

Michael Albers
Head of Unit
Abuse of Dominance Review
Antitrust Policy and strategic support
Directorate-General for Competition
B-1049 Brussels

Brussels, 14 April 2006

Dear Mr. Albers,

RE: DG Competition Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses.

Please find here attached ECCA's comments on the Commission Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses.

I would like to thank you for having provided us this extended deadline for submission.

Yours faithfully,

Caroline Van Weede
Managing Director
European Cable Communications Association (ECCA)



European
Cable
Communications
Association

ECCA 4731

ECCA's Response to the Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses

I. INTRODUCTION

The European Cable Communications Association (ECCA) is an association of cable operators and their national associations active in Europe. Its main objective is to foster co-operation between cable operators and to promote and represent their interests at European and international level. ECCA members currently serve more than 55 million subscribers.

ECCA members own and operate cable broadband distribution networks across much of western and central Europe, and in Scandinavia. Our breadth of geographic coverage and experience in providing a full range of video, telephony and broadband internet retail products based on privately financed and operated Hybrid-fibre-coaxial (HFC) cable networks gives the cable industry an informed perspective on the issues associated with public support for broadband access infrastructure.

ECCA members welcome the Commission's efforts to promote competition and, seen in this context, the Commission's Consultation on the Discussion Paper on the Application of Article 82 of the Treaty is particularly important, especially in light of the avowed aim of the Commission to migrate, over time and where possible, from (*ex ante*) sector specific regulation to (*ex post*) competition rules. In this context, it is important to consider the important role played in the competitive process by the deployment of a critical competing infrastructure such as cable TV, and the continued challenges posed to the growth of cable TV networks through the actions of traditional "incumbent" PSTN operators on the one hand, and terrestrial and satellite broadcasters on the other. Most importantly, these challenges to, and from, cable TV have produced positive results for the European Union in the competitive broadband digital marketplace, which is characterised by clear and compelling evidence that demonstrates broadband deployment is most advanced precisely where infrastructure competition is most developed.

II. REGULATORY/COMMERCIAL/TECHNICAL CONTEXT

Cable operators services exist in a relatively unique environment, which has an important bearing on the extent to which they can ever exercise anything resembling market power. For example:

- The traditional telephony dimension of their business, and their provision of broadband services, is subject to a detailed regulatory framework at Community level which governs electronic communications networks and services. On a short cycle of every two years, National Regulatory Authorities review in detail the various product markets in which cable operators compete, and determine whether or not they should be the subject of *ex ante* regulation. These determinations are made in direct collaboration with the Competition and Information Society Directorates of the Commission under the auspices of the so-called "Article 7 Task Force". In addition, they are also subject to an institutionalised system of peer review by other National Regulatory Authorities,

whether on an individual basis or through the European Regulators' Group/International Regulators' Group. In turn, the deliberations of National Regulatory Authorities under this regulatory framework are subject to detailed requirements regarding public consultations. There thus exists a comprehensive regulatory tool which addresses all manner of exercise of market power stemming from the market structures in which cable operators find themselves.

- The broadcasting dimension of their business is subject to the ubiquitous "must carry" rules, and to a series of varied Member State (and, indeed, regional) rules geared towards the preservation of the goals of plurality and diversity on the one hand, and retail price controls on the other. The net result of these fragmented rules is that investment decisions often become seriously skewed and economies of scale become almost impossible to achieve other than in a handful of Member States which permit consolidation. In such operating environments, there are hidden costs to doing business and, indeed, the only way in which one can remain profitable is to explore the various ways in which to exploit the economies of scope that are available to cable operators (namely, the ability to provide a "triple play" of telephony, Internet access and video offerings). Retail pricing restrictions can have a particularly negative impact on overall revenue flows if a cable TV operator's telephony business is also price constrained at the wholesale level (*e.g.*, because an incumbent PSTN operator's termination charges are price regulated, it is often the case that such charges apply reciprocally to its competitors).
- The Lisbon Agenda staked much of the EU's economic well-being on the development of broadband services. The greatest success stories in the development of broadband in the EU have been precisely in those geographic areas where cable TV provides a real infrastructure alternative to the incumbent PSTN operator. Perversely, however, the Community's policy decision to bridge the perceived "digital divide" in many Member States by encouraging State aids to local government projects designed to roll out cable networks has meant that many private cable operators have had their investments undermined in those regions where such subsidies are being directed.
- Cable operators find themselves in a unique part of the media/telephony value chain. They sit, literally, at the crossroads of technological convergence. This brings with it tremendous opportunities to offer a diverse product offering. It also brings with it extreme competitive pressures, insofar as they are subject to the attentions of PSTN incumbents on the one hand, and public terrestrial and satellite broadcasters on the other. At one extreme, increasingly commoditised telephony services will always serve as the platform for the leverage of dominance by PSTN incumbents; at this end of the market, the goal of cable operators is to be able to match the telephony offering of the PSTN incumbent so as not to render themselves unattractive for the remainder of their service offerings. At the other extreme, public terrestrial and satellite broadcasters will be able to benefit from their large installed bases and unrivalled access to content; here, cable operators need to invest heavily in obtaining inputs in the form of quality content in order to compete with these media 'incumbents' before they can invest in the further deployment of their network. Added to this, public service broadcasters are heavily subsidised by their Member States which means, despite the increased vigilance of the Commission to ensure that those funds are not used outside the public broadcaster's public service remit, that independent cable TV operators' costs are indirectly raised to match such competition when the State-funded subsidisation of the Internet-related service offerings of such public service broadcasters occurs.
- The fact that cable is a shared medium has some important implications for its overall competitiveness. Insofar as a cable TV operator will become truly commercially

successful, for example, the fact that it is a shared medium will mean that congestion will occur. This will in turn mean that the cable TV operator will have to embark on a new wave of investments to be able to upgrade its existing network, yet alone to expand that network, in order to cope with increased (and shared) traffic flows.

- Precisely because cable is a shared medium, when considering the issue of wholesale commercial access, it is important that the technical differences between PSTN and HFC cable networks are reflected in the assessment of their potential substitutability. Although HFC cable networks generate services which compete head-to-head with services transmitted over PSTN networks, at the network level they have particular technical characteristics which mean that they are not full substitutes with PSTN networks as is explicitly recognised in the ex ante assessment of wholesale broadband markets under the New Regulatory Framework. Accordingly, wholesale access obligations would likely diminish the ability of operators to monitor capacity and traffic, prevent service degradation and ensure transmission quality in equal measure.
- Finally, to the extent that cable operators are providing a traditional media service to their customers -- indeed, this constitutes the bulk of their business -- it must be borne in mind that they are not at that time able to reap any benefits of "network effects". Unlike traditional telecommunications offerings, which are bi-directional, a traditional media offering is one which is enjoyed by the customer as an individual, without the need for interaction with other members of the network, nor is the value attached by the customer to the media service offered linked to any perceived value in having more customers on that network. Given that many forms of exclusionary behaviour are exacerbated by the existence of "network effects", this should play an important role in the evaluation of any competitive implications flowing from the commercial actions of cable TV operators.

It is critical for competition agencies to bear the matters listed above in mind when formulating general principles regarding their evaluation of potential exclusionary abuses under Article 82 of the Treaty. Such matters have a significant bearing on the ways in which costs are to be assessed, efficiencies are to be measured, the characterisation of legitimate competitive actions which have the outward appearance of exclusionary predatory pricing or bundling, and the business rationale for refusing to deal.

III. ANALYTICAL FRAMEWORK

Fundamental Principles

ECCA welcomes the fact that DG Competition's Article 82 discussion puts its enforcement policy as regards Article 82 in the context of the other policy reviews it has conducted over recent years, including:

- The Vertical Restraints Block Exemption Regulation and Guidelines.¹
- The Horizontal Block Exemption Regulation and Guidelines.²

¹ Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices OJ [1999] L 336, p 21 and Guidelines on Vertical Restraints OJ [2000] C 291, p 1.

² Regulation (EEC) No 2821/71 of the Council of 20 December 1971 on application of Article 81(3) of the Treaty to categories of agreements, decisions and concerted practices, OJ [1971] L 285, p. 46-48 and Guidelines on the applicability of Article 81 to horizontal co-operation agreements, OJ [2001] C 3, p. 2.

- The Article 81(3) Guidelines.³
- The Technology Transfer Block Exemption Regulation and Guidelines.⁴
- The Horizontal Merger Guidelines.⁵

Each of these policy advances has adopted an approach which is, on the whole, effects-based using economic principles, as opposed to form-based. Many other elements of those reviews are also relevant to the review of Article 82 and ECCA encourages DG Competition to adopt a best practice approach based on the success of the previous reviews.

ECCA wishes to place on record its support for the general approach of the Article 82 Discussion Paper. The most important of these is the emphasis placed on the central role of consumer harm, as opposed to competitor harm. Although this is not surprising, it is welcome and should help to ensure that there will be fewer decisions in the future which display a confusion as to what enforcement is seeking to achieve.

Similarly, the Discussion Paper (especially Section 5) attempts to place the application of Article 82 within a framework of analysis which should ensure that undertakings receive both consistent advice and have a much greater understanding of how Article 82 is likely to be enforced in the future.

More fundamentally, there is the important recognition that even with potentially exclusionary practices, it is necessary to carry out a balancing exercise which takes into account potential pro-competitive effects. In this respect, ECCA welcomes the explicit introduction of an efficiency-defence mechanism which in our view should serve to limit spurious complaints and unfounded enforcement activity.

IV. SPECIFIC ISSUES

In light of the preceding discussion at the level of general principle, ECCA now turns to a series of specific matters raised in the Discussion Paper.

Foreclosure

At a fundamental level, it is not entirely clear that the implied link between "dominance" and the ability to foreclose exists in all cases. Indeed, there is reason to doubt that this implied link is reliable in either direction. In other words, it is possible to think of cases both where a dominant undertaking has no ability to foreclose and of cases where an undertaking not in a dominant position might act in a manner intended to foreclose a rival. This means that a thorough and well-balanced assessment of economic effects is essential in all cases and the presumptions, even if rebuttable, should be reduced to the minimum possible.

³ Guidelines on the application of Article 81(3) of the Treaty, OJ [2004] C 101, p. 97-118.

⁴ Commission Regulation (EC) No 772/2004 of 27 April 2004 on the application of Article 81(3) of the Treaty to categories of technology transfer agreements, OJ [2004] L 123, p. 11-17 and Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements, OJ [2004] C 101, p. 2-42.

⁵ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ [2004] C 31, p. 5-18.

In relation to dominance, there is a concern that in complex and innovative markets, such as those in which ECCA members operate, static views of market dynamics may cause competition authorities and regulators to take an inappropriately narrow view on market definition. Over-reliance on product characteristics and a backward-looking approach can lead to a failure to take fully into account the emergence of competing technologies and the evolution of customer choices. Indeed, in today's broadband, digital market, given the pace of technological advancement and the increasing and welcome focus on spectrum liberalisation, barriers to entry for competing platforms are far less prevalent.

In fast-moving markets, an over-emphasis on market definition rather than on tangible abuse can lead to the wrong results. Where technological change can strip value or lower costs dramatically, a more integrated approach which bridges the analytical gap between market definition and market power may be necessary.

Second, the concern that dominant undertakings which do not have the ability to foreclose are nonetheless subject to the "special responsibility" not to impair genuine undistorted competition lies at least in part in the relatively low threshold at which dominance can be established under EU law. However, it also fails to capture the fact that many markets in a modern economy function well even with only a few large players. Indeed, it is clear that temporary positions of market power can improve competitive dynamics because of the beneficial effects on investment and innovation.

To the extent that the Commission wishes to go further than existing jurisprudence by adopting new categories of "dominance", including "75% dominance", "quasi-monopoly" and "legal monopoly", ECCA members believe that it is essential for the Commission to explain why this categorisation is being made, what are the expected implications of such a categorisation, and what are the expected different effects that the Commission believes will occur if strategic commercial behaviour is effected by any one of these separate categories of dominant firm.

These concerns are exacerbated by the very wide interpretation which the Commission applies to foreclosure. At paragraph 58, the Commission states that:

"By foreclosure is meant that actual or potential competitors are completely or partially denied profitable access to a market. ... Rivals may be disadvantaged where the dominant company is able to directly raise rivals' costs or reduce demand for the rivals' products. ..."

This test seems to suggest that the 'actual or potential competitor' should be able to choose the scale of entry and that it would be foreclosed if it found entry at that scale unprofitable. In this context, it should be noted that access to a market does not necessarily mean that the 'actual or potential competitor' needs to have the same market coverage or market access as the incumbent, merely that it has access to a sufficient number of customers in that market to make entry feasible.

It also seems to suggest that dominant undertakings should not bid for scarce inputs or improve their products. ECCA members, despite the fact that it is confronted with dominant market actors at either end of the value chain on which they operate, would not advocate the adoption of such an extreme approach. Such behaviour need not necessarily be considered to be foreclosing, but rather may simply be competition on the merits.

Equally, there may be situations where a firm that might not possess a substantial market power *ex ante* might nevertheless have very strong incentives to engage in anti-competitive practices. The returns from acquiring a dominant position through the application of abusive anti-competitive practices, such as predation, might easily be higher than the returns from applying the same practices with the purpose of simply maintaining a dominant market position. Nevertheless, the harm to consumers might be more significant in the first scenario.

This could be particularly relevant in the case of multi-product or vertically integrated competitors to ECCA members (such as certain content providers) or even as a result of otherwise perfectly legitimate licensing arrangements between content owners and platform providers.

The Discussion Paper mentions in passing that sector-specific regulation would remain unaffected by Guidelines based on the Discussion Paper (at paragraph 6). However, it should be noted that regulatory requirements may already restrain the commercial behaviour of undertakings and should be taken into account in determining whether and how to apply the competition rules. It also fails to take into account two key issues which are of concern to ECCA members.

First, regulatory solutions do not necessarily rely on competition law methods for defining markets and for identifying competitive harm. Nor do they necessarily seek to achieve outcomes which are the same as those sought by competition laws. For example, regulation may in certain circumstances impose access conditions (including prices), which competition laws could not.

It is important that the distinction between competition and regulation is recognized, particularly in relation to sectors involving the development of alternative infrastructures. Thus, decisions reached by NRAs in relation to market definition should not be considered to be decisive in relation to proceedings undertaken pursuant to Article 82. Equally, when reviewing market definitions proposed by NRAs, the Commission should ensure that its approach remains focused on how the market in question would be defined for the purpose of applying the competition rules.

Second, it is also important that clearer guidance be given in relation to the doctrine of essential facilities, referred to at paragraph 209 of the Discussion Paper. Others have already suggested that greater reference be made to the case-law of the Commission and the Community Courts in the Discussion Paper. In relation to infrastructure and essential facilities, the Commission needs to identify in a more systematic and detailed way when it considers infrastructure to be indispensable and what objective is being sought by requiring access to that facility (and perhaps even on what terms).

In this regard, the decision of the United States Supreme Court in the *Trinko Case* is exceptionally relevant and, to the extent the Commission regards the judgment in that case to be inapplicable or irrelevant, it should say so. In the US, the essential facilities doctrine (as developed in the lower courts), requires: (1) control by a monopolist of an essential facility or resource serving the monopolist's market; (2) a competitor's inability practically to duplicate the essential facility; (3) the monopolist's denial of the use of the facility to a competitor; and (4) the feasibility of providing access to the facility.⁶

In the *Trinko Case*⁷, the Supreme Court addressed three of the most controversial areas arising under section 2 of the Sherman Act.

- (1) A dominant firm's refusal to deal with its rivals.

⁶ See *MCI Communications Corp v AT&T Co* 708 F 2d 1081, 1132 (7th Cir 1983).

⁷ *Verizon Communications Inc v Law Offices of Curtis V Trinko, LLP* US Supreme Court decision of 13 January 2004. *Trinko*, a New York City law firm, was a local telephone service customer of AT&T. In its complaint, *Trinko* alleged that Verizon had provided interconnection access to its local exchange network on a discriminatory basis as part of an anticompetitive scheme to prevent AT&T and other competitors from encroaching on its historical local exchange monopoly.

The Supreme Court concluded that the refusal to deal alleged by *Trinko* “does not fit within the limited [duty to deal] exception recognized in *Aspen Skiing*” since there was no allegation that Verizon had voluntarily engaged in a prior course of dealings with its rivals, or that it had refused to provide any product that it already sold at the retail level to any other customers.

(2) The essential facilities doctrine.

The Court also concluded that the essential facilities doctrine had no application in *Trinko* since the *Telecommunications Act 1996* required Verizon to provide interconnection services to other carriers on a non-discriminatory basis, precluding any claim that access to the services at issue was unavailable. Perhaps more telling, however, was the Court’s seemingly hostile attitude towards the essential facilities doctrine itself. Observing that the doctrine had been “crafted by some lower courts,” the court emphasised that it has never been recognised by the Supreme Court, and the Court found “no need to either recognize it or to repudiate it here.” Moreover, the Court went out of its way to distinguish its prior decisions in *Railroad Terminals* and *Associated Press* – standard citations for the origin of the “essential facilities” doctrine – as involving concerted action, as opposed to a unilateral refusal to deal.

(3) Monopoly leveraging.

The Court held that the Second Circuit had erred “to the extent that the Court of Appeals dispensed with a requirement that there be a ‘dangerous probability of success’ in monopolizing a second market” in the context of a monopoly leverage claim.

The *Trinko Case* is clearly relevant insofar as EU and US case-law both rely on the essential facilities doctrine at lower levels. ECCA respectfully submits that *Trinko* lends weight to some of the language found for example in the *Bronner Case*⁸ which draws limits on when access is required to be granted. As the Court held in that case:

*“It should be emphasised in that respect that, in order to demonstrate that the creation of such a system is not a realistic potential alternative and that access to the existing system is therefore indispensable, it is not enough to argue that it is not economically viable ... For such access to be capable of being regarded as indispensable, it would be necessary at the very least to establish... that it is not economically viable to create a second home-delivery scheme for the distribution of daily newspapers with a circulation comparable to that of the daily newspapers distributed by the existing scheme”.*⁹

Whilst the doctrine of essential facilities may continue to have some traction in relation to railway, port and bridge cases, ECCA respectfully submits that its relevance is extremely limited, if at all, in relation to sectors which are subject to rapid change as a result of the introduction of new technologies. In particular, the doctrine should not be allowed to be abused by spurious complainants seeking to gain a commercial advantage over those who have invested in alternative infrastructure.

ECCA also questions the applicability of Article 82 to oligopolistic dominance. ECCA cannot think of any situations where market structure would lead to a finding of oligopolistic collective dominance and exclusionary abuse in the absence of some form of concerted practice. For reasons of predictability, and in order to make compliance possible, such anti-competitive behaviour should be captured by using Article 81.

⁸ *Oscar Bronner* [1998] ECR pp I-7791.

⁹ At paragraphs 45 and 46.

1. The Hypothetical Competitor Test & Predatory Pricing

A second main area of concern is how the Discussion Paper deals with the 'equally efficient competitor' test, and the relationship between that test and predation.

The Discussion Paper takes the view in relation to predation that only conduct which would exclude a hypothetical "as efficient" competitor is abusive (see, for example, paragraph 63). According to the Discussion Paper, foreclosure of an "as efficient" competitor (a hypothetical competitor with the same cost as the dominant firm) can only result if the dominant firm prices below its costs. The Discussion Paper suggests that where reliable information on the dominant undertaking's costs is not available, the Commission may instead use cost data of apparently efficient competitors.

There are a number of problems with this approach. Above all, any test based on a rival's costs is problematic in terms of predictability and welfare analysis. In addition, the 'equally efficient competitor' test may fail to take into account other important considerations, such as diversity of supply, quality and reliability. It may also fail to appreciate that across a diverse product or service package being generated in a converged environment, recourse to narrowly defined product markets based on historical single platform patterns of supply and demand may be an artificially narrow basis upon which to base a predatory pricing assessment. Indeed, the nature of digitalised products means that predation should be assessed over as broad a range of services as is appropriate in light of emerging demand patterns; such an approach better reflects the investment risks being borne by operators across the range of bundled products (as such, when assessing predation in the cable TV context, it would be more much appropriate to adopt the approach to the service bundle adopted by the Commission in its price squeeze assessment in the *Wanadoo Case*, rather than its narrower approach in its assessment of predatory pricing in the *Deutsche Telekom Case*).

It could also be argued that formalistic price-cost tests are not consistent with an effects-based approach in any event. The key to predation is a finding of some strategy or intent to exclude, coupled with evidence as to conduct. This requires evidence of the:

- sacrifice of short-run profits;
- negative impact on rival profitability, leading to market exit; and
- the recoupment of the short-term loss (even if this is not, strictly speaking, required by the European courts) associated with the predatory price, based on the ability to exploit increased market power.

ECCA takes the view that there is substantial merit in considering recoupment as a threshold test to be able to exclude the pursuit of unmeritorious cases. However, this should not be achieved by way of a rebuttable presumption, as appears to be the case at paragraph 122 of the Discussion Paper, where the Commission states:

"it will in general be sufficient to show the likelihood of recoupment by investigating the entry barriers to the market" ... "as dominance is already established, this normally means that entry barriers are sufficiently high to presume the possibility to recoup".

There also remains a lack of clarity on the relationship between new investment and predation. In particular, the Discussion Paper does not specify whether the intention of the parties at the time of the investments were planned and approved could be sufficient to rebut any inference of predation.

2. Tying and Bundling

The Commission recognises, at paragraph 178 of the Discussion Paper that:

- “both companies with and without market power engage in tying and bundling”;
- that bundling is a “fundamental part of many economic activities”; and that
- “tying and bundling are common practices that have often no anticompetitive consequences”.

Thus, the Discussion Paper should emphasise that the four conditions referred to in paragraph 183 are cumulative for the finding of an infringement pursuant to Article 82.

The Commission also recognises, at paragraph 181, that for tying/bundling to be abusive, it is “normally necessary to define the relevant market(s) on which both the tying and the tied product are sold.” However, the Discussion Paper seems to undermine or confuse these important principles in two main ways, both of which are of concern to ECCA members:

First, the Commission states, at paragraph 185, that it is:

“not necessary that the two products belong to two separate product markets. In a market with differentiated products, two products may be sufficiently differentiated that a company can be said to tie or bundle two distinct products.”

In its discussion of the evidence required to show that products are distinct, the Commission considers that three elements should be considered: consumer preferences, commercial practices of competitors and equivalents in other geographic markets, and product development. Given the importance of these criteria, far greater explanation should be given as to which factors are relevant and the rationale provided for their relevance.

In relation to foreclosure, the Commission explains that it is applying a two-step test. First, it assesses which customers are tied in and then whether these customers form a “sufficient part” of the relevant market so that the market can be considered to be foreclosed. As with the chapter of the Discussion Paper dealing with rebates, this notion seeks to identify “how big a share of customers’ requirements on average the entrant at least should capture”. The dominant company’s practices may be regarded as foreclosing if the shares of customers’ requirements purchased from actual rivals are smaller than the required share.

In terms of the potentially chilling effect on competition, this represents a serious difficulty. It is almost certainly too uncertain to be applied in practice and is far too open to mis-calculation and mis-characterisation when it comes to enforcement. It would appear to be designed to protect competitors, and not customers.

The Commission’s methodology for assessing mixed bundling at paragraphs 188 et seq is difficult to apply in practice without some further detailed explanation. The proposed cost test is hard to apply, particularly when mixed bundling is applied with rebate schemes.

Although the Commission rightly accepts in principle that a dominant firm can justify its tying/bundling conduct on the basis of safety considerations, at paragraph 204 it essentially takes away that possibility by stating that it is “not the task of a dominant company to take steps on its own initiative” to deal with these issues. However, it would be better to have a more tolerant approach to safety and service integrity justifications, as they are often an important rationale for tying/bundling. Indeed for cable operators, the ability to migrate its customer based from an analogue to a digital stream is an increasingly relevant concern as security of transmission from a copyright perspective is challenged by new distribution technologies.

It is difficult to see that the traditional conditions used to analyse competitive harm in a bundling case - namely, the existence of market power in one market, which is leveraged into another market, by which competition is significantly reduced - can hold true in the case of the type of bundling effected by cable operators in most European countries.

Cable operators' traditional product market is that of TV broadcasting. Cable operators are either currently, or in the process, of expanding into telephony and broadband. Seen in the context of where they sit in the value chain, ECCA takes the view that cable operators cannot exercise market power by way of leveraging into adjacent markets, especially given the potential for market entry via alternative technologies.

However, even if it were assumed that the requisite market power existed in connection with the provision of TV broadcasts, it is difficult to see how cable operators could reduce competition in either telephony or in broadband Internet. Telephony competitors are generally dominant incumbent PSTN operators. Given the fixed and sunk nature of a telephony network, there is no realistic possibility of inducing exit or even reducing the ability of PSTN incumbents to compete. This is also the case for broadband access, which is an incremental product, particularly for the fixed network employing DSL technologies.

In contrast, cable operators incur substantial investment costs in upgrading their networks to support bi-directional services, and face ongoing costs in increasing capacity on nodes as a result of the shared access nature of the technology. As such, it is highly doubtful that fixed networks would ever be capable of being foreclosed through the bundling practices of cable TV operators.

Cable operators need to remain free from restraint to offer innovative bundled products, not least to continue to counter incumbent PSTN operators who are in the process of allocating increasingly substantial levels of resources to the task of delivering pay-TV services over their own broadband networks.

3. Refusal to Supply

The Discussion Paper only covers situations where a dominant company denies a buyer access to an input and the effect is to exclude that buyer from participating in an economic activity downstream ("vertical refusals to supply").

Overall, it should be noted that the traditional refusals to supply tangible goods raise significantly different issues to IPRS and, indeed, are largely covered by the analysis of foreclosure effects in other sections of the Discussion Paper. However, the Discussion Paper contains insufficient recognition of the many justifiable reasons why undertakings in all markets, and whatever their market position, may need to terminate supply.

For this reason, and to avoid unnecessary interference in commercial negotiations, it is essential to keep sight of the fact that for there to be an infringement of Article 82, the input that is not being supplied is essential to allow competition to take place on the downstream market. For this purpose, "essential" should not mean "preferable" in the sense of better quality or lower production costs, but must mean something that is genuinely indispensable. If one is to consider a lowering of the standard of "essential" as the basis for mandating access, this should only be done in the context of a thorough sector-specific review to determine the scope of *ex ante* regulation, as the range of issues which will need to be taken into account to conduct a proper cost-benefit analysis is arguably too ambitious for a fact-specific *ex post* investigation.

IPRs raise different issues. Whilst it is clear that Article 82 can be infringed in exceptional circumstances where there is a refusal to license IPRs, the criteria laid down in the *IMS Case*

remain very difficult to apply in practice. In particular, it is unclear to what extent the “new kind of product” is distinguishable from existing products. In high technology sectors, where technological change drives shorter product cycles and where existing products are 'migrated' into new generations of services, this is a particularly difficult distinction to draw. What is clear, however, for cable operators, is that access to new forms of technologies, product innovations and formats that are being linked to content services by dominant producers can, and will, be a significant differentiator between competing platforms.

The Discussion Paper, at paragraphs 239 and 240, appears to go further than the *IMS Case* in talking about “follow-on innovations”. This language appears to be unsupported in existing case law and unclear in its scope and intent. As such, given the dynamics of the sector in which ECCA members operate, it is a cause for some concern.

There is also the issue of interoperability, which following the *Microsoft Decision* can be seen as a distinct form of refusal to supply. As discussed above, it is important in such cases to recognise that the effect on consumer welfare is indirect, remote and even more difficult to assess than in other cases. However, this difficulty should not be allowed to increase the burden on rights-holders by reducing the burden of proof to establish an infringement of Article 82.

4. Efficiency Defences

In ECCA's view, the debate regarding "efficiencies" is one of the most critical issues underpinning the whole debate regarding the re-appraisal of Article 82. The Commission's administrative practice under Article 82 has almost exclusively dealt with the issue of efficiencies in a very limited manner, namely, conceding its relevance only where it provided a "reasonable" or "objective" rationale for engaging in particular forms of market behaviour. In the merger context, it is arguable that efficiencies have had an even more restrictive role to play, being something tangible which needs to be passed on to consumers directly in the form of lower pricing or improved quality.

There is great uncertainty as to the scope of the various defences set forth in the Discussion Paper. The burden of proof is clearly on the party claiming the benefit of the defence. However, the nature of the defence is not always clear: to what extent can I meet competition from a given competitor? Precisely which kinds of efficiencies will be relevant in the context of Article 82? How can I show these will be passed on when there is already a finding of dominance (even at relatively low market share levels)? What timeframe can be taken into account?

Moreover, it is not clear that merger experience and the experience under Article 81(3) will be particularly useful in understanding how the efficiencies defence will be applied.

Mergers benefit from a presumption of benefit to the economy, and the efficiency analysis is part of an overall balancing exercise in that analysis - the question being once the efficiencies are taken in account, does the merger still significantly impede effective competition? It appears that, given the absence of an exemption provision in relation to Article 82, a similar approach will be taken to efficiencies and Article 82.

A merger analysis is essentially forward-looking, since the harmful effects will only be felt if the transaction goes ahead. Unlike merger control, the enforcement of Article 82 is essentially backward-looking. The question therefore arises whether the Commission's albeit limited experience in relation to merger efficiencies will be applicable in relation to Article 82.

It is also unclear from the Discussion Paper how the fourth condition of Article 81(3) [afford such undertakings the possibility of eliminating competition in respect of a substantial part of

the products in question] will interact with efficiencies under Article 82. Indeed, for a long time, the fourth condition of Article 81(3) was thought of as excluding individual exemption for dominant undertakings. This thinking appears no longer to be current - nevertheless, it would be helpful for the Commission to illuminate its thinking on the various degrees of competition and the elimination or diminution thereof which are relevant to this exercise. If the Commission intends to retain its categorisation of "dominance", "75% dominance", "quasi-monopoly" and "legal monopoly", this discussion of the interplay between Article 81(3) and Article 82 becomes all the more important.

These issues are particularly relevant as it is unclear whether the Commission will take an *ex ante* or *ex post* approach when assessing such efficiency claims.

V. CONCLUSIONS

ECCA welcomes the Commission's desire to generate a meaningful debate with a view to developing a more "effects-based" approach under Article 82 of the Treaty to replace the traditional, and rather formalistic implementation of that provision. However, the natural institutional tendency to characterise an "approach" as a legal "test" should be avoided, given the particular complexities which characterise many technology-driven industries such as the cable industry.

Those complexities add an additional dimension of fact-specific analysis to commercial practices such as predatory pricing and bundling. Many of the conventional wisdoms surrounding the exclusionary effects of such practices in traditional industrial sectors do not sit comfortably with innovation-driven markets in which economic value shifts quickly from one part of the value chain to another.

Moreover, the evaluation of the exclusionary effects of such practices in the abstract might tend to underestimate the delicate competitive and regulatory balance that cable operators must often negotiate. What is required is a better understanding of competitive efficiencies from the viewpoint of what drives investment, industry growth, and the importance of meeting competition. That is perhaps best achieved by conducting a cost-benefit analysis of the price of regulatory censure as measured against the need to give effect to such "efficiencies".