Law and Interdisciplinarity

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The Interplay of Law and Economics in Competition Law

From the Humble Beginnings to the More Economic Approach*

Wolfgang Wurmnest

I. Introduction

It is a simple truth that the two disciplines of law and economics can have a particularly fruitful relationship in the area of economic regulation. Most commentators agree that legal rules applying to the economy should make economic sense. Otherwise unwarranted welfare losses will occur. Having said

* The text draws to a very large extent from *W. Wurmnest*, Marktmacht und Verdrängungsmissbrauch (2nd edn., 2012). I warmly thank *Martin Fischer* for his linguistic review of the manuscript and *Svenja Langenhagen*, *Justin Röper* and *Luca Wölk* for their work on the footnotes.

that, the legal system also has certain needs and peculiarities that must be respected in order to create an optimal regulatory framework.

One of the key areas of economic regulation is competition (antitrust) law,[1] the rules of which seek to maintain unfettered competition on the market. In Germany, there is a long tradition of applying economic insights to shape the body of competition law. This joint venture is certainly one of the earliest "law & economics" movements, one that started in the nineteenth century. With the benefit of hindsight, one can see that not all of the effects of this collaboration have been favourable for competition, even though things have generally improved significantly over the course of time. This chapter will examine two major developments that took place in Germany and consider the lessons which can be learned about the sound interplay between law and economics in the area of competition law.

The first part adopts a historical perspective, analysing the interplay between law and economics over the course of the development of the modern German legal system. It will therefore start in 1871, when Germany became a unified state. In the decades that followed, more and more markets came to be controlled by various types of collusion amongst competitors to the detriment of free and unfettered competition. Unlike in the US, where the Sherman Act was passed in 1890,[2] it took much longer to develop a modern competition law in European states. In Germany the first modern competition act was adopted only in 1957 after an intense debate, and even this act was far from perfect. However, in the same year the European Economic Community was established, which has over the years developed a powerful competition law system. Today, the interpretation and application of the European competition rules strongly shapes the national competition rules of the EU Member States. National competition laws are also to a large extent harmonised with the EU rules.

Against this background, the second part of this chapter will take a closer look at the "more economic approach" to the interpretation and application of competition law. This approach has been introduced incrementally by the EU Commission over the last two decades and bases the application of competition law to a greater extent on robust economic insights. The debate on the "more economic approach" was strongly influenced by US developments, which will also be briefly explained.

The final part will explain three lessons that can be learned from the long history of competition law and economics in Europe.

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[1] The notions of "competition" and "antitrust" law are used synonymously in this chapter.

[2] 26 Stat. 209 (1890). On the passing of this Act, see *H.B. Thorelli*, The Federal Antitrust Policy (1955), 164 ff.; *R.J.R. Peritz*, Competition Policy in America, 1888–1992: History, Rhetoric, Law (1996), 9 ff.

II. The difficult beginnings: no competition law, please!

A. The German cartelisation movement and its backing by economic thought

After the German unification in 1871, the increased industrialisation led to various waves of economic booms, but also to oversupply and price crashes. As a result, German industries looked for a means to consolidate supply and demand. More than in other European States,[3] it was typical for competitors to restrict competition through agreements on, for example, output restriction, price fixing or market allocation, although these arrangements were in the beginning often local in reach and fluid.[4] The first German-wide institutionalised cartels were formed in 1876 in the steel industry and in the potash mining sector – the latter cartel was actually an initiative of state-owned companies in Prussia and Saxony-Anhalt.[5] Towards the end of the nineteenth century, cartels spread not only to more and more industries but also became significantly more stable and organised,[6] and individual members were sometimes forced to join the cartel, occasionally even by the state.[7]

This approach was backed by prevailing German economic theory. The *Historische Schule* led by the economist *Gustav (von) Schmoller* saw the formation of large business associations and monopolies as a natural consequence of the ongoing process of industrialisation in a modern economy. Cartels, they believed, aimed at "saving production costs and furthering technical improvements in production".[8] In line with historic precursors they regarded these eco-

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[3] See *U. Wengenroth,* Die Entwicklung der Kartellbewegung bis 1914, in: H. Pohl (ed.), Kartelle und Kartellgesetzgebung in Praxis und Rechtsprechung vom 19. Jahrhundert bis zur Gegenwart (1985), 15–27, 16: "Allenfalls in Österreich, Belgien und – mit Abstrichen Frankreich – können wir tendenziell ähnliche Entwicklungen beobachten, ohne daß die Kartelle dort vor dem ersten Weltkrieg eine ebenso beherrschende Stellung wie in Deutschland erreichten."

[4] *H. Roth*, Die Kartellverordnung vom November 1923 und ihre Bonner Variante, Jahrbuch für Wirtschaftsgeschichte 3/4 (1962), 11–56, 11, points out that cartels in the various German states were formed as early as the first third of the nineteenth century but that these structures saw a particular boom after the foundation of the German Reich; see also *F. Kleinwächter*, Die Kartelle: ein Beitrag zur Frage der Organisation der Volkswirtschaft (1883), 138, pointing out that many cartels were formed after the economic crash of 1873.

[5] *H.G. Schröter*, Kartellierung und Dekartellierung 1890–1990, Vierteljahrschrift für Sozial- und Wirtschaftsgeschichte 81 (1994), 457–493, 459.

[6] *Schröter* (n. 5), 459. On the economic factors that supported the establishment of such structures, see *Wengenroth* (n. 3), 17 ff.

[7] On the legitimisation of the Potash Mining Syndicate in 1910 by the German legislature, see *K.W. Nörr*, Die Leiden des Privatrechts (1994), 17 f.

[8] *G. von Schmoller*, Verhandlungen der am 28. und 29. September 1894 in Wien abgehaltenen Generalversammlung des Vereins für Socialpolitik über die Kartelle und über das ländliche Erbrecht (1895), in: Verein für Socialpolitik (ed.), 234: "[Kartelle sind] gleichsam

nomic power structures as a form of self-governance which helped realise economies of scale and organise the market to avoid ruinous competition. Far-reaching agreements amongst competitors were seen to have saved markets from "falling prices, bankruptcy, capital devaluation, dismissal of workers and breadlessness".[9] The Austrian economist *Friedrich Kleinwächter* characterised cartels as "modern guilds"[10] and emphasised that cartels were "children born out of necessity" to overcome economically difficult times of oversupply.[11]

Given that cartels and monopolies were regarded as an essential component of industry, the German legislature at first refrained from enacting modern competition legislation. The coming of the twentieth century did not bring much change, and the war economy in World War I even fostered cooperation amongst competitors.[12] During the debate on possible legislative action against the cartels, the Sherman Act was noted but a reception of US law was generally rejected. The view prevailed that unlike in the US, where trusts had – in the words of *Schmoller* – established "a system of robbery and fraud" making far-reaching prohibitions necessary, the German cartels worked for the benefit of the general public, and thus such legislation to restrict the establishment of such structures was thought unnecessary.[13] What followed was that Germany turned into a country of cartels ("Land der Kartelle").[14]

B. The embracing of economic teachings by the Reichsgericht

That cartels could spread across industry and trade was possible only because German courts did not develop rules for the protection of the competitive process based on the general provisions of private law. When the establishment of cartels increased significantly, those who were affected by such structures tried to seek redress before the ordinary courts under the general rules of law.[15] The discussion largely hinged on the question of whether outsiders or those cartel members that were sanctioned by the cartel for not complying with its rules

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eine naturgesetzliche, […] nicht zu hindernde, auf Ersparung an Produktionskosten und technische Verbesserungen der Produktion gerichtete Entwicklung [der modernen Wirtschaft]".

[9] *L. Brentano*, Über die Ursachen der heutigen socialen Noth (1889), 23: "Preissturz, Bankrott, Kapitalentwerthung, Arbeiterentlassung und Brodlosigkeit".

[10] *Kleinwächter* (n. 4), 179: "moderne Zünfte".

[11] *Kleinwächter* (n. 4), 143: "Kinder der Not".

[12] See *O. Lehnich*, Der Gegenwärtige Stand der Kartellfrage, Zeitschrift für die gesamte Staatswissenschaft 87 (1929), 501–544, 502.

[13] *Von Schmoller*, as cited by *J. von Hein*, Die Rezeption US-amerikanischen Gesellschaftsrechts in Deutschland (2008), 117 f.

[14] *Schröter* (n. 5), 457; *J. Basedow,* Kartellrecht im Land der Kartelle: zur Entstehung und Entwicklung des Gesetzes gegen Wettbewerbsbeschränkungen, Wirtschaft und Wettbewerb 2008, 270–273, 270.

[15] On the early case law, see *R. Schröder*, Die Entwicklung des Kartellrechts und des kollektiven Arbeitsrechts durch die Rechtsprechung des Reichsgerichts vor 1914 (1988), 9 ff.

could claim damages or injunctions. Ordering such legal consequences required that the conspirators had engaged in unlawful behaviour. Against this background, it was argued that price-fixing agreements and similar arrangements were void for infringing freedom of trade (*Gewerbefreiheit*) as enshrined in § 1 *Gewerbeordnung* and thus should be unenforceable against those who infringed the agreement. Alternatively, the general clauses of tort law could have served as a basis for redress against cartels. After the adoption of the *Bürgerliches Gesetzbuch* (BGB), businesses tried to rely on, *inter alia*, § 823(1) BGB to stop the anti-competitive conduct of their competitors and contractual partners. To the detriment of competition, both approaches were rejected by the *Reichsgericht* (Imperial Supreme Court) in a series of judgments handed down between 1890 and 1902.[16]

From the perspective of the interplay between law and economics, the 1897 judgment on the Saxon wood pulp cartel is of particular relevance here. The case concerned an agreement in which the producers of wood pulp in Saxony agreed to market their products only via a central sales point to ensure reasonable prices above the competitive level. It was alleged that one of the cartel members sold its products directly to customers, thereby bypassing the cartel's centralised sales system. The association in charge of the organisation of the cartel therefore claimed a contractual penalty from the member for violation of the agreement. To avoid payment, the cartel member claimed that the contract setting up the cartel was void. This argument was rejected by the *Reichsgericht*. The court cited *Kleinwächter*'s work and referred to the works of other economists to explain why cartels are necessary to avoid ruinous competition.[17] Against this background the court argued that agreements concluded "in good faith" to ensure reasonable prices in the industry were valid, and as a result contractual penalties for violations of such an agreement were enforceable. That courts in other jurisdictions, namely in the US, had declared such contracts to be null and void, was noted by the court (which even cited comparative sources),[18] without however much attention being paid to the reasons motivating those judgments.

C. Weimar Republic: controlling abuses of economic power

During the Weimar Republic (1919–1933), the German economic mainstream believed that an economic order based on cartels and other collective actors was a natural consequence of capitalism. The teachings of economists like *Werner Sombart*, who argued that economic concentration is typical for an

[16] RG, judgment of 25 June 1890, RGZ 28, 238 – Rabattkartell Buchhandel; RG, judgment of 4 Feburary 1897, RGZ 38, 155 – Sächsisches Holzstoffkartell; RG, judgment of 14 December 1902, RGZ 56, 271 – Börsenverein des deutschen Buchhandels.

[17] RG, judgment of 4 Feburary 1897, RGZ 38, 155, 157 – Sächsisches Holzstoffkartell.

[18] RG, judgment of 4 Feburary 1897, RGZ 38, 155, 159 – Sächsisches Holzstoffkartell.

advanced capitalistic economy,[19] and *Eugen Schmalenbach*, who posited that the increased amount of fixed costs in industrial mass production leads to massive overproduction and thus forced businesses to cooperate,[20] were readily received by lawyers and used to justify cartels and other forms of economic concentration.[21]

Germany was, however, tormented by a galloping inflation and an economic crisis in the post-war period, and the legislature came under pressure to take at least some steps to restrict price increases stemming from cartel formations. What arose from this was that in 1923, a time when around 1,500 cartels were operating in Germany,[22] the *Verordnung gegen Missbrauch wirtschaftlicher Machtstellungen* (KartellVO)[23] (Ordinance against the Abuse of Economic Positions of Power) was enacted.

This instrument, which was drafted in less than four weeks, was born of out necessity "to do something" to counter the economic crisis.[24] Given that cartels were seen by many as a useful means of structuring the economy, the KartellVO did not declare price-fixing conspiracies and other form of anticompetitive agreements as illegal and void. The German legislature merely allowed for a little more control over the cartel's conduct.[25] Accordingly, the power to terminate cartel agreements by cartel members for good cause was strengthened (§ 8 KartellVO), and a mild form of oversight for potential abuses was established via a special cartel court (§ 9 KartellVO). In addition, the Ministry of Economic Affairs was empowered to have prices and terms reviewed by the courts on the basis of public policy standards (§ 10 KartellVO). Despite its modest scope, the KartellVO was subject to fierce criticism by lawyers, and the *Deutsche Juristentag* of 1928 demanded a long list of changes to strengthen the powers of cartels.[26]

Given the paucity of remedies under the KartellVO, persons affected by the cartels also had to rely on the general provisions of private law to seek justice.

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[19] On Sombart's teachings, see *Nörr* (n. 7), 70.

[20] *E. Schmalenbach*, Die Betriebswirtschaftslehre an der Schwelle der neuen Wirtschaftsverfassung, Zeitschrift für Handelswissenschaftliche Forschung 22 (1928), 241–251, 241 ff.

[21] *Nörr* (n. 7), 70 f.

[22] *Roth* (n. 4), 16, referring to an estimation of *Metzner*, Industrie- und Handelszeitung, Karlsruhe 27 November 1925. See also *R. Liefmann*, Kartelle und Trusts und die Weiterbildung der volkswirtschaftlichen Organisation (6th edn., 1924), 18 (estimating that thousands of cartels had existed or existed in Germany at the time).

[23] Verordnung gegen Missbrauch wirtschaftlicher Machtstellungen, Reichsgesetzblatt 1923 I, 1067 ff., corrected in Reichsgesetzblatt 1923 I, 1071.

[24] See *Nörr* (n. 7), 54 ff.

[25] See *J. Jickeli*, Das Kartellrecht in der Weimarer Republik – Lehren für das europäische Kartellverbot, in: A. Hoyer et al. (eds.), Gedächtnisschrift für Jörn Eckert (2008), 405–424, 415 ff.

[26] Verhandlungen des Fünfunddreißigsten Deutschen Juristentages 1928 (Salzburg), vol. 2 (1929), 851 f.

Even though the *Reichsgericht* in 1897 had not stopped the cartelisation process by declaring anticompetitive agreements void, it did accept that certain abusive practices of cartels could be prohibited under the general rules of tort and unfair competition law. The leading case was decided in 1931 and concerned exclusionary conduct that today would be scrutinised under predatory pricing standards. Specifically, several large producers of petrol had cooperated to divide Germany into various geographic zones with uniform prices. An independent petrol station that purchased petrol from a foreign competitor had refused to adjust its petrol prices to the level set forth by cartel, so the cartelists ensured that all the petrol stations in the surrounding area undercut the prices of the independent seller. The independent petrol station sued the producers to obtain an injunction. As the predatory pricing strategy could not be stopped on the basis of the KartellVO, given that the cartel merely coordinated their behaviour via an information exchange that was not covered by the cartel concept under the Ordinance (which demanded a legally binding agreement),[27] the *Reichsgericht* had to take recourse to the general clause of unfair competition law as well as to § 826 BGB to find that such anticompetitive conduct was *contra bonos mores*.[28] The court was well aware that price cutting, as such, is the essence of competition and should not be prohibited by the law.[29] But given that particular circumstances of the case, the systematic undercutting was regarded as an unlawful manoeuvre to drive the independent petrol station out of business rather than an instance of lawful price competition. Otherwise, reasoned the German court, an economically healthy outsider confronted by a powerful group of competitors with deep pockets would have no choice but to exit the market or raise its prices to the level of those of the cartel, even if the cartelists because of their higher cost of production could not compete on the merits with the outsider. In declaring the coordinated price cutting as unlawful, the *Reichsgericht* discarded expert opinions by *Rudolf Callmann*,[30] *Rudolf Isay*[31] and *Hans Carl Nipperdey*,[32] three renowned competition law experts who had argued that the price-cutting conduct was lawful.

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[27] See *Nörr* (n. 7), 96. In addition, undercutting the prices of outsiders was not actionable under Sec. 9 KartVO, see RG, judgment of 9 January 1928, RGZ 119, 366, 369 – Linoleum-Konvention.

[28] RG, judgment of 18 December 1931, RGZ 134, 342, 350 ff. – Benrather Tankstelle.

[29] RG, judgment of 18 December 1931, RGZ 134, 342, 355 – Benrather Tankstelle.

[30] *R. Callmann*, Außenseiter und Kampfpreise, Juristische Wochenschrift 1930, 1647–1650.

[31] *R. Isay*, Der Vernichtungszweck im Wettbewerbsrecht, Gewerblicher Rechtsschutz und Urheberrecht 1929, 1368–1380, 1370 ff.

[32] *H.C. Nipperdey*, Wettbewerb und Existenzvernichtung, Kartell-Rundschau 1930, 127–152.

D. The road towards a modern competition law: changes in economic and legal thinking

After the Nazis came to power, the concentration of power in the economy gained further ground. This collaboration helped the government to control and direct private economic activities. During the course of World War II, the Ministry of Economics even tightened the grip on cartels to ensure a strong platform for war production.[33]

The excesses of economic concentration that were already visible during the Weimar Republic and which reached their peak during the Third Reich led, however, to a shift in economic and legal thinking. At the beginning of the 1930s, a group of scholars centred around the economist *Walter Eucken* and the lawyers *Franz Böhm* and *Hans Großmann-Doerth* established a school of thought which elaborated an economic and legal framework to protect competition and to push back the teachings articulated by the Historic School and related approaches.[34] This circle was referred to as the Freiburg School, as *Eucken* held a chair at the University of Freiburg and *Böhm* started his academic career there before he was later removed from university service for criticising the Nazis' oppression of Jews.[35]

Unlike *Schmoller* and *Kleinwächter*, *Eucken* and *Böhm* were very sceptical about the positive effects of widespread collaboration amongst competitors. They had seen how cartels and monopolies could effectively control competition and eliminate economic freedom of other market players. Therefore, the idea of a limitation of private power through law became one of the key ideas of this line of thought, and later the term "Ordoliberalism" was established as a general term for conceptions of a legal and economic order based on this belief.

The ordoliberal economists rejected the economic justification of cartels and monopolies that had dominated until then. *Eucken* emphasised that the process of competition will be inhibited if private businesses obtain too much economic power over their competitors. Authorities should intervene to ensure free

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[33] On the competition policy of the Third Reich, see *Nörr* (n. 7), 131 ff.; *A. Pöting*, Die Kartellgesetzgebung als Instrument staatlicher Wirtschaftslenkung im Zeitalter des Nationalsozialismus (2006), 83 ff.

[34] See *F. Böhm/W. Eucken/H. Großmann-Doerth*, Unsere Aufgabe, printed as the preface to: *F. Böhm*, Die Ordnung der Wirtschaft als geschichtliche Aufgabe und rechtsschöpferische Leistung (1937), VII–XXI, IX ff.

[35] On the foundation of the Freiburg School, see *A. Heinemann*, Die Freiburger Schule und ihre geistigen Wurzeln (1989), 8 ff.; *D.J. Gerber,* Constitutionalizing the Economy: German Neo-liberalism, Competition Law and the "New" Europe, The American Journal of Comparative Law 42 (1994), 25–84, 28 ff.

competition and ban economic concentrations as far as possible.[36] One Freiburg economist, *Leonhard Miksch*, even went so far as demanding far reaching public intervention, namely to control *all* dominant firms so that they act "as if" they were controlled by competition,[37] but that view was not shared by other scholars.

To overcome the lack of comprehensive private law regulations directed at stopping anti-competitive conduct, *Böhm*, who had already spoken out sharply against abuses of market power in his habilitation thesis,[38] started to work on a private law doctrine to prevent restrictions of competition. One of his key ideas was that cartels and dominant firms should not be allowed to rely on the principle of freedom of contract, guaranteed under private law, to restrict the freedom of action of other market participants to the detriment of the competitive process.[39]

The sceptical views of the Freiburg scholars regarding cartels and monopolies were matched, to a large extent, by the interests of the Western Allies, above all those of the Americans. In the immediate aftermath of the war there was a strong interest in dissolving German cartels and monopolies, which had greatly promoted the German war economy and the Nazi-regime.[40] Even though the beginning of the Cold War led to a more forgiving view of the Western-German economic structures, the Americans were very firm in their belief that without proper competition law, Western Germany should not be allowed to become a sovereign state.[41] At the same time, some ordoliberal thinkers gained important positions in post-war Germany and tried to

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[36] *W. Eucken*, Die Wettbewerbsordnung und ihre Verwirklichung, ORDO: Jahrbuch für die Ordnung von Wirtschaft und Gesellschaft 2 (1949), 1–99, 64 ff.; *W. Eucken*, Grundsätze der Wirtschaftspolitik (1952), 334 ff.

[37] *L. Miksch*, Wettbewerb als Aufgabe: Grundsätze einer Wettbewerbsordnung (1947), 98 ff.

[38] See *F. Böhm*, Wettbewerb und Monopolkampf: Eine Untersuchung zur Frage des wirtschaftlichen Kampfrechts und zur Frage der rechtlichen Struktur der geltenden Wirtschaftsordnung (1933).

[39] Over the course of his career, *Böhm* developed different justifications for this general theme, see *K.W. Nörr*, An der Wiege deutscher Identität nach 1945: Franz Böhm zwischen Ordo und Liberalismus (1992), 1 ff.; *E.-J. Mestmäcker*, Das Privatrecht vor den Herausforderungen der wirtschaftlichen Macht, Rabels Zeitschrift für ausländisches und internationales Privatrecht 60 (1996), 58–71, 58 ff.

[40] The agreement reached at the Potsdam Conference in 1945 stated (II B, Economic Principle 12): "At the earliest practicable date, the German economy shall be decentralized for the purpose of eliminating the present excessive concentration of economic power as exemplified in particular by cartels, syndicates, trusts and other monopolistic arrangements". On the deconcentration policy of the Western allies in the direct aftermath of World War II, see *W. Möschel*, Entflechtungen im Recht der Wettbewerbsbeschränkungen (1979), 4 ff.; *L. Murach-Brand*, Antitrust auf deutsch (2004), 42 ff.

[41] For details, see *Murach-Brand* (n. 40), 164 ff.

implement their ideas in the law. A Draft Competition Act[42] was elaborated by a group of experts, including *Böhm*, under the leadership of *Paul Josten,* who had close ties to the Freiburg School.[43] This so-called Josten Draft was presented to the German administration in 1949.[44] As it was, however, in part too interventionist, it did not play a major role in the following negotiations surrounding the first German competition act, the draft of which was essentially worked out by the officials of the German Federal Ministry of Economics and the three Western powers, under the leadership of the US.[45]

When the first modern competition act, the Act Against Restraints of Competition (*Gesetz gegen Wettbewerbsbeschränkungen*, GWB), was passed in 1957 after a very intense debate, it was neither a mere copy of the Sherman Act nor did it reflect the interventionist thinking of some members of the Freiburg School. Rather, the combined efforts of the US coupled with the insights generated by the Freiburg School and other liberal thinkers made it possible to swing the pendulum towards a system that protects free und unfettered competition, but the fierce resistance of the industry meant that these prohibitions were to an extent watered down in the legislative process. For the first time in Germany, however, the law prohibited cartels as a general rule and allowed them only in exceptional cases. In addition, it established a regime to control anticompetitive conduct of dominant firms.

The German GWB was thus a compromise and far from perfect. Two enormous gaps soon became apparent. First, the prohibition of cartels was too narrowly drafted, as only contracts could be regarded as cartel agreements. This led the *Bundesgerichtshof* (Federal Supreme Court) in 1970 to rule that concerted practices on price fixing which did not involve contractual agreement could not be sanctioned under the GWB.[46] This decision was harshly criticised[47] and corrected by the legislature when the German GWB was aligned in

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[42] Entwurf zu einem Gesetz zur Sicherung des Leistungswettbewerbs und zu einem Gesetz über das Monopolamt mit Stellungnahme des Sachverständigen-Ausschuss zu einigen grundsätzlichen Fragen der deutschen Monopolgesetzgebung und Minderheitsgutachten, gedruckt im Auftrag des Bundesministers für Wirtschaft (ohne Jahresangabe).

[43] The economist Paul Josten had served in the Ministry of Economic Affairs during the Third Reich and had close contacts with the Freiburg School. After World War II, he became a high-ranking administrator in the German economic administration established in the British and American Sector of Germany, see *Murach-Brand* (n. 40), 107 with n. 130.

[44] On the Josten Draft, see *E. Günther,* Die geistigen Grundlagen des sogenannten Josten-Entwurfs, in: H. Sauermann/E.-J. Mestmäcker (eds.), Wirtschaftsordnung und Staatsverfassung, Festschrift für Franz Böhm zum 80. Geburtstag (1975), 183–204, 187 ff.; *Murach-Brand* (n. 40), 107 ff.; *Nörr* (n. 7), 163 ff.

[45] For details, see *Murach-Brand* (n. 40), 175 ff., 227.

[46] BGH, judgment of 17 December 1970, Gewerblicher Rechtsschutz und Urheberrecht 1971, 276, 279 f. – Teerfarben.

[47] See *W. Möschel,* 70 Jahre deutsche Kartellpolitik: Von RGZ 38, 155 "Sächsisches Holzstoffkartell" zu BGHZ 55, 104 "Teerfarben" (1972), 24 ff.; *K. Schmidt*,

1998 with the European prohibition of anti-competitive agreements (today Art. 101 Treaty on the Functioning of the European Union, TFEU). Second, there was no mechanism to prevent concentrations. This gap was closed 1973 with the introduction of a merger control regime in 1973. As part of this, the Monopolies Commission was established, which is an independent body comprised of mainly lawyers and economists which monitors merger activity in Germany and advises and informs the legislature and the public on competition policy.

III. The interpretation and application of modern competition law: the European economic approach

Around the same time that the German competition order was being established, the European competition rules were being negotiated. The first antitrust rules were laid down in the 1952 Treaty establishing the European Coal and Steel Community. As they reflected the peculiarities of the coal and steel industry, they were not regarded as a blueprint in the negotiations leading to the 1957 Treaty establishing the European Economic Community, which, *inter alia*, set out the prohibition of anticompetitive agreements and of abusive practices of dominant undertakings.[48] Today these rules are enshrined in Art. 101 and 102 TFEU.

After the German and European rules for the protection of competition became effective, *inter alia*, by establishing proper competition authorities and enforcement rules, the interplay between law and economics also assumed a more practical component. The staff of the enforcement authorities, namely the *Bundeskartellamt* and the European Commission, came to consist of lawyers and economists, with both working closely together when judging industry conduct and sanctioning anticompetitive practices. In addition, courts were more often confronted with economic expert opinions. As consequence, the integration of economic theory into competition law became a very practical topic.

A. Post-Chicago economics and beyond

While prior to World War II a large variety of rather heterogeneous economic approaches to competition law existed, over the course of time the leading approaches taught in the US and Europe have become narrower. The prevailing

Wirtschaftsrecht: Nagelprobe des Zivilrechts – Das Kartellrecht als Beispiel, Archiv für die civilistische Praxis 206 (2006), 169–204, 181, with further references.

[48] On the negotiations leading to the European competition rules, see *W. Wurmnest*, Marktmacht und Verdrängungsmissbrauch (2nd edn., 2012), 66 ff.

doctrines for competition policy have to a greater and greater extent been based on neoclassical microeconomic price theory concepts within the area of industrial organisation. As a starting point, these concepts base the analysis of competition problems at the theoretical level strongly on pricing decisions and decide allocation problems based on the efficiency yardstick. Put simply, price theory became very influential in the US with the rise of the so-called Chicago School of economic thought in the 1970s, which analysed competition problems based on rational market actors and a strong belief in the corrective force of markets. What this meant was that this Chicago School advocated for very limited intervention in the market, an approach which can be contrasted with the Harvard School.[49]

Today, the current lines of thought for competition law and policy are typically grouped under the heading "Post-Chicago-Economics" within the research area of modern industrial organisation.[50] These doctrines are based on much more refined sets of analytical tools than those available to the Chicago School in the 1970s. Such Post-Chicago developments include, amongst other things, game-theory insights on the strategic interactions of market participants. As data is more readily available, econometric studies of real-world examples have also gained increasing importance and are today firmly established in modern economic thinking. At least at the theoretical level, Post-Chicago economics are embraced by a broad majority of competition economists.

That mainstream economic doctrine has become narrower does not however mean that there is a broad consensus on competition policy matters. These doctrines are often very abstract, and thus disputes arise on their application to individual cases. In addition, some findings of modern industrial economics are challenged in part by the findings generated by experimental and behavioural economics, to name two important strands of novel research. Experimental economics is testing general assumptions about market behaviour based on experimental studies conducted in the field or in a laboratory with test subjects.[51] Behavioural economics, a field which was strongly advanced by the psychologists *Daniel Kahneman* and *Amos Tversky*,[52] focuses to a large extent on the issue of bounded rationality by integrating insights from psychology and neuroscience into the economic analysis, thereby adapting the results inferred

[49] On the views of the competing schools regarding single firm conduct, see *H. Hovenkamp*, The Harvard and Chicago Schools and the Dominant Firm, University of Iowa Legal Studies Research Paper No. 07-19 (2010), available at https://ssrn.com/abstract=1014153 or http://dx.doi.org/10.2139/ssrn.1014153 (last accessed 15 August 2022).

[50] *C. Ewald*, Grundzüge der Wettbewerbsökonomie, in: G. Wiedemann (ed.), Handbuch des Kartellrechts (4th edn., 2020) § 7 para. 8.

[51] On this approach, see *A.E. Roth*, Introduction to Experimental Economics, in: J.H. Kagel/A.E. Roth (eds.), Handbook of Experimental Economics (2020), 3–109.

[52] See *M. Englerth/E.V. Towfigh*, Verhaltensökonomik, in: E.V. Towfigh/N. Petersen (eds.), Ökonomische Methoden im Recht (2nd edn., 2017), § 8 para. 481.

from the *homo oeconomicus* concept.[53] And even *Friedrich von Hayek*'s definition of competition as an "open discovery procedure" ("*Wettbewerb als Entdeckungsverfahren*")[54] and his plea to keep markets open in order to allow for innovation has not been forgotten. Thus, still today, economists may produce different answers to the same questions.[55]

B. The "more economic approach" by the EU Commission

Professional standards have to be updated regularly. This is generally true and applies equally to the economic insights which are used to resolve legal issues. Since the end of the 1990s, the EU Commission has therefore prepared, advocated and finally applied a "more economic approach" to competition law. This shift, in part driven by US influence,[56] precipitated a heated debate on the reach and usefulness of such an approach, especially in Germany.[57] The intensive debate on the more economic approach should, however, not be seen as a fight between those lawyers in favour of the integration of economic thought into the law and those who oppose economic thinking. There is a broad consensus in the antitrust community today that economic insights are indispensable for the analysis of competition law issues.[58] The debate therefore centres around the question how legal and economic criteria can be optimally assembled to form a coherent regime. In this respect, a reasonable compromise between economic theory and the necessities of the law must be found, as it is impossible to create rules against anticompetitive practices whose application comprehen-

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[53] On this approach, see *C. Jolls/C. Sunstein/R.H. Thaler,* Behavioral Approach to Law and Economics, Stanford Law Review 50 (1998), 1471–1550; *R.B. Korobkin/T.S. Ulen*, Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics, California Law Review 88 (2000), 1053–1144.

[54] *F.A. von Hayek*, Der Wettbewerb als Entdeckungsverfahren (1968).

[55] See, generally, *H. Fleischer*, Informationsasymmetrie im Vertragsrecht: Eine rechtsvergleichende und interdisziplinäre Abhandlung zu Reichweite und Grenzen vertragsschlußbezogener Aufklärungspflichten (2001), 10.

[56] For details, see *B. Wardhaugh*, Competition, Effects and Predictability: Rule of Law and the Economic Approach to Competition (2020), 92 ff.

[57] See the contributions to *D. Schmidtchen/M. Albert/S. Voigt* (eds.), The More Economic Approach to European Competition Law (2007).

[58] See *P. Behrens*, Comment: Controlling dominance or protecting competition: from individual abuses to responsibility for competition, in: H. Ullrich (ed.), The Evolution of European Competition Law: Whose Regulation, Which Competition? (2006), 224–232, 225 f.; *F. Schuhmacher*, Die stärker ökonomisch orientierte Anwendung der Wettbewerbsregeln, in: S. Griller (ed.), Die europäische Wirtschaftsverfassung de lege lata et ferenda (2007), 193–219, 215; *D. Zimmer*, Der rechtliche Rahmen für die Implementierung moderner ökonomischer Ansätze, Wirtschaft und Wettbewerb 2007, 1198–1209, 1206; *W.-H. Roth*, The "More Economic Approach" and the Rule of Law, in: Schmidtchen et al. (n. 57), 37–57, 54 ff.; *R. Podszun/S. Kreifels*, Digital Platforms and Competition Law, Journal of European Consumer and Market Law 2016, 33–39, 34 ff.

sively reflects economic findings in each individual case, serves legal certainty and can be enforced at reasonable cost.[59]

The term "more economic approach" is slightly misleading as it is not necessarily about "more" economics but also concerns the integration of modern economic theories of harm into the interpretation and application of the law.[60]

A first characteristic of this new approach is a stronger emphasis on consumer welfare as the primary goal of competition law. This change counters the often alleged critique that European competition law prohibits pro-competitive practices in order to protect competitors instead of competition.[61]

Second, the European Commission stresses the need to analyse the actual or at least the likely effects of the conduct in question on the market and consumers to a greater extent than was done before ("effects based approach"). Critics have often alleged that under EU law, a "formalistic" approach prevailed,[62] especially with regard to the block regulation exemptions[63] and the field of exclusionary conduct.[64] Merely looking at the form of conduct has the danger that pro-competitive conduct can be banned although it benefits consumers and competition.

Third, the EU Commission seeks to analyse efficiency considerations in more detail and avoid far-reaching presumptions of illegality. On a more theoretical level, modern insights of competition economics should be integrated into the framework, and on a more practical level the advantages for consumers and competition must be taken into account when judging particular conduct ("efficiency defence").

At an institutional level, the European Commission established the position of chief competition economist within the Directorate-General for Competition; this individual – together with his or her team – is charged with providing sound economic advice for general policy initiatives as well as with regard to

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[59] *Wurmnest* (n. 48), 230.

[60] *D. Zimmer*, Law and Economics im Recht der Wettbewerbsbeschränkungen, in: Studienvereinigung Kartellrecht e.V. (ed.), Kartellrecht in Theorie und Praxis: Festschrift für Cornelis Canenbley zum 70. Geburtstag (2012), 525–535, 533.

[61] On this critique, see *R. O'Donoghue/J. Padilla*, The Law and Economics of Article 102 TFEU (3rd edn., 2020), 89.

[62] See *R.J. Van den Bergh/P.D. Camesasca*, European Competition Law and Economics: A Comparative Perspective (2nd edn., 2006), 1: "For a long time, European competition law was permeated by legal formalism."

[63] See *E. Bueren*, Der "New economic approach" der Kommission für horizontale und vertikale Wettbewerbsbeschränkungen, Wettbewerb in Recht und Praxis 2004, 567–575, 567.

[64] See *Competition Law Forum Article 82 Review Group*, The Reform of Article 82: Recommendations on Key Policy, European Competition Journal 1 (2005), 179–183, 180 ff.; *E. Rousseva*, Rethinking Exclusionary Abuses in EU Competition Law (2010), 200.

case enforcement.[65] At the national level, equivalent positions have been created, for example in the *Bundeskartellamt*.

The "more economic approach" was first applied to restrictive practices under Art. 101 TFEU, with the adoption of block exemption regulations and corresponding guidelines which took greater notice of the potential effects of agreements.[66] With the adoption of the Merger Regulation 139/2004, this approach was also applied to merger control.[67] The new regime introduced the SIEC-test in lieu of the market dominance test without, however, abandoning the latter criterion completely.[68] Furthermore, the analysis is based on forecasting effects of the merger based on empirical models, and an efficiency defence was created, according to which a merger can be cleared despite a dominant position on the market if the companies can show that their merger generates efficiencies which outweigh the adverse effects of the merger on competition.[69] The modernisation process was complemented by adapted guidelines.[70] Finally, the "more economic approach" was expanded to the application of Art. 102 TFEU. As abusive practices of dominant firms are one of the most disputed areas of competition law, it was no surprise that opinions differed significantly on the question of the extent to which the prerequisites for sanctioning such practices should be adapted. After a very intense debate, also occurring within the European Commission, guidance on the Commission's enforcement priorities in applying Art. 102 TFEU to abusive exclusionary conduct by dominant undertakings was adopted.[71]

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[65] On the tasks of the chief competition economist, see *L.-H. Röller*, Economic Analysis and Competition Policy Enforcement in Europe, in: P.A.G. van Bergeijk/E. Kloosterhuis (eds.), Modelling European Mergers: Theory, Competition Policy and Case Studies (2005), 13–26, 16 f.

[66] For details, see *Wardhaugh* (n. 56), 95 ff.

[67] Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation), Official Journal of the European Union 2004 L 24/1.

[68] *D. Zimmer*, Significant Impediment to Effective Competition: Das neue Untersagungskriterium der EU-Fusionskontrollverordnung, Zeitschrift für Wettbewerbsrecht 2 (2004), 250–267, 250 ff.; *A. Christiansen*, Der "More Economic Approach" in der EU-Fusionskontrolle (2010), 84 ff.

[69] See Recital 29 Merger Regulation.

[70] Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, Official Journal of the European Union 2004 C 31/5; on these guidelines, see *Christiansen* (n. 68), 83 ff.

[71] Communication from the Commission, Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, Official Journal of the European Union 2009 C 45/7.

C. Economic insights and the rule of law

What makes life for lawyers very difficult is the fact that mainstream economics constantly evolves and even insights propagated by leading voices in the field may change over a span of time that, from a legal perspective, is relatively short. In addition, competing theories may offer different solutions. The reception of economic knowledge must therefore be understood as a continuous process, and caution should be exercised before broad changes are carried out. Usually, novel economic arguments are first examined by scholars and the competition authorities. Later, these insights may be incorporated into the existing legal framework by the courts, exercising the necessary caution.[72] Once a certain economic concept has found its way into the law, the peculiarities of the rule of law apply ("*Eigengesetzlichkeiten des juristischen Entscheidungsprozesses*"[73]). The interpretation and application of legal rules is based on a degree of stability, as certainty and predictability are key components of the rule of law.[74] As a result, when a decision has been delivered by the highest court, competition authorities and lower courts will apply this precedent (or the rule contained therein) to comparable settings. If it becomes apparent that the economic theory on which a certain legal decision was based might be flawed in light of new insights, the antitrust authorities can correct their sanctioning practice relatively quickly. By contrast, it will take much longer for the courts to depart from an established line of case law. In such a scenario there is however, at least in the long run, no other path than to overrule an established precedent. Otherwise, the law would degenerate into a storage medium for outdated economic theory.[75] Nevertheless, this process of adaptation will always be slower than the development of economic knowledge (and certainly too slow from the perspective of economists).[76]

A further problem is the question of which economic theory enforcers and courts should be relying on. In this context it needs to be underscored that economics is not a "hard" science. Rather all theories are based on assumptions which can produce different outcomes. In addition, some approaches have been developed for general application whereas others can only offer insights in very specific settings. Against this background, lawyers need to pragmatically evaluate the economic arguments in light of the given market circumstances and

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[72] *L.A. Sullivan/W.S. Grimes*, The Law of Antitrust. An Integrated Handbook (2nd edn., 2006), 21.

[73] This expression is attributed to Max Weber, see *H. Fleischer*, Behinderungsmißbrauch durch Produktinnovation: Eine ökonomische und juristische Analyse zum deutschen, europäischen und amerikanischen Kartellrecht (1997), 104.

[74] *Wardhaugh* (n. 56), 40.

[75] *Wurmnest* (n. 48), 234 f.

[76] *Wurmnest* (n. 48), 235.

the facts of the case at hand.[77] Which pieces of economic thought are integrated into the law is thus a genuine legal question.[78]

Competition law cannot focus exclusively on the economic perspective of the individual case but must also keep institutional aspects in mind. Authorities and courts must remain functional. It must be possible to enforce antitrust law within a reasonable time span, and those subject to the law must be able to predict, at least to a certain extent, when their conduct will infringe the law. Thus, legal rules must be framed in a way that courts and administrative bodies can apply them. This not only requires that economic standards of proof are not overly complex, but also that rules are shaped in a way to provide some ex ante guidance on appropriate commercial conduct.[79]

Having said this, it is also necessary to note that the more simply a legal rule is structured, the more its accuracy will decrease, and this can lead to the wrong economic results. Therefore, it is critical to factor in the risks and potential costs to the competitive process that arise from such enforcement errors. Such errors may include over-enforcement by prohibiting pro-competitive conduct (type I error) or under-enforcement by leaving anti-competitive conduct unsanctioned (type II error). The more detrimental a practice is to competition, the more serious the competitive consequences of an economically wrong decision.[80] An approach which incorporates this thinking helps in structuring legal rules even though measuring the precise cost for competition occurring from such errors is not possible.[81]

D. Predatory pricing as an example

1. Two influential cases from the US Supreme Court

Striking the right balance between economic insights and legal needs has been particularly vigorously debated with regard to predatory pricing, i.e. below-cost pricing strategies by firms aimed at driving out or disciplining competitors.[82] This debate was strongly influenced by developments in the US. To

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[77] *H. Fleischer/K.U. Schmolke/D. Zimmer*, Verhaltensökonomik als Forschungsinstrument für das Wirtschaftsrecht, in: H. Fleischer/D. Zimmer (eds.), Beitrag der Verhaltensökonomie (Behavioral Economics) zum Handels- und Wirtschaftsrecht (2011), 9–62, 45.

[78] See, generally, *H.-D. Assmann*, Die Transformationsprobleme des Privatrechts und die Ökonomische Analyse des Rechts, in: idem et al. (eds.), Ökonomische Analyse des Rechts (1993), 17–61, 60; *Fleischer/Schmolke/Zimmer* (n. 77), 45.

[79] *Wardhaugh* (n. 56), 217.

[80] *E.-J. Mestmäcker*, Der verwaltete Wettbewerb: Eine vergleichende Untersuchung über den Schutz von Freiheit und Lauterkeit im Wettbewerbsrecht (1984), 98.

[81] *C. Ewald*, Ökonomie im Kartellrecht: Vom more economic approach zu sachgerechten Standards forensischer Ökonomie, Zeitschrift für Wettbewerbsrecht 9 (2011), 15–47, 19: "rechts- und wettbewerbspolitische Spielräume".

[82] For reasons of space, this chapter does not deal in detail with exclusionary conduct of dominant firms by means of above-cost pricing.

better understand its origins, it is important to consider two leading cases of the US Supreme Court that spurred the economic debate on predatory prices and also had a strong impact on the incorporation of economic insights into legal thinking.

In 1911, the US Supreme Court condemned the Standard Oil Trust for an unlawful predatory pricing strategy. The dominant trust had established ways to quite accurately estimate the production and transport costs of its competitors, and this enabled it to offer its products in all sales regions at prices just below those of its competitors. In some cases these prices were below Standard's own cost of supply. The Supreme Court regarded this pricing policy as anti-competitive and an unlawful market monopolisation.[83]

As undercutting a competitor's prices is, however, the essence of competition, condemning low prices as unlawful has the potential to hamper price competition. An example of such an economically unsound judgment can be found in the US Supreme Court's decision in *Utah Pie Co. v. Continental Baking Co*. of 1967. The case concerned a local price war between a regional supplier of frozen pies and its much larger competitors that operated across the entire US market. The local supplier, which sold its products exclusively in Utah and neighbouring states, held around two-thirds of the relevant market, whereas the three national competitors each had a very small share of the market in Utah. When the three competitors undercut the prices of the local supplier in Utah in an attempt to challenge this dominance, the latter sued them for damages and was successful. Since the national producers deliberately undercut prices and acted with the intention of enlarging their position at the expense of the local supplier, the Supreme Court found the pricing strategy to be unlawful price discrimination.[84] The absurdity of this finding is obvious. By relying on predatory intent inferred from internal statements of the defendants, the Supreme Court protected a medium-sized supplier against competition without explaining why the price cuts were harming competition as a whole and not only the challenged competitor.[85]

2. Competing economic doctrines

Unsound judgments like *Utah Pie* have fuelled calls for a stronger economic justification for the classification of low prices as predatory. Some proponents of the Chicago School even questioned whether predatory pricing should be banned at all. As far back as 1958, *John S. McGee* published an influential article in which he argued that the *Standard Oil Trust* case was wrongly

[83] *Standard Oil Co. of New Jersey v. United States*, 221 US 1 (1911).

[84] *Utah Pie Co. v. Continental Baking Co.*, 386 US 685, 696 ff. (1967).

[85] See the critique voiced by *W.S. Bowman*, Restraint of Trade by the Supreme Court: The Utah Pie Case, The Yale Law Journal 77 (1967), 70–85.

decided.[86] He argued that pricing below cost will not hamper competition but merely harm the firm resorting to such a strategy. Not only will such a step result in the loss of a considerable amount of money during the low price campaign, it also has literally no chance to recoup these losses after having pushed competitors out of the market as new entries will prevent supra-competitive prices. Such a pricing policy is therefore "foolish".[87] This conclusion was seconded by *Roland H. Koller*, whose study of the cases decided up to 1970 concluded that predatory pricing was essentially a myth as it was hardly ever successful.[88] Against this background, *Robert Bork* offered the following summary in his general critique of the US antitrust law enforcement policy:

> "It seems unwise […] to construct rules about a phenomenon that probably does not exist or which, should it exist in very rare cases, the courts would have grave difficulty distinguishing from competitive price behavior."[89]

That predatory prices are always irrational was, however, not supported by the empirical evidence.[90] Despite this, *McGee*'s position remained influential in the economic literature for a long time no major economic theory countered the Chicago School model with a rigorous model as to why it would indeed be economically rational for a market participant to engage in predatory pricing.[91] Things changed significantly in the 1980s with the advent of modern industrial economics and game theory models. Building on the work of *David M. Kreps* and *Robert Wilson*[92] as well as that of *Paul Milgrom* and *John Roberts*,[93] game theory could demonstrate that the use of predatory pricing tactics can pay off for market-dominant companies in various scenarios. Losses sustained by below-cost prices cannot be recouped by later supra-competitive prices alone, but the dominant market player may also benefit from a deterrence effect or from

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[86] *J.S. McGee*, Predatory Price Cutting: The Standard Oil (NJ) Case, Journal of Law and Economics 1 (1958), 137–169.

[87] *McGee* (n. 86), 168: "I am convinced that Standard did not systematically, if ever, use local price cutting in retailing, or anywhere else, to reduce competition. To do so would have been foolish; and, whatever else has been said about them, the old Standard organization was seldom criticized for making less money when it could readily have made more."

[88] *R.H. Koller*, The Myth of Predatory Pricing: An Empirical Study, Antitrust Law & Economics Review 4/4 (1971), 105–123.

[89] *R.H. Bork*, The Antitrust Paradox: A Policy at War With Itself (1978), 154.

[90] See *A. Edlin*, Predatory Pricing (2012), 22 ff., available at https://works.bepress.com/aaron_edlin/74 (last accessed 15 August 2022). *Edlin* concludes (at 24): "What is learned from this empirical evidence? Even if one takes a narrow view of predatory pricing and considers only below cost pricing as candidates for predation, the view that predation is as rare as dragons is not born of the empirical evidence."

[91] *Fleischer* (n. 73), 61.

[92] *D.M. Kreps/R. Wilson*, Reputation and Imperfect Information, Journal of Economic Theory 27 (1982), 253–279.

[93] *P. Milgrom/J. Roberts*, Predation, Reputation, and Entry Deterrence, Journal of Economic Theory 27/2 (1982), 280–312. On these studies, see *Fleischer* (n. 73), 62 f.

disciplining competitors. The – thus far very limited – findings of experimental and behavioural economics confirm that predatory pricing indeed may pay off.[94]

But *Utah Pie* also led the proponents of the Harvard School to develop a more sophisticated standard of analysis. In 1975, *Phillip Areeda* and *Donald F. Turner* published an article which formed the basis of a two-prong test to separate unlawful predatory prices from pro-competitive price-cuts, which was later elaborated in more detail.[95] To succeed, *Areeda* and *Turner* argued, the plaintiff must prove that the predatory firm's prices are for a substantial amount of sales below the relevant measure of cost and that there is a market structure from which the predatory firm can reasonably anticipate to recoup its sustained losses through supra-competitive prices after its rivals have been eliminated. As the relevant measure of cost, *Areeda* and *Turner* suggested average variable cost (AVC) measured over a relatively short time span as a proxy for marginal costs. Even though this two-prong test may at first sight look simple and clear, this proves not to be the case. The allocation of costs into the categories of fixed and variable is to a certain extent based on subjective choices and depends on the time span one looks at. Put simply, in the long run all costs are variable.[96] As a result, many other measures of cost have been proposed, such as average avoidable cost, average total cost and long-run average incremental cost – none of which, however, have overcome the application problems.[97] In addition, basing the recoupment test merely on a calculation of sacrificed losses and measurable future gains does not adequately reflect the (newer) findings of Post-Chicago economics, which argue that the economic viability of a predation strategy can also result from disciplining competitors (even on other markets) or from deterring entry by newcomers.[98]

Summing up, today most economists agree that predatory pricing can make economic sense provided that certain market conditions are met. In the following section, the application of these findings by courts in the US and in the EU are analysed.

3. The reception in the United States

(a) In the US, the economic critique ignited by *Utah Pie* led the Supreme Court to adapt a very strict approach towards predatory pricing. In *Brooke Group*, the

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[94] *Wurmnest* (n. 48), 382 ff.

[95] *P. Areeda/D.F. Turner*, Predatory Pricing and Related Practices Under Section 2 of the Sherman Act, Harvard Law Review 88 (1975), 697–733.

[96] *H. Fleischer*, Gezielte Kampfpreisunterbietung im Recht der Vereinigten Staaten – Der Supreme Court zwischen Chicago School und Post-Chicago Economics, Wirtschaft und Wettbewerb 1995, 796–808, 800 f.; *O'Donoghue/Padilla* (n. 61), 359.

[97] For details see *Wurmnest* (n. 48), 392 ff.

[98] For details see *Wurmnest* (n. 48), 408 ff.

US Supreme Court essentially embraced a price/cost-approach coupled with a very strict recoupment test. These prerequisites apply regardless of whether the action is based on Sec. 2(a) Clayton Act as amended by the Robinson-Patman Act or on the prohibition of market monopolisation as prohibited by Sec. 2 Sherman Act.[99] In *Weyerhaeuser*, a case of predatory buying, this strict test was confirmed in 2007.[100]

(b) With regard to the relevant measure of cost, the Supreme Court did not embrace a certain cost standard, as the parties to the dispute in *Brooke Group* agreed that the relevant measure of cost is AVC.[101] And at the Court of Appeal level the applicable standard is disputed. Many courts rely on standards that are proxies for marginal cost, such as AVC,[102] and regard prices above the average total cost (ATC) as *per se* legal.[103] And though it is disputed at the Court of Appeal level whether prices between AVC and ATC are legal or illegal, even the courts which accept that prices above AVC can in certain instances be unlawful apply very strict standards of proof.[104] All in all, the *Areeda/Turner* price/cost-approach is thus very influential in the US.

(c) Regarding the second prong of the recoupment requirement, it is worth noting that in the earlier *Matsushita* case the Supreme Court had already been very sceptical of successful predation strategies. Referring, *inter alia*, to Chicago School commentators, the court pointed out that "there is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful."[105] Also in *Brooke Group*, the plaintiff lost because recoupment could not be proven. However, this case concerned a very special setting. The dispute concerned a price war in the cigarette industry following the launch of a generic brand by the plaintiff (Liggett, later renamed Brooke Group), a small cigarette producer with a market share of around 3%. This firm sued its competitor Brown & Williamson, which had a market share of around 10%, for damages arising from unlawful predatory pricing. Given that the market share of the defendant was so low, it was hard so see how a price war could damage competition. The market was, however, characterised by a rather stable oligopolistic structure. Liggett therefore argued that the defendant engaged in the low-price policy to obtain a market share that would give it the price leadership in the oligopoly. Once it had secured that position, the price of no-name cigarettes was to be gradually increased in order to make the cheap brands

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[99] *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 US 209, 222 f.

[100] *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 SCt 1069 ff. (2007).

[101] *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 US 209, 222 with n. 1 (1993).

[102] See *Arthur S. Langenderfer, Inc. v. S.E. Johnson Co.*, 729 F2d 1050, 1058 (6th Cir. 1984); *International Travel Arrangers v. NWA, Inc.*, 991 F2d 1389, 1399 (8th Cir. 1993).

[103] *International Travel Arrangers v. NWA, Inc.*, 991 F2d 1389, 1396 (8th Cir. 1993).

[104] For details, see *Wurmnest* (n. 48), 424 f.

[105] *Matsushita Elec. Indus. Co. v. Zenith Radio*, 475 US 574, 589 (1986).

unattractive to consumers and to keep the high profit margins for branded cigarettes. Given the oligopolistic structure in the cigarette industry, the defendant could rely on the behaviour of the other competitors, so that losses from the price war could be recouped through profits in the brand segment. Even though the Supreme Court did not rule out that a recoupment through oligopolistic behaviour was feasible, it underscored the various difficulties of concerted price increases.[106] The majority of the Supreme Court justices therefore found that the evidence presented by the plaintiff was not sufficient to demonstrate the likelihood of such a form of recoupment so that the lower court was right to dismiss the action "as a matter of law" without involving the jury.[107]

(d) US courts deciding on predatory pricing after *Brooke Group* have also relied regularly on the recoupment requirement as a tool to dismiss actions as a matter of law.[108] To understand the procedural implication of this decision, it is worth noting that in the US private enforcement of antitrust law is very strong. The prospect of treble damages coupled with other incentives make claims attractive.[109] Sometimes cases come before the courts that have limited chances of success. Under US procedural law the jury decides on the merits of the claim and – especially – the amount of damages sustained. Before the trial starts the defendant can, however, petition to the court to dismiss the action without proceeding before the jury. Such a motion is granted if the evidence shows there is no genuine dispute as to any material facts such that a fact-finder would not be able to enter a judgment against the party making the motion to dismiss.[110] Deciding a case "as a matter of law" is thus a procedural tool by which judges can strike out apparently unfounded cases. The importance of *Brooke Group* lies in the fact that the hurdle for relying on this instrument was set rather low.

Even though the recoupment test is a barrier that is very difficult to overcome for plaintiffs, courts are nevertheless slowly retreating from the irrationality postulate voiced by the Chicago School. The 10th Circuit has recognised that modern economic thinking has concluded that predatory pricing strategies are much more likely to occur than argued by Chicago economists, so that a slightly more relaxed interpretation of the recoupment test seems in order:

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[106] *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 US 209, 240 ff. (1993).

[107] The three dissenting judges argued that there was considerable evidence of the existence of an unlawful predation strategy such that the action could not be dismissed "as a matter of law" but should have been decided by the jury, see *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp*., 509 US 209, 254 ff. (1993).

[108] For details, see *Wurmnest* (n. 48), 436 ff.

[109] On the US system of private enforcement, see *C.A. Jones*, Private Enforcement of Antitrust Law in the EU, UK and USA (1999), 80 f.

[110] See Rule 56 Federal Rules of Civil Procedure.

"Recent scholarship has challenged the notion that predatory pricing schemes are implausible and irrational. […] Post-Chicago economists have theorized that price predation is not only plausible, but profitable, especially in a multi-market context where predation can occur in one market and recoupment can occur rapidly in other markets. […] Although this court approaches the matter with caution, we do not do so with the incredulity that once prevailed."[111]

(e) Summing up, the reception of economic insights by the courts in the US has led to a test that focuses very much on type I errors. To avoid over-enforcement by prohibiting pro-competitive price cuts, courts have embraced a very narrow test. This caution can be explained in part by the influence of Chicago School thinking, but it seems to me that the particularities of the private enforcement system have played a much stronger role. In addition, novel economic thinking makes its way rather slowly into the court rooms, and as a consequence the chances for harmed plaintiffs to obtain relief from the courts remain very low.

4. The reception in Europe

The discussion in the US also influenced the reception of economic ideas into the law in Germany and Europe. Put simply, the Chicago School did not receive much acclaim in Europe. Thus, the argument that predatory pricing may not harm competition was not strongly voiced on this side of the Atlantic. In addition, as the European Commission only started to sanction predatory pricing abuses by dominant firms in the 1980s, the experiences gained in the US could be considered when shaping the application of the European competition rules. The US approach was not followed. Rather, the Commission and the European courts took a more critical stand on (selective) price cuts by dominant firms. The major differences between the European approach and the US approach can be summarised as follows:

(a) A first difference relates to the reliance on price/cost standards. Even though the *Areeda/Turner* rule was discussed in Europe, the European Court of Justice (ECJ) did not apply it with the same rigour as many of the courts in the US. The ECJ held in *AKZO* that prices of a dominant firm below AVC are to be regarded as predatory. The Court held that a

"dominant undertaking has no interest in applying such prices except that of eliminating competitors so as to enable it subsequently to raise its prices by taking advantage of its monopolistic position, since each sale generates a loss, namely the total amount of the fixed costs (that is to say, those which remain constant regardless of the quantities produced) and, at least, part of the variable costs relating to the unit produced."[112]

This measure of cost is, however, not regarded as the sole benchmark in testing for abusive conduct. Prices within the range of AVC and ATC can also be

[111] *United States v. AMR Corp.*, 335 F3d 1109, 1112 und 1114 f. (10th Cir. 2003).

[112] ECJ, judgment of 3 July 1991, Case C-62/86, ECR 1991 I-3359 para. 71 – AKZO/Commission.

unlawful if a plan for eliminating competitors can be proven. Such prices, explained the Court, "can drive from the market undertakings which are perhaps as efficient as the dominant undertaking but which, because of their smaller financial resources, are incapable of withstanding the competition waged against them."[113]

Integrating "predatory intent", i.e. the plan to eliminate a competitor, into the analysis bears the danger of coming to false conclusions as reached in *Utah Pie*. This risk is heightened if the *AKZO* judgment is read in a way that creates a presumption that a proven plan can be effectively implemented to the detriment of competition without looking further at the specific features of the market.[114] This threat has, however, not materialised because the Commission in its recent decision practice has relied on very strong evidence and not only on isolated statements of the management.[115] If the predatory pricing strategy cannot be proven directly with internal documents, the anti-competitive intentions can also be shown by looking at the specific factors of the pricing policy to show that the low-price strategy makes no commercial sense for the dominant form or is profitable only if it achieves an anticompetitive goal.[116] In this context the effect of the pricing strategy on the market needs to be taken into account to ensure that the low prices actually do harm competition and not only competitors.

It is worth noting that enforcement practice adapted the relevant measure of cost to reflect the unique aspects of the industries in question. The idea behind the adaptation is that dominant firms must be stopped from driving out competitors that are, in principle, as efficient as the predatory firm.[117] Accordingly, the *Tetra Pak* judgment, in which the ECJ held that prices below AVC must always be regarded as unlawful,[118] is too strict[119] and is no longer to be regarded as good law. The Tribunal of First Instance correctly softened this rule to a rebuttable presumption by holding that "prices below [AVC] give grounds for

[113] ECJ, judgment of 3 July 1991, Case C-62/86, ECR 1991 I-3359 para. 72 – AKZO/Commission.

[114] Cf. ECJ, judgment of 3 July 1991, Case C-62/86, ECR 1991 I-3359 para. 72 – AKZO/Commission.

[115] See, e.g., European Commission, decision of 16 July 2003, COMP/38.233, paras. 110 ff. – Wanadoo Interactive.

[116] TFI, judgment of 6 October 1994, Case T-83/91, ECR 1994, II-755 para. 151 – Tetra Pak/Commission; TFI, judgment of 30 January 2007, Case T-340/03, ECR 2007, II-107 para. 197 – France Télécom/Commission.

[117] ECJ, judgment of 27 March 2012, Case C-209/10, ECLI:EU:C:2012:172 para. 38 – Post Danmark/Konkurrencerådet.

[118] ECJ, judgment of 14 November 1996, Case C-333/94 P, ECR 1996, I-5951 para. 41 – Tetra Pak/Commission.

[119] *O'Donoghue/Padilla* (n. 61), 368.

assuming that a pricing practice is eliminatory".[120] The ECJ as well has subsequently hinted that dominant firms may have reasons to price below some measures of cost.[121] In its guidance notice on Art. 102 TFEU, the Commission therefore states that it will usually take the average avoidable cost as a starting point, and it reasons further that only pricing below long run average incremental cost is capable of foreclosing efficient competitors from the market.[122] The applied cost standards thus reflect novel economic insights quite well.

(b) The second important difference in comparison to US law regards the recoupment criterion. The European Court of Justice held in *Tetra Pak* that "in the circumstances of the present case" it is not necessary "to require […] proof that Tetra Pak had a realistic chance of recouping its losses."[123] This is a remarkable statement because the sanctioned dominant firm relied on *Brooke Group* to argue that its prices were lawful[124] – ultimately to no avail. In *France Telecom*, the ECJ confirmed that under EU law no recoupment test is necessary to condemn price cuts as abusive.[125] That does not, however, preclude the Commission from assessing "the possibility of recoupment of losses" when considering the economic rationality of the below-cost pricing.[126] In its guidance notice on Art. 102 TFEU, the Commission also does not advocate a strict recoupment test but instead seeks to prove likely foreclosure effects with structural considerations such as high entry barriers.[127] In addition, the enforcement authority underscores the necessity of taking into account the findings of Post-Chicago economics. For example, the notice refers to the possibility of dominant firms using low prices to influence the expectations of potential entrants or to deter entry by acquiring the reputation of being a predator.[128]

(c) A third difference between US law and the European practice is that under EU law "above-cost" pricing is not *per se* legal, even though such prices

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[120] TFI, judgment of 30 January 2007, Case T-340/03, ECR 2007, II-107 para. 130 – France Télécom/Commission.

[121] ECJ, judgment of 2 April 2009, Case C-202/07 P, ECR 2009, I-2369, para. 111 – France Télécom/Commission; ECJ, judgment of 27 March 2012, Case C-209/10, ECLI:EU:C:2012:172 paras. 40 f. – Post Danmark/Konkurrencerådet.

[122] Communication from the Commission (n. 71), paras. 64, 67.

[123] ECJ, judgment of 14 November 1996, Case C-333/94 P, ECR 1996 I-5951 para. 44 – Tetra Pak/Commission.

[124] The applicant relied on *Brooke Group* before the TFI, but the Tribunal held that "it is not necessary to demonstrate specifically that the undertaking in question had a reasonable prospect of recouping losses so incurred", see TFI, judgment of 6 October 1994, Case T-83/91, ECR 1994 II-755 paras. 143, 150 – Tetra Pak/Commission.

[125] ECJ, judgment of 2 April 2009, Case C-202/07 P, ECR 2009, I-2369, para. 110 – France Télécom/Commission.

[126] ECJ, judgment of 2 April 2009, Case C-202/07 P, ECR 2009, I-2369, para. 111 – France Télécom/Commission.

[127] Communication from the Commission (n. 71), para. 70.

[128] Communication from the Commission (n. 71), para. 68.

have only been prohibited in very specific circumstances.[129] For example, in *Compagnie maritime belge*, a liner conference that was exempted under a block exemption regulation selectively cut prices for transport services for those ships matching the schedule of a newcomer that competed with the conference. The European Court of Justice held that the shipping cartel intended a dual benefit from this strategy: first, to eliminate "the principal, and possibly the only, means of competition open to the competing undertaking" and, second, to "continue to require its users to pay higher prices for the services which are not threatened by that competition".[130] Without generally ruling on the right of the liner conference to meet competition by cutting prices, the Court underscored that

> "the conduct at issue here is that of a conference having a share of over 90% of the market in question and only one competitor. The appellants have, moreover, never seriously disputed, and indeed admitted at the hearing, that the purpose of the conduct complained of was to eliminate [the newcomer] from the market."[131]

Summing up, the reception of economic thinking in Europe has paid much more attention to type II errors. This development has been influenced by various factors. One factor is certainly that the Chicago School never gained much ground in Europe, and therefore the irrationality argument had hardly any impact in Europe. Another factor might be that the law of predatory pricing was shaped much later in Europe, at a time when on the one hand the irrationality argument was already on the decline and on the other hand it was apparent that *Utah Pie* was wrongly decided. In addition, home grown problems have shaped the course of legal development by the courts. Whereas in Europe only dominant firms can be sanctioned for predatory pricing, under US law, the Robinson-Patman Act can apply to non-dominant firms. Coupled with a strong private enforcement system, it seems that safeguards against type I errors are less important under EU law as compared to US law.

IV. Lessons to be learned from the modern interplay between law and economics

A. Lesson no. 1: Competition law must be based on sound legal concepts

There can be no doubt that the early cooperation between law and economics was a disaster for competition and consumers. The *Historische Schule* was

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[129] For details, see *O'Donoghue/Padilla* (n. 61), 404 ff.

[130] ECJ, judgment of 16 March 2000, Joined Cases C-395/96 P and C-396/96 P, ECR 2000, I-1365, para. 117 – Compagnie maritime belge transports/Commission.

[131] ECJ, judgment of 16 March 2000, Joined Cases C-395/96 P and C-396/96 P, ECR 2000, I-1365, para. 119 – Compagnie maritime belge transports/Commission.

beholden to the idea that the economy should be governed by private actors, as had been the case with guilds and other institutions, without adequately considering the devastating effect of such structures on consumers and firms not participating in the arrangement. Over the years, the negative side effects of such economic structures became clearly visible. Unfortunately, even in the Weimar Republic the economic belief in a private ordering of the market remained strong. Although the impact of the *Historische Schule* faded, new economic justifications came up to defend the cartel movement. It would, however, be wrong to blame Germany's failure to develop a modern competition law before World War II on economists alone. The legal profession, too, played its part in the drama. First, lawyers and courts too readily absorbed economic thoughts in favour of a private ordering of the market instead of developing a system to constrain economic power based on the rule of law. As the legal historian *Knut Wolfgang Nörr* has put it:

"We can see that the legal profession sought and found justifications for cartel conduct in neighbouring sciences. Cartels, lawyers were taught, were children of the times, witnesses of modern development, and the dawn of a new economic phase. But is this sufficient to approve cartels from a legal point of view? Were they also from a legal perspective children of their time, did they reflect modern developments in the legal system?"[132]

Unfortunately, these questions were not at the forefront of the legal debate even though the regulation of economic power is a fitting task for the legal profession. Thus, the law can take up insights from other disciplines but only as far legal principles allow. In this respect, legal scholars and courts do not deserve much credit for their actions up to the end of the Weimar Republic. The debate focused too greatly on the rights of cartels to rely on freedom of contract and the so-called internal perspective of the contract, i.e. the relationship between the cartel and its members. Only where the stipulations restricted a contractual party excessively would the contract be declared void. That unlawful restrictions of competition by agreement also have an effect on the market was a legal issue that was discovered rather late; one can even say: too late.[133] Even though the *Reichsgericht* hinted in the Saxon wood pulp cartel case of 1897 that not all cartel agreements are enforceable and named as examples cartels aiming at a "real monopoly" and a "usurious exploitation" of consumers,[134]

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[132] *Nörr* (n. 7), 71: "Wir sehen also, dass die Juristen bei den Nachbarwissenschaften Rechtfertigungen für die Kartelle suchten und fanden. Kartelle, so ließen sie sich gern belehren, seien Kinder der Zeit, Zeugen der modernen Entwicklung, und mit ihnen bräche der Morgen einer neuen Wirtschaftsepoche an. Waren die Kartelle aber mit dieser Begründung rechtlich legitimiert? Waren sie Kinder ihrer Zeit auch unter dem Gesichtspunkt des Rechts, spiegelten sie die modernen Entwicklungen in der Rechtsordnung wider?"

[133] *Schmidt* (n. 47), 181: "Die Außenwirkung wettbewerbsbeschränkender Verträge: ein zu spät erkanntes Rechtsproblem".

[134] RG, judgment of 4 Feburary 1897, RGZ 38, 155, 158 – Sächsisches Holzstoffkartell: "Verträge der in Rede stehenden Art können somit vom Standpunkte des durch die

these exceptions never played a role in later decisions.[135] For too long, courts neglected the external effects of contracts concluded to the detriment of competition as it was difficult to integrate these negative effects into the traditional instruments of private law.[136] Tort law was turned into a sword against certain anti-competitive practices only quite late and thus did not provide comprehensive protection against such conduct. It was consequently scholars like *Böhm* whose writings broadened this narrow perspective by also focusing on the effects of anticompetitive agreements on third parties.

Thus, the key lesson from the beginnings of the interplay between law and economics is that lawyers must develop their own concepts to safeguard legal values in competition regulation.

B. Lesson no. 2: Respect the rule of law

The second lesson to be learned from the evolution of the competition law and economics movement is that the rule of law must be respected when integrating economic insights into competition rules. This is the essence of the debate on the "more economic approach". There is no doubt that economic findings have developed significantly over the last decades. Thus, today the task of the competition lawyer is to refine the prohibitions in a manner that reflects economic thinking but that does so in a way respecting the rule of law. The two central questions are which economic findings should be integrated and how should we structure the tests for the detection of anticompetitive conduct. The integration of economic insights into competition law is an ongoing task, and the outcome also depends on the structure of the law. Different structures of the law (as, for example, encountered in different jurisdictions) may mean that the reception of comparable economic in-sights will nevertheless translate into different rules and different approaches for the assessment of anti-competitive conduct. This was demonstrated above for predatory pricing.

Economists are quick to criticise the decisions of authorities and courts, saying that determinations do not sufficiently reflect economic insights. What these observers often overlook is the necessity to reduce economic complexity to a level that can be handled by litigants and courts. Such simplification is critical in keeping the application of the law manageable and ensuring that competition law can also be enforced through actions by private parties. Some economists might regard this necessity as regrettable. Nonetheless, it is the

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Gewerbefreiheit geschützten allgemeinen Interesses aus nur dann beanstandet werden, wenn sich im einzelnen Falle aus besonderen Umständen Bedenken ergeben, namentlich wenn es ersichtlich auf die Herbeiführung eines thatsächlichen Monopols und die wucherische Ausbeutung der Konsumentenabgesehen ist, oder diese Folgen doch durch die getroffenen Vereinbarungen und Einrichtungen thatsächlich herbeigeführt werden."

[135] *Möschel* (n. 47), 32.

[136] *Schmidt* (n. 47), 181.

price to be paid for the legislature having placed the protection of competition in the hands of the law and entrusted the courts with the task of deciding on the existence of a restriction of competition.[137] Respect for the rule of law demands that rules are shaped in a way that provides some ex ante guidance on appropriate commercial conduct.[138] In the discussion on the more economic approach, the "form vs. effect" dichotomy often did not grasp the necessities of legal regulation. There can also be no doubt that market effects and efficiency gains must be taken into account when judging the lawfulness of a business practice. Requiring excessive economic proof will, however, turn competition law into a blunt sword in the fight against anti-competitive conduct and may undermine the rule of law.[139]

C. Lesson no. 3: Economists on the bench are not the solution

This overview has demonstrated that lawyers and courts sometimes struggle to understand and assess economic insights. Often such insights are presented as expert opinions to support a case or practice. Against this background the question arises whether economists should be appointed to the bench of competition courts.

In this regard it is worth noting that the integration of competition economics into competition law is a rather smooth process in the area of public enforcement. Economists and lawyers ideally work hand-in-hand in competition authorities, and thus economic insights can be competently scrutinised. As legal recourse against decisions of competition authorities is centralised before certain courts, these courts also have access to the necessary knowledge to deal with economic insights.

The proper evaluation and reception of economic thinking is more burdensome when it comes to private enforcement as the (local) jurisdiction of the ordinary courts is less concentrated. Even though economic expert opinions, for example on the amount of damages caused by anti-competitive conduct, have become increasingly frequent in private enforcement actions, it would not in my view make sense to appoint economists – who are not qualified to serve as proper judges – to every competition court. Experience tells us that the assessment of economic evidence is only a small fraction of the judge's role in proceedings, and most decisions concern other issues, often related to civil procedure. The latter issues cannot be decided by an economist who is not also trained as a lawyer. Even though an economist on the bench would help in dealing with expert opinions, this person would be of no help for most decisions to be taken by courts in the course of the proceeding. This would have the effect of increasing the workload for the other judges and counsels against

[137] *Wurmnest* (n. 48), 247.
[138] *Wardhaugh* (n. 56), 217.
[139] *Wurmnest* (n. 48), 256.

the appointment of economists to courts on a large scale.[140] I think further consolidations of jurisdiction and the training of antitrust judges in economic matters are better ways to ensure a sound reception of economic insights. These steps will help the courts to build up the necessary expertise to deal with such economic evidence.[141]

[140] For details, see *Wurmnest* (n. 48), 238 ff.
[141] *Wurmnest* (n. 48), 241 f.