The Tension Between Regulation and Competitive Market Forces in Europe

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This Essay is an affectionate salute from two Louisiana law school graduates who had separately a fondness for Shael and Helen Herman, and thereby met at a Tulane programme, and subsequently pursued an affinity for European law and policy, as husband and wife. It is a pleasure and an honour to be able to contribute from Brussels to this scholarly commendation.

Our theme is the shifting frontier between competition law and regulation. One of us is an official. One of us is a practitioner. The official is engaged in policy development for de-regulating markets which have been micro-managed by some national public authorities in order to ensure "fair" competition. The practitioner worries that EU competition policy is being mis-used as a disguised means to regulate the markets, rather than as originally intended, to remedy and penalise abuses and infringements. So this Article will note two contrasting trends in European law and policy.

We remind the reader far from Brussels of some basic institutional facts. The European Commission serves as guardian of the treaties, proposer of new policies and prime enforcer of the European competition rules. Decisions taken by the Commission can be appealed to the European Court of First Instance in Luxembourg. Controversies arising before national courts which present problems of European law may be submitted by the national court to the European Court of Justice for a preliminary ruling on the particular problem.

We begin with telecommunications.

Until the 1980s, the European telecommunications sector was characterised by a strong public service monopoly tradition, together with national industrial policies of creating 'national champions', often

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run in conjunction with postal services. The environment began to change with privatisation and the introduction of limited competition in some countries in the mid 80s, primarily driven by the increasing application of information technology in the telecommunications sector, which offered the potential to revolutionise the industry.

Inspired by major trading partners and, with new technologies putting pressure on exclusive rights in telecommunications, the EU progressively dismantled the historic telecoms monopolies, beginning in 1987 with terminal equipment and concluding in 1998 with the full liberalisation of all services and infrastructure. *Liberalisation* of services (in effect, de-monopolisation or abolition of exclusive rights) was progressively put into place alongside progressive *harmonisation* of regulation. Harmonised regulation was initially based on the principle of Open Network Provision (ONP) where incumbents were allowed to retain ownership of their infrastructures but were obliged to provide access to their networks under ONP conditions of transparency of technical interfaces, non-discrimination and cost orientation. De-monopolisation needed complementary rules—usually imposed as access conditions (including price controls) on the incumbent—to act as a proxy for actual competition.

The impact of full liberalisation in 1998 was dramatic. Incumbents started entering into each other's markets. New entrants invested in new services and infrastructure, and users received a better deal. Countries like Spain and Ireland that had negotiated delays in opening up their markets changed their minds and chose to liberalise earlier than planned. The EU market grew and many tariffs, especially for long distance telephony, decreased. The *ex-ante* harmonised regulation was critical for this success. Some consider that the breakthrough was the benchmarking of interconnection price agreements in 1997, pegging Member States' interconnection rates to the best regulatory practice in Europe. Countries like New Zealand that liberalised their markets without *ex ante* regulation subsequently recognised their mistake.

The electronic communications sector continues to evolve towards competitive markets. At a macro level the process has been successful in transforming the communications landscape in Europe and improving the competitiveness of the EU. The initial rapid expansion of the market in the early years of liberalisation was followed by a period of market consolidation. The bursting of the dotcom bubble meant that this consolidation happened very quickly and was very severe. It led to a questioning of regulatory policy on both sides of the Atlantic. Some called for the relaxation of regulation to alleviate financial difficulties in

the sector. But premature removal of regulation from an uncompetitive market, or failure to regulate in the presence of a dominant company, would likely jeopardise the gains of the last fifteen years and possibly reduce the competition that resulted from liberalisation. Incumbents might re-establish their dominance in former markets or be able to leverage their power into other markets.

As early as 1999, the Commission was obliged to review the operation of the then-new regulatory framework. The positive effects of liberalisation were recognised but convergence had emerged in the meantime as a major factor for evaluation. Digital technologies allow all information (voice, text, audio and video) to be converted into digital form, in turn, allowing all content to be delivered over all networks. The Internet was rapidly becoming a common global infrastructure for the delivery of a wide range of electronic communications services spanning all previously existing categories of services and infrastructures. The network-dependent rules of the old framework were clearly going to be overtaken by technology. Markets would merge in response to convergence. This meant that a coherent regulation of infrastructures and associated services, taking account of convergence, was needed alongside any separate regulation that might be appropriate for content services.

The new regulatory framework therefore incorporates the principle of technological neutrality required by convergence in order to achieve proportionate regulation of converging markets. For purposes of market entry rules, for access and inter-connection of networks, and for *ex ante* regulation that temporarily substitutes for real competition, the new regulatory framework covers all transmission infrastructures (such as cable networks, satellite transmission networks, wireless networks and telecoms networks) in the same or similar ways. Regulation of commercial content services—such as e-commerce or audio-visual services—that may be offered over transmission infrastructures are covered by other Community instruments (such as the e-commerce directive[1] and the TV Without Frontiers Directive[2]). The title of the new regulatory framework reflects this change: "telecommunications" regulation has become "electronic communications" regulation.

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1. Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market ("Directive on electronic commerce").

2. Directive 97/36/EC of the European Parliament and of the Council of 30 June 1997 amending Council Directive 89/552/EEC on the coordination of certain provisions laid down by law, regulation or administrative action in Member States concerning the pursuit of television broadcasting activities.

The EU regulatory framework is based on five principles:

(1) Regulation should be kept to the minimum necessary to achieve the desired goals.
(2) Regulation should be based on clearly defined policy objectives of:
    (a) fostering economic growth and competitiveness; and
    (b) ensuring that objectives of general interest are met where they are not satisfied by market forces alone.
(3) Regulation should strike the right balance between flexibility and legal certainty.
(4) Regulation should be technologically neutral or objectively justifiable if it is not.
(5) Regulation may be agreed globally, regionally or nationally, but should be enforced as closely as is practicable to the activities being regulated.

The new regulatory framework seeks to promote competition and the development of the single market while protecting the interests of European citizens. Its legal basis is therefore article 95 EC. If, as expected, electronic communications markets become more competitive and converge, the new framework would systematically remove *ex ante* obligations and allow the normal application of EC competition law to constrain the commercial behaviours of companies in those markets. The new framework relies heavily on independent national regulatory authorities established in each Member State to apply the rules in the light of local market conditions. Coordination mechanisms are laid down to ensure consistent application of the EU framework in all Member States.

Because there are many electronic communications markets where competition has not yet developed, the new regulatory framework continues to provide for regulation in markets where there is effectively no real competition. National authorities may therefore impose, subject to Commission powers of review, *ex ante* obligations on companies with Significant Market Power, or SMP, which is equated with the concept of dominance as interpreted under EC competition law. The markets in which companies may be subject to such *ex ante* regulation have been identified by the Commission according to three criteria that are intended to capture only those markets where *ex ante* regulation is justified. The 3 criteria, which are applied cumulatively, are:

- high and non-transitory market entry barriers;

- markets that have a tendency towards non-competitive outcomes; and
- competition law remedies are insufficient to correct the lack of competition in the market.

Any markets proposed for regulation that do not appear in the Commission's list must be agreed with the Commission (in the consultation procedure described below). A standard procedure forms part of the regulatory framework for electronic communications whereby national regulators notify the Commission of their market definitions and market power analyses; as part of this procedure, the Commission vets the market definition and the analysis of market power in the relevant market. If the Commission disagrees with the definition or analysis, it has the power to require withdrawal of the notified measure. In practice, the Commission, having indicated its doubts about a proposed measure, discusses with national regulators on an informal basis the difficulties or weaknesses that it identified with their proposed measures. Generally this allows the problems with notifications to be resolved during the two month period built into the vetting procedure.

The new framework protects the interests of European citizens in several respects: (1) a guaranteed universal service that covers disabled users; (2) specific provisions for consumer protection, including simple dispute resolution procedures, and access to clear tariff information; and (3) a high level of protection in respect of the processing of personal data and our right to privacy. The new framework prohibits unsolicited commercial emails, or spam, and creates a link with possible national, or Third Pillar, measures that derogate from the e-privacy rules when national authorities engage in law enforcement activities.

Four new bodies were created in the new regulatory framework to assist the Commission in supervising the application of the rules: (1) the Communications Committee[3]; (2) the European Regulators Group[4]; (3) the Radio Spectrum Committee; and (4) the Radio Spectrum Policy Group. The new regulatory package consists of:

- a Framework Directive[5]
- an Authorisation Directive[6]

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3. As referred to in article 22 of Directive 2002/21/EC (*see post*).

4. As referred to at point 36 of the Recitals of Directive 2002/21/EC (*see post*).

5. Directive 2002/21/EC of the European Parliament and the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services (Framework Directive).

- an Access and Interconnection Directive[7]
- a Universal Service and Users Rights Directive[8]
- a Privacy and Electronic Communications Directive[9]
- a Decision on a Regulatory Framework for Radio Spectrum Policy[10]
- an article 86 (Commission) Directive on Competition in the Markets for Electronic Communications Networks and Services.[11]

In addition, a Regulation on unbundled access to the local loop (2887/2000/EC[12]) was fast-tracked into adoption although it was proposed at the same time as the above directives. The underlying approach, of mandating new entrants' access to the "last mile" of the incumbent's subscriber network infrastructure is conceptually similar to the earlier regulatory framework.

The Framework Directive covers definitions, scope, duties of national regulators, market definition and market power assessment procedures by national regulators and Commission review procedures for evaluation of draft national *ex ante* regulatory measures; it also covers numbering, naming and addressing and standardisation.

Under the rules for market analysis in the new framework, national regulators must conduct a three stage procedure before imposing or withdrawing any existing *ex ante* obligations: (1) they must first define the relevant market based on the Commission's initial recommended list of 18 markets (particularly the geographic scope); (2) they must assess the market power of undertakings on the market to determine if there is

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6. Directive 2002/20/EC of the European Parliament and of the Council of 7 March 2002 on the authorization of electronic communications networks and services (Authorisation Directive).

7. Directive 2002/19/EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities (Access Directive).

8. Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users' rights relating to electronic communications networks and services (Universal Service Directive).

9. Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (Directive on privacy and electronic communications).

10. Decision No 676/2002/EC of the European Parliament and of the Council of 7 March 2002 on a regulatory framework for radio spectrum policy in the European Community (Radio Spectrum Decision).

11. Commission Directive 2002/77/EC of 16 September 2002 on competition in the markets for electronic communications networks and services.

12. Regulation (EC) No 2887/2000 of the European Parliament and of the Council of 18 December 2000 on unbundled access to the local loop.

effective competition on the market; and (3) if they find no effective competition, they must designate at least one undertaking as having Significant Market Power and they must impose at least one regulatory remedy, either identified in Community legislation or specifically agreed by the Commission. If they find a market to be effectively competitive, they must withdraw any pre-existing obligations.

To protect the single market, and achieve consistency of application, the Commission services review the proposed national *ex ante* measures before their adoption at national level. If the proposed measure appears to jeopardise the single market or seems incompatible with Community law, and would affect intra-Community trade, the Commission can require, after consultation of the Communications Committee, withdrawal of either the relevant market definition or the national regulator's assessment of the market power held in the relevant market. Remedies are not subject to the above review procedure (but are fully subject to the Commission's enforcement powers under article 226 EC). In view of the discretion given to regulators on the choice of remedies, this issue has been addressed in a Common Position Paper of the European Regulators Group.[13] Companies may also appeal the decisions of their national regulator in national courts.

The Authorisation Directive recognizes the right to enter markets and provide services and it limits the conditions that Member States can impose on market entrants. It also lays down principles for charges and fees and requires that the award of rights of way be transparent, non-discriminatory and expeditious. Local authorities must separate their award of rights of way procedures from commercial activities such as network and service provision. The rules for market entry lay down a "light-touch" general authorisation procedure allowing companies to enter markets quickly and administratively simply. When companies need numbers or radio spectrum to provide their services, the procedures for acquiring the right to use these resources must be open, transparent and non-discriminatory. As an exception, the new framework recognises that Member States may nonetheless apply specific criteria and procedures to award the use of spectrum for radio and television broadcasting.

The Access and Interconnection Directive focuses on the wholesale aspects of network and service provision. When companies cannot agree commercial terms of interconnection or access, national regulators may

13. Paper entitled "ERG Common Position on the approach to appropriate remedies in the new regulatory framework". Approved at ERG8 Plenary on 1 April 2004, *available at* http://www.erg.eu.int/documents/docs/index_en.htm.

intervene. The directive incorporates the principle of "any-to-any" connectivity and allows national regulators to impose obligations to achieve this. This directive contains the list of possible remedies for national regulators to impose at the wholesale level when they determine that a relevant market is not effectively competitive. Regulators may also seek Commission approval if a wholesale remedy not identified in this directive is thought to be more appropriate. Since this directive is oriented to interconnection and access at the wholesale level, pre-existing Community rules on the right of broadcasters to access conditional access systems (in set top boxes) of encrypted broadcasting services are carried forward in this directive; provision is made for future adaptation. The "toolbox" from which regulators can pick their appropriate remedy is composed of obligations for transparency, non-discrimination, accounting separation, mandated access to a network or service, or price regulation.

This directive covers the scope, costing and financing of universal service schemes, and designation of universal service providers. A fundamental requirement of universal service is to provide users on request with a connection to the public telephone network at a fixed location, at an affordable price. The requirement is limited to a single narrowband network connection. The definition is technologically neutral and allows Member States to use wired or wireless technologies to satisfy the requirements of universal service provision. The connection must be capable of supporting speech and data communications sufficient for online access to services over the Internet. During the legislative adoption process, there were calls for inclusion of broadband data rates within the definition of universal service. As a compromise, it was agreed to review the definition of universal service in 2005, a full year before the assessment of the new regulatory package as a whole as some believed that broadband rollout might justify extending the definition of universal service quickly.

The Universal Service Directive legislates for the first time in an area that touches upon both infrastructure and content regulation: the mandatory television and radio broadcasting carriage rules that Member States impose on cable network operators. It is one of very few areas in the new regulatory framework that bridges the gap between infrastructure and content regulation. The relevant rules are called "must carry" in as much as they represent broadcasting content that network operators are required to carry. The must carry rules create a tension with the general provision in the Treaty on the right to provide services in the EU.

The new paradigm of converging and widely available electronic communications services not only offers new possibilities for users but also raises new risks for their personal data and privacy as well as new challenges for national authorities to collect information needed for law enforcement and national security. The e-privacy directive protects fundamental rights and freedoms of natural persons, to a different extent for legal persons, with regard to automated storage and processing of their data. The Directive does not legislate in regard to the data protection issues that are not governed by the First Pillar competence of Community law, so the possibility for Member States to take measures necessary for the protection of public security, defence, State security, and criminal law enforcement is not affected by the directive. Nonetheless, the directive explicitly reflects the requirement that such national measures must be appropriate, proportionate to the intended purpose, necessary within a democratic society and in accordance with the European Convention for the Protection of Human Rights and Fundamental Freedoms.

The e-privacy directive requires that traffic data (identifying the users and subscribers of electronic communications services, what numbers originated calls and where they terminated) must be deleted or rendered anonymous by companies after it is no longer needed for commercial purposes. Data needed for processing calls and billing subscribers may be processed for the duration of the billing cycle and the period in which the bill may be challenged. Companies must obtain the consent of their customers to engage in marketing and to offer other added value services. Before seeking consent, companies must inform their customers of the data processing to which the data will be subject.

Location data (identifying the approximate geographical location of users of mobile services) can only be processed with the consent of the subscriber and only to the extent and for the duration necessary to provide the value added service in question. Again, the user must be informed of the type of data processing involved and whether the data will be transmitted to third parties in order to provide the service. Consent must be obtained.

Unsolicited communications, including faxes and emails, are prohibited without the express consent of the receiver, unless a pre-existing business or commercial relationship exists and, even then, a specific opt out must be offered to the receiver upon each receipt of such messages. Direct marketing tactics and disguised sender identities are prohibited and a valid return address must be provided for recipients to request that no further messages be sent.

Unbundled access to the local loop was taken out of the draft for a new regulatory framework, turned into a stand-alone Community instrument, given accelerated treatment by the EP and Council and adopted for application from January 2001. The purpose was to create competition in the local access network, and to stimulate a more competitive provision of broadband (xDSL) services by mandating shared access to the local loop. Local loop unbundling was specifically called for in the Lisbon Council conclusions (March 2000), and was supported by national regulators. The measure did not prove to be as successful as was originally expected, possibly because of the requirement for some network rollout by new entrants, but demand for unbundled local loops has been growing significantly in recent months, fuelled by developments like "Voice over Internet Protocol (VoIP)". Another product that is closer to a wholesale broadband end-to-end service, "bitstream access" has proved to be attractive to some new entrants (and is covered by one of the identified markets in the Commission's list). The pricing of unbundled local loops presents a difficult issue, because the local loop is an input to the provision of telephone services and some telephone line rentals are still priced below cost in a number of Member States.

Commission directive 2002/77/EC[14] carries forward the original abolition of all special and exclusive rights but updates the coverage from telecommunications to electronic communications; it maintains the legal requirement for operators that own both a cable network and a telecoms network to separate the commercial management of such networks, without a need divest themselves of either network; and it updates the terminology of this new directive to that of the new regulatory framework under article 95 EC. This directive has been used as a the legal basis to bring France to the Court of Justice over their discriminatory (and non-technologically neutral) treatment of cable networks in France as compared to telecoms networks. When cable television network operators in France offer telecommunications services, they are subject to more onerous regulation than telecoms operators.

The new regulatory framework takes account of the technological convergence between broadcasting, telecommunications and information technology, covering transmission networks and associated facilities (e.g., conditional access services) that carry broadcasting services.

14. Commission Directive 2002/77/EC of 16 September 2002 on competition in the markets for electronic communications networks and services.

However, the framework does not regulate services that provide broadcasting content (e.g., TV channels). Nevertheless, the new framework allows regulators to take account of the links between transmission and content. For instance, Member States may attach 'must carry' rules to their authorisations for the provision of broadcast transmission services.

The story of telecoms is encouraging. In the first three-quarters of the 20th century, the old telecoms monopolies failed to deliver. They offered high-priced services of indifferent quality with little innovation. Up until the 1980s, traditional telecoms monopolists controlled all forms of telecommunications. They controlled all equipment attached to the networks, and themselves issued licences for others to use their networks. The impact of full liberalization of all telecoms services in 1998 was dramatic. The number of fixed telecoms operators doubled in the then EU Member States in the period between 1998 and 2003.[15] Incumbents started entering each other's markets. New entrants invested in new services and infrastructure, and consumers received a better deal all round. Member States, like Spain and Ireland, who had negotiated delays in opening up their markets, changed their minds and choose to liberalize earlier than planned. The EU market grew, and everybody benefited. Between 1996 and 2002, EU telecommunications services got much cheaper. On average, for the same telecoms services, consumers spent about 30% less of their income in 2002 than they had in 1996. Over the 1996 to 2002 period, the affordability index for average income users in all Member States sank to a record low in 2002.[16] However, some of these developments were lost in the bursting of the dotcom bubble at the end of the 90s.

In its Eleventh Implementation report adopted in February 2006[17], the impact of liberalization and harmonization continues to impress. The report takes note that "the sector has always been defined by rapid technological and market change. …traditional markets are maturing and competition is driving players to invest in new technologies to deliver innovative services based on convergence between broadband networks, audiovisual media and electronic devices, with consumers benefiting from higher data speeds and improved quality". The report goes on to describe the sector in glowing terms:

15. SEC(2004) 866, at 4.
16. *Id.* at 44.
17. COM (2006) 68 final.

> The e-communications services sector continues to represent the largest segment of the overall ICT sector, accounting for 44.4% of the total value, up from 43% last year. The sector was worth €614 billion in 2005, €273 billion of which derived from e-communications services. Overall revenue growth continued strong at estimated levels of between 3.8% and 4.7%. The production and use of ICT accounts for around 40% of productivity growth and one quarter of overall growth in Europe.[18]

The figures for growth and investment suggest competition encourages market players to invest and innovate. This creates a virtuous circle of greater choice of services of good quality at lower prices. In short, history appears to teach us that better choice, richer technological offerings, and more competitive price are associated with deregulated markets rather than regulated ones. So the European Commission has been preaching abstinence and self-restraint to national regulators.

The Microsoft Case

The second part of this Article considers whether European competition enforcers have gone beyond the traditional bounds of antitrust law and have started to use competition policy as a disguised means to regulate the markets. This will be illustrated with a case that is no doubt familiar to many, the *Microsoft* case.

Microsoft is a famous company which has been involved in a succession of celebrated antitrust cases. One of the authors has had the challenging privilege of acting for the company in its European competition law procedures. Microsoft's U.S. antitrust controversies reached a climax in 2000 and 2001, with the celebrated order of District Judge Jackson; the company's successful appeal to the D.C. Circuit Court of Appeals; the recusal of Judge Jackson; the assignment of the remanded case to a new judge, Judge Kollar-Kotelly; settlement negotiations pursuant to her instructions; a settlement in November 2001; litigation on the adequacy of the settlement and the constitutional propriety of the settlement before her under the Tunney Act; and her final judgment in November 2002.

The European case, which involves a number of the same actors as the U.S. case, began with the issuance of a Statement of Objections in August 2000, followed by another on different grounds in August 2001 and a further one in August 2003. This last one led to a European Commission Decision in March 2004 condemning Microsoft under

18. *Id.* at 2.

article 82 of the EC Treaty for two alleged abuses of its dominant position. Both abuses are novel in orthodox competition law.

The first abuse related to the inclusion in the basic Windows operating system for personal computers of a number of media functionalities, notably video streaming. The theory was that in offering an operating system which was richer in features than its predecessor, Microsoft was actually selling as a bundle two products which ought to have been sold separately. Thus in 1999, when Microsoft added video streaming capacity to the many other media features already included in the basic Windows operating system (such as audio streaming, video downloading or high quality sound), it was violating its duty under article 82. There would have been no infringement if the unimproved version of Windows, lacking video streaming capacity, had been left on the market (albeit at the same price as the improved version!) when the improved version was launched. By analogy (and analogies are always imperfect) the inclusion by a dominant car manufacturer of a radio or a GPS system as a standard feature of the car being considered as a bundle when radios or GPS systems were a novelty would be problematic; on the Commission's theory, the car manufacturer would cure the antitrust problem by selling some old models lacking a GPS, even if no customer would want them.

The behavioural remedy for the "tying" offence was intriguing. Microsoft was ordered to develop a special "fully functioning" version of Windows, without media functionality. In accordance with the Commission's instructions, Microsoft removed 200 files from the operating system, thus developing an operating system to control a modern computer but lacking the capacity to exploit its multi-media features. Indeed, the lack of commercial reality of the offence and the remedy is demonstrated by the fact that while over 30,000,000 copies of normal Windows have been delivered since the emasculated version of Windows was launched, perhaps 1,730 of the latter have actually been delivered to end users or lovers of the electronically eccentric. Our own copy of Windows XP-N ("N" for "not": *not* with media functionality) is a precious souvenir which may one day acquire antitrust antique status.

The theory as to how this tie caused harm to the market is also somewhat novel. There is no impediment to prevent a user having several media players on his or her computer. Microsoft's so-called tie did not in fact compel the user to use its media player. The Commission's theory of competitive harm is based on so-called "indirect network effects". The competitive harm results because (the Commission says) third party content providers will react in a particular

way: they will encode only in Windows media formats because it is the best way to be sure that their content can be played by the widest possible audience. The Commission's theory is that XP-N would force content providers to think again. In truth, the success of Apple's iPod and iTunes media store might be a far more important factor in their thinking. Content providers are far more likely to reconsider the idea of encoding in only one format by the success of these Apple products than by the emergence of an emasculated version of Windows.

Overall, it seems difficult to avoid the conclusion that antitrust enforcers indulged in the temptation to organise the market rather than detect and punish recognised abuses of the market. It is hard to imagine why offering a better and more richly featured product for the same price is in common sense terms an economic offence.

The second abuse is often described as relating to interoperability. On the interoperability side of the case, the applicable law is richer. But the remedy remains revolutionary in antitrust terms. The accusation was that Microsoft should have furnished to one of its competitors details of the technology by which its servers communicated with each other when cooperatively delivering a directory service. More precisely, Microsoft should have delivered, in 1998, details of the secret communications protocols underlying what would in 2000 become Active Directory, the directory portion of the server operating system called Windows Server 2000. There was controversy as to whether these protocols were banal rules of the road or whether they were the fruit of hundreds of person years of research. There was dispute as to the extent to which the technology was covered by patents. It was concededly eligible for protection as a trade secret. The Commission's line was that trade secrets, not being the creation of a public law right, were eligible for no deference from EC competition law.

Since the cases of *Volvo v. Veng*[19] and *Magill*[20], it has been established that failure to license design rights and copyright could in exceptional circumstances constitute an infringement of article 82. Commentaries commonly say that *Microsoft* is a "compulsory licensing" case, but it is much more than compulsory licensing. All previous compulsory licensing cases involved material which was *already* familiar

19. Case 238/87, Volvo (UK) Ltd. v. Veng AB, [1988] ECR 6211.

20. Commission Decision 89/205/EEC of 21 December 1988 (*Magill TV Guide/ITP, BBC and RTE*), OJ [1989] L 78/43, upheld by the CFI in Case T-69/89, Radio Telefis Eireann v. Comm'n, [1991] ECR II-485, upheld on appeal by the ECJ in Cases C-241/91 P and C-242/91 P, Radio Telefis Eireann (RTE) and Independent Television Publications Ltd (ITP) v. Commission, [1995] ECR I-743.

(like the shape of a Volvo door in *Volvo/Veng*, the hours of BBC television programmes in *Magill*, and the contours of a map of Germany especially convenient for the pharmaceutical industry in *IMS*), widely known and widely used.

By contrast, Microsoft was ordered to prepare a description of how its Windows source code functions, a task which has occupied over 200 people and today engages fifty people in Redmond, then hand this over to its competitors, and license them to use it and Microsoft's IP rights in the process. Microsoft must make the specially written description easy enough for a person without deep Windows expertise to use. This is a first in competition law history. The Commission argues that the criteria of *IMS* do not apply, by reference to various points of policy. Various exceptional circumstances or "factors" are mentioned. None of them alone is sufficient to justify a compulsory licence but they are said to be individually "relevant". Microsoft argues that without very clear standards no compulsory licence can possibly be lawful; and that in this case, in light of the material at stake and the legal rights attached to that material, the jurisprudence of the European Courts called for not less rigorous criteria.

The difficulty was to identify the limiting principles from the *Magill* compulsory licensing case: if it was valid to order the BBC to tolerate the reproduction of its future programmes on a weekly basis by a weekly magazine that competed with the BBC's weekly magazine, what was the generally applicable legal principle relevant to other copyright holders, or other IP holders, or other licensors? We have seen that one of these limiting principles is the concept of *new product*, which aims to ensure that a refusal to license does not prevent the development of a secondary market which the rightholder is not himself exploiting.

A restatement of the applicable limiting principles came with the European response to *Trinko*[21] (or was *Trinko* the U.S. response to *Oscar Bronner*[22]?), namely *IMS*. *IMS* was the scribe at a meeting of German pharmaceutical industry companies which desired to develop the best and most logical method of capturing pharmaceutical sales data information so as to maintain the privacy of individual pharmacies, and match locations of doctors, pharmacies and patients. A map of Germany divided into so-called "bricks" using postal codes as frontiers was drawn up. There was a dispute over whether the map's copyright was held

21. Verizon Commc'ns, Inc. v. Law Offices of Curtis Trinko, 124 S. Ct. 872 (2004). See also the *Verizon v. Trinko* roundtable discussion in 7(2) GLOBAL COMPETITION REV. 16 (2004).

22. Case C-7/97, Oscar Bronner GmbH & Co. KG v. Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co. KG & Others, [1998] ECR I-7791.

jointly by the pharmaceutical companies or was the property of IMS, which had organised the meeting. There was no doubt that a map could be copyright, regardless of its simplicity or complexity. There was debate over whether copyright in the map was infringed by the presentation of sales data allocated by reference to the zones or bricks constituting the map. The effectiveness of marketing efforts by each pharmaceutical company could be judged by the number of packets of medicines prescribed by doctors and delivered by pharmacies in each zone. There were other formats in which data could be presented than the one pioneered by IMS, but in the eyes of the Commission the IMS format was the only one which would be acceptable to customers. The Commission felt that it was essential to have access to that format in order to supply to the pharmaceutical companies sales data about deliveries of medicines by wholesalers to pharmacies. The Commission's theories were couched in terms of "essential facilities". The President of the Court of First Instance suspended the immediate effectiveness of the Commission Decision, following which the case is no longer being pursued at Commission level. However, the German domestic litigation continued, and generated a question from the *Oberlandesgericht Frankfurt* to the European Court of Justice. Under what conditions could the refusal to license an IP right constitute an abuse of a dominant position?

The European Court of Justice proposed four criteria in a judgment which emerged just after the Commission Decision in Microsoft. The Court's ruling, drawing from *Magill* and *Bronner*, stated or recapitulated the four conditions under which a dominant undertaking may be ordered to license its intellectual property rights:

(a) The licence must be *indispensable* for carrying on a particular business;
(b) the refusal is such as to *exclude any competition* on the secondary market;
(c) the refusal prevents *the emergence of a new product for which there is potential consumer demand*; and
(d) the refusal is *not objectively justified*.[23]

These conditions are cumulative.[24] One may assume they are likely to be interpreted restrictively and applied with much caution.[25]

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23. *IMS*, *op. cit.* paras. 37-38.

24. *See* Advocate General Poiares Maduro's Opinion of 14 July 2004 in Case C-109/03, KPN Telecom BV v. Onafhankelijke Post en Telecommunicatie Autoriteit (OPTA), judgment currently pending, para. 35.

25. As acknowledged by Advocate General Poiares Maduro:

The Advocate General's Opinion and the Court's judgment in *IMS* diverge slightly. Advocate General Tizzano started his analysis from *Commercial Solvents* and *Télémarketing*[26] (which are "true" refusal-to-deal cases) before going on to the IP cases *Volvo/Veng* and *Magill*, as well as to *Bronner*.[27] The Court chose to start its analysis[28] directly from *Volvo/Veng* and *Magill* (both refusals to license). The Court's diverging approach in such an important case cannot have been trivial or meaningless. It should mean that the encroachment on IP rights by compulsory licensing is to be examined separately from the general refusal to deal cases.

Intense debate has ensued as to whether the Microsoft decision is consistent with the *IMS* judgment.

First, in actual practice the technology is not *indispensable* for competitors to enter the server market or to remain there. The existence of several types of server operating systems confirmed that competing products existed without having had access to the technology at issue, one of them having emerged during the period of the alleged abuse. Particular debate concerned whether the technology was meant to assist the competing servers more perfectly to communicate with Microsoft servers or to act in a network of Microsoft servers replicating how a Microsoft server acts. The Commission Decision states that a non-Microsoft server operating system should be able to perform as if it were a *replication* of a Windows server operating system in the delivery of certain services.[29] It further argued that Microsoft's specifications are

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> [A] duty under Article 82 EC for a dominant undertaking to aid its competitors should not be assumed too lightly and refusal to supply a competitor is not automatically considered abusive just because the inputs in question are necessary to compete on a secondary market. A balance should be kept between the interest in preserving or creating free competition in a particular market and the interest in not deterring investment and innovation by demanding that the fruits of commercial success be shared with competitors.

Id. para. 39.

26. Case 311/84, Télémarketing v. CLT and IPB, [1985] ECR 3261.
27. Paras. 48-49 *et seq.* of AG Tizzano's Opinion.
28. *IMS*, *op. cit.*, para. 34 *et seq.*
29. Microsoft Decision, *op. cit.*, para. 669 (Emphasis added]:

> *As regards the use of open industry standards implemented in Windows, interoperability within a Windows work group network largely depends on specifications that are proprietary or are extended versions of standard protocols. Therefore, open industry standards fall short of enabling competitors to achieve the same degree of interoperability with the Windows domain architecture as Windows work group server operating systems do. Since all major work group server operating system vendors already support most of the open industry standards supported in Windows, it can be concluded that this degree of interoperability proves to be insufficient for them to viably compete in the market. Therefore, reliance on open*

indispensable for this purpose because no other alternative was viable by which Microsoft's competitors could interoperate with servers using the Windows operating system.

Second, there is no *new* product for which there is unmet demand: while the Commission hopes *new products* may emerge from licensees, the Decision has nothing specific in mind, and imitations mimicking what Microsoft already offers to customers are not new to the market place. There is no secondary market that is currently unexploited.

Third, as to *elimination of competition*, competition has not been eliminated due to the condemned conduct in 1998, nor subsequently: nothing more than a risk has been identified, a threat which has now been imminent for eight years. There is a clear contrast to cases such as Magill, where the BBC's refusal to license the IP right caused Magill to exit the market forthwith.

Fourth, as to *objective justification*, the value and complexity of the technology and the efforts required to create it as well as the IP rights attaching to it entitle Microsoft to choose not to accede to an exorbitant demand for assistance. Indeed it seems difficult to imagine what could be more persuasive justification than effort, skill and the creativity confirmed by the grant of patents.

Thus the Microsoft Decision involves the classic problem of whether competition law should be enforced so as to assist competitors, or to assist the process of competition. The notion is that forcing innovators to share their technology will stimulate innovation: Microsoft would be stimulated to try harder through having its technology expropriated. It might be called the horticultural approach: in rose bushes, pruning stimulates effort by the plant to produce. When applied to the grabbing of technology, it sounds nonsense because it is nonsense.

The Decision is an attempt to reconfigure how the marketplace works, by handicapping the leading player in perpetuity in two respects. Some commentaries on the case have rather assumed there must have been a big problem, so something needed to be done. Yet the Decision does not say the technology is really indispensable to be on the market; it merely expresses a fear of a risk to competition, a weak justification to impose unprecedented extraordinary remedies. Such major encroachments on Microsoft's rights should only have been considered if there was a commensurate paralysing competitive obstacle.

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industry standards cannot be considered to be at present a realistic substitute to disclosures by Microsoft.

Both infringements identified by the Decision, indeed created by the Decision, are astonishing, unprecedented. The Decision condemns a company for not offering a product which no rational person wants to buy. It condemns a company for launching a richer-featured product at no extra price, by reference to a fear of what other people might do in response to the launch, so called tipping. It sees the offering of extra functionalities in a richly featured product not as the delivery of something better, more useful and more enjoyable, but as an illegal bundle.

Likewise, it condemns a company for not saying yes to a competitor who requests valuable and secret future technology. And the remedy is to help anyone with an interest build a replica, a functional equivalent. Neither new offence helps consumers. Neither new remedy encourages innovation.

There has been a remarkable absence of consumer harm. Instead, the Commission's case has largely been made by large competitors of Microsoft who seek a better outcome in Brussels than they obtained before their domestic courts. They are free to do so. But competition law should honour technical creativity and persistence no less than legal creativity and persistence.

It is easy to say competition law should benefit competition rather than competitors. Applying that worthy principle may not be easy. Where there are vociferous complainants, it is wise to act on the basis of facts not speculation or creative forecasts or artificial market definitions. Yet the Decision speaks of risks to competition which could happen imminently, but which have not happened. The commercial problems it envisages are based on competitors complaints and surveys of opinion. Yet the ample contrary evidence of the real world was discarded.

Article 82 exists to sanction abuses and thereby enhance the process of competition, not to pursue a regulatory policy favouring one business model rather than another. This neutrality as to the outcome of the competitive process is all the more necessary in important Commission decisions especially in a high technology field. The principles applied to one dominant player must be capable of application by other authorities and by courts. Likewise, if there are no limiting principles, enforcement becomes arbitrary and prone to abuse. Conduct should not suddenly become so illegal that it gets the heaviest fine in history.

Microsoft is a company which has made extraordinary technological achievements in only thirty years. Its products have great importance for our daily lives at home and at work. A litigation or a controversy involving Microsoft frequently proceeds in a unique manner, with a lot of

technology to understand as background and often a lot of passion in the foreground. There may well be a sense that it is necessary to apply special standards to Microsoft because of its wealth and the importance of its influence over computers. Other IT companies may be very large and may even be dominant, but somehow Microsoft arouses a unique level of concern.

There are two responses to this concern. First, Microsoft's activities are not unregulated nor unsupervised by government agencies. This applies to the scope of IP and copyright protection for software and inventions associated with computers. It applies to public procurement: governments choose to prescribe that as a policy matter they will procure software other than from Microsoft. It applies to the disclosure of standards and to file formats. It is not the case that only the contested Decision can constrain the influence of Microsoft. To put it plainly, if the concern of the European Commission is how to control the market power of Microsoft, governments and international organisations have the resources, and use those resources, to do this themselves.

Second, distorting normal legal principles to reach the desired result creates its own subsequent distortions, difficulties and injustices. Article 82 is not designed to regulate the market but to remedy abuses of market power. The Commission is asking the Court to make an astonishing departure from the established principles as to tying. The theory of the infringement is truly counter-intuitive, penalising the creative company which offers a better product for the same price, even if consumers demonstrably make their own choices about whether to use the new "bundled" features from Microsoft or from some other supplier. As to compulsory disclosure, the recent and authoritative judgment of the European Court in *IMS* is discarded in favour of other amorphous and unpredictable considerations. The two remedies are what characterise the whole case. They are not regulating the primary market, they are seeking to shape how other markets work.

It is extremely difficult to formulate permanently valid principles by reference to which the contested Decision can convincingly be upheld. For competition law to help competition, we need identified abuses, the blocking of unexploited markets, affirmative hindering of competitive opportunity by caprice or self-oriented conduct. The Commission seems to be targeting not real abuses but Microsoft's dominance. The Commission says it wants a level playing field, competition on the merits outside the personal computer area, but the new abuses it creates make it impossible to act in other markets without Commission approval or other

than within a Commission sponsored regime. This is a case of regulation of the market via the competition rules.

The perceptive reader will have observed that one of us prudently commends deregulation and uses the Commission's legal instruments to that end; and that the other contends the Commission's powers to enforce article 82 of the EC Treaty have been misused. We look forward to debating these worthy topics in a refurbished New Orleans in the esteemed company of Shael and Helen.