that version 2.0 of the proposed settlement will be replaced by version 3.0 in the coming months. It is difficult to predict the ways in which the two will differ. It has been rumoured that the parties are considering giving authors and publishers an opt-in rather than requiring them to opt-out. In the meantime, the European Commission is working on preparing legislation for orphan works that would deal with the recognised problem of being unable to obtain consent from rights holders who cannot be identified.

These changes – if they become reality – will clearly need careful consideration, not least as to how they will affect the competitive situation in the US, in Europe and elsewhere. However, it seems clear that unless there are also other changes – such as giving third parties access to the copies authorised under the proposed settlement on fair, reasonable and non-discriminatory terms – possibly insurmountable competition concerns will remain.

Ofcom decisions on pay-TV

After a three-year inquiry into the UK market for pay-TV, Ofcom has announced three decisions.

First, the broadcaster British Sky Broadcasting has been told that it must offer to supply its channels Sky Sports 1 and Sky Sports 2 to other retailers, so that the programmes on these channels can be made available on cable and terrestrial television. The wholesale price of this sale will be set by Ofcom.

Second, Ofcom has approved Sky and Arqiva's request to offer pay-TV services on digital terrestrial TV. But this approval is conditional on the deal on Sky Sports 1 and 2 going through. In addition, if Sky decides to offer movie channels on digital terrestrial TV, then those channels must also be offered to other digital terrestrial TV operators.

Third, the UK's communications regulator says that it is going to open a consultation about the possibility of making a reference to the Competition Commission on the subject of movies on TV. It is concerned about the sale and distribution of subscription video-on-demand premium movie rights.

Ofcom says that Sky has, for many years, held exclusive rights to broadcast a large number of popular sports events and also the first run of Hollywood movies. It believes that Sky is currently exploiting its power by limiting the wholesale distribution of its premium channels and that this has the effect of restricting competition from retailers using other platforms.

Sky immediately announced it will appeal Ofcom's decision.

RBS fined £28.5m

Following an investigation by the UK's Office of Fair Trading, the Royal Bank of Scotland has agreed to pay a penalty of £28.59m for giving information about prices to one of its competitor banks.

RBS admitted breaches of competition law between October 2007 and February or March 2008, when various members of its professional practices coverage team gave confidential information about future pricing to their counterparts at Barclays Bank. The OFT found evidence that the information was taken into account by Barclays in fixing its prices.

The OFT investigation followed a tip-off from Barclays. Under the OFT's leniency policy, Barclays is immune from penalties because it was the first to report its participation in the infringement. And RBS's admission and co-operation meant that its fine was reduced from an initial figure of £33.6m.

Ali Nikpay, OFT senior director of cartels and criminal enforcement, said: "This case highlights the strong benefits of acting promptly to report anticompetitive conduct to the OFT and of co-operating with such investigations".

RBS staff had made the disclosures to Barclays in a number of ways – by phone, at social events, at meetings with clients and at gatherings of the industry as a whole. They gave information about the pricing of loan products to large firms providing professional services, such as firms of solicitors, accountants or estate agents. RBS and Barclays are the main providers of these products for this type of firm. The information given included specific details of the price of two proposed loan facilities, as well as disclosures on future pricing in general.

Consent order on US funeral services

The US Federal Trade Commission (FTC) has proposed a consent order which allows the country's largest funeral provider to acquire the fifth largest – on condition that it sells off a number of its services and assets.

Service Corporation International (SCI) will be allowed to go ahead with its acquisition of Keystone North America Inc so long as it sells 22 funeral homes and four cemeteries. If SCI follows this consent order, the FTC will not treat the takeover as anticompetitive.

The undertakers and cemeteries concerned are situated across the US. In each of the geographical areas, the markets are highly concentrated, and SCI's acquisition of Keystone, as originally proposed, would have eliminated the intense head-to-head competition between these two firms.

Buyers must be approved by the FTC and the sales must take place within 90 days. The FTC order also requires SCI to sell related equipment, customer and supply contracts, and other assets such as trade names and property.

The order contains several provisions to ensure the future success of the businesses:

- the FTC will evaluate all proposed buyers to make sure that they will be able to compete effectively after SCI takes over Keystone;
- if there is no sale within 90 days, the FTC will appoint a trustee to sell the assets;
- SCI must provide transitional services to the buyers so that there is a smooth handover of ownership, with continued operation of the services;
- SCI must allow all their current managers to work for the new owners; and
- SCI must make sure that all the services continue to be viable throughout the process.

The FTC consent order will be subject to public comment until 26 April, after which the Commission will decide whether or not to make it final.

Music in New Zealand

National music copyright rules have changed following a Commerce Commission investigation.

The investigation, which was launched last year, followed a complaint about royalty agreements between music copyright owners and Phonographic Performance NZ Ltd (PPNZ). These agreements were said to be exclusive, so that people who wanted to buy licences for copyrighted music had to deal via PPNZ. This stopped them from negotiating on price directly with the copyright owners.

There were, the Commission said, serious competition concerns about this arrangement. So PPNZ and the four major recording companies in New Zealand (Sony, Warner, EMI and Universal) have now agreed to treat their royalty agreements as non-exclusive. This will allow buyers to negotiate directly with the four companies. It will also open up about 70% of the market to competitive negotiation.

In addition, the recording companies have published protocols outlining their direct dealing policies.