Unilateral conduct by non-dominant firms: A comparative reappraisal

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Introduction

In 2008, an ICN Task Force Report looked into the rules on superior bargaining positions in several jurisdictions worldwide.[1] It found that a few jurisdictions had specific rules on superior bargaining positions, or functionally equivalent competition law or non-competition law rules, but that other jurisdictions, such as the United States, did not have any functionally equivalent rules for unilateral conduct of non-dominant firms.

This contribution addresses two questions, one of a descriptive nature and one of a normative nature.

As a matter of descriptive comparative law, it seeks to revisit the question how Japan, Germany and the United States approach unilateral conduct of firms below the threshold of dominance on the relevant market. In part II of this paper, I use a comparative common-core approach by first outlining the legal formants in the three jurisdictions under review, before considering four typical hypothetical case scenarios that raise questions of unilateral conduct of non-dominant firms. My conclusion in the descriptive-comparative part of the paper is that all three jurisdictions, including the US, apply rules to unilateral conduct of non-dominant firms, often in similar situations.

Large food retailers have historically been in the crosshairs of legislators and enforcers,[2] and increasing concentration in this sector has renewed the calls for protection of allegedly vulnerable suppliers and corresponding enforcement action.[3] This raises the second, normative, question to what extent unilateral conduct by non-dominant firms raises competition issues and requires intervention by competition law that is addressed in part II of this paper.

My conclusion in the normative part of the paper is that unilateral conduct below the threshold of dominance on the relevant market should not be subject to competition-law scrutiny.[4] From a conceptual standpoint, there will rarely be a credible theory of harm from the perspective competition policy. There may be isolated cases in which a credible theory of harm can be advanced. However, the sum of the administrative costs and the costs of type I errors (false

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1 ICN Task Force for Abuse of Superior Bargaining Position [sic], Report on Abuse of Superior Bargaining Position, 7th

2 For the position of chain stores as the 'public enemy' in the US during the Great Depression, see Phillip Areeda & Herbert Hovenkamp *Antitrust Law: An Analysis of Antitrust Principles and Their Application* 3rd edn (Aspen 2006-2013) § 2302.

3 See, for example, European Commission *Green Paper on Unfair Trading Practices in the Business-to-Business Food and Non-Food Supply Chain in Europe* COM(2013) 37 of 31 January 2013; European Commission *The Economic Impact of Modern Retail on Choice and Innovation in the EU Food Sector – Final Report* (September 2014) <http://ec.europa.eu/competition/publications/KD0214955ENN.pdf>; Bundeskartellamt (Federal Cartel Office) *Sektoruntersuchung Lebensmitteleinzelhandel – Abschlussbericht* (30 September 2014), available at <http://www.bundeskartellamt.de/Sektoruntersuchung_LEH.pdf?__blob=publicationFile&v=7>; Bundeskartellamt, 3 July 2014, B2-58/09 – *EDEKA*; Organization for Economic Cooperation and Development (OECD) *Policy Roundtable Buying Power of Multiproduct Retailers* DAFFE/CLP(99)21 (1998), available at <http://www.oecd.org/daf/competition/abuse/2379299.pdf>; OECD *Policy Roundtable Monopsony and Buyer Power* DAF/COMP(2008)38 (2008), available at <http://www.oecd.org/daf/competition/44445750.pdf>; Philippe Chauve & An Renckens 'The European Food Sector: Are Large Retailers a Competition Problem?' (2015) Journal of European Competition Law and Practice (JECLAP) (Advance Access 1 April 2015).

4 See the proviso below for unilateral conduct that aims at collusive conduct, such as invitations to collude; here, I am in favour of continued, in some cases even enhanced, scrutiny.

positives) that result from the application of vague competition law rules such as rules on superior bargaining positions far outweigh the costs from type II errors (false negatives) which result where competition law practices abstinence in the few problematic cases. Also, some of the more egregious cases not caught by competition rules may still be scrutinized from the perspective of contract law, reducing the costs from false negatives even further (but slightly increasing the costs from false positives).

This does not necessarily mean that none of the cases in which rules such as those on superior bargaining decision are applied should be addressed under competition law at all. These rules are often employed in cases in which the firm in the 'superior' bargaining decision is actually dominant on a properly defined relevant market. In some cases in which rules on superior bargaining positions are enforced, the question of dominance is simply not addressed because it is easier for the competition authority or plaintiff to rely on the lower threshold of a superior bargaining position. Moreover, as Professor *Shiraishi Tadashi* has pointed out, in some of the cases addressed under the provisions on superior bargaining positions, the circumstances that prevented the dependent parties from switching to another partner may have been reasons to define the relevant market more narrowly.[5]

This paper accepts Professor Shiraishi's 'baseline' that the factors used to justify the superior bargaining position should give pause for thought and possibly justify a narrower market definition than a first glance would suggest. This, however, is not always the case. Jumping too quickly from the factors that are adduced to justify a superior bargaining position to a market definition that is so narrow as to comprise only the allegedly 'superior' firms risks falling into what is known as the 'toothless fallacy'.

The normatively desirable approach is therefore (1) to require the addressee to be dominant on the relevant market before its unilateral conduct is scrutinized under competition law, but (2) to allow for the possibility that the relevant market may be much narrower than it would at first appear, while (3) not disregarding the principles used in market definition, such as the importance of focussing on marginal consumers rather than those consumers whose elasticity of demand is lowest, or the necessity to consider both demand-side and supply-side substitutability.

Such an approach would mean that a subset of those cases currently scrutinized under the provisions on superior bargaining positions will still be caught, but the analysis will become more rigorous. A final consideration is that a move of abolishing rules on superior bargaining positions could increase the costs from false negatives: where the firm in question is actually dominant, there may be competitive harm from its abusive conduct, but it may escape competition law scrutiny where the competition authority or the plaintiff lacks the necessary information to prove dominance. To the extent this is seen as creating unacceptable costs of false negatives, jurisdictions with rules on superior bargaining positions should consider downgrading the prohibition of abuses of a superior bargaining positions to mere presumptions of dominance. This would reduce the costs of false negatives, but would substantially reduce the costs of false positives, that is, cases where xxx

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[5] Tadashi Shiraishi 'A Baseline for Analyzing [sic] Exploitative Abuse of a Dominant/Superior Position' (2013) (5) *UT Soft Law Review* 1 *at* 6, available at <http://ssrn.com/abstract=2246558>.

Part I: A legal comparison of unilateral conduct rules for non-dominant firms

Scope of the enquiry

This section outlines the rules on superior bargaining positions, or its flipside, economic dependency, in Japan, Germany and the United States. As so often in comparative law, the national terminology and definitions differ between jurisdictions. Accordingly, one has to take care not to use the idiosyncratic legal terminology and definition of superior bargaining positions used in any particular jurisdiction. Otherwise, there would be a risk of missing functional equivalents in other jurisdictions, which may have rules to similar effect, but do not refer to these rules as rules on superior bargaining positions.

Instead, the working definition used for the purpose of the comparison has to start from the 'real world issue' that is at the centre of the research question. The 'real world issue' that is raised by the various rules on superior bargaining or economic dependency provisions is the following. All jurisdictions reviewed here accept that firms are subject to constraints when they enter into (horizontal) agreements with their competitors; there is also agreement that firms may under certain conditions have to take care that they do not enter into vertical agreements with their suppliers or distributors that restrict competition. Moreover, there is a consensus that a firm in a *dominant* position, that is, a firm with a sufficient degree of market power is subject to certain constraints even as far as its unilateral conduct is concerned. The general rule is, however, that *unilateral conduct by non-dominant firms* is unproblematic from a competition policy perspective.

The reason for the general rule is that vigorous competition is more likely to result when firms know that they are acting in a safe harbour provided only (1) they do not enter into restrictive (horizontal or vertical) agreements, and (2) they are not in a dominant position. Within this safe harbour for non-dominant firms, firms are completely free as to their choice of parameters for unilateral conduct, such as choosing or rejecting trading partners, negotiating for different conditions with each of the trading partners, setting their own prices as high or low as they wish, and so on.

The 'real life issue' in this legal comparison, then, is to examine rules that depart from this general rule of a safe harbour for unilateral conduct of non-dominant firms.

Accordingly, for the purposes of the comparison, this paper will consider 'rules on unilateral conduct of non-dominant firms' to comprise all rules on unilateral conduct that apply to firms that do not (necessarily) have a dominant position in the relevant market. This may mean that the rules require some heightened degree of (bargaining) power, or that they do not require *any* degree of market or bargaining power. For the purpose of this enquiry, I exclude rules on unilateral conduct that are meant to prevent collusion between competitors in its incipiency, such as prohibitions of invitations to collude or calls for a collective boycott; even though technically they are rules on unilateral conduct, they ultimately seek to prevent horizontal agreements.

The scope of the forms of unilateral conduct to be examined is more difficult to define in the abstract. On the one hand, there are certain forms of prohibitions on unilateral conduct that have no, or very little, relation to competition policy concerns. For example, non-dominant firms are prohibited from unilaterally selling poisonous food, and few would take issue with taking such conduct out of the 'safe harbour'.[6] In contrast, prohibitions related to 'unfair trade practices' are often very closely related to competition policy concerns, because unilateral conduct by non-dominant firms is prohibited precisely because of its effects on competitive relationships. I have described the conceptual problems in defining the scope of problematic prohibitions on unilateral conduct elsewhere. For the purposes of this contribution, I will employ a common-core approach and focus on four hypothetical case scenarios that exemplify many of the issues typically addressed by rules on superior bargaining positions and other rules on unilateral conduct by non-dominant firms.[7]

Overview of the legal formants on 'unilateral conduct of non-dominant firms'

Japan

Today,[8] the main rules on superior bargaining positions in Japan are found in Articles 19, 2(9) of the Antimonopoly Act (AMA).[9] Article 19 of the AMA prohibits 'unfair trade practices'. Article 2(9)(v) of the AMA includes in the definition of prohibited 'unfair trade practices':

> (v) Engaging in any act specified in one of the following by making use of one's superior bargaining position over the counterparty unjustly, in light of normal business practices:
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> (a) Causing said counterparty in continuous transactions (including a party with whom one newly intends to engage in continuous transactions; the same applies in (b) below) to purchase goods or services other than those to which said transactions pertain;
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> (b) Causing said counterparty in continuous transactions to provide money, services or other economic benefits;
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> (c) Refusing to receive goods in transactions with said counterparty, causing said counterparty to take back such goods after receiving them from said counterparty, delaying payment to said counterparty or reducing the amount of payment, or otherwise establishing or changing trade terms or executing transactions in a way disadvantageous to said counterparty.

The JFTC's 'Guidelines Concerning Abuse of Superior Bargaining Position under the Antimonopoly Act' of 30 November 2010 explain and illustrate the

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6 While the example may look like an *argumentum ad absurdum*, there is still a connection to competition policy concerns. For example, where the definition of 'poisonous' food is set sufficiently arbitrarily, it may be used to exclude competitors from entering a market (genetically modified food?).

7 Below xxx.

8 When referring to older literature, one has to take into account that the applicable rules have slightly changed when the Antimonopoly Act (AMA) was amended in 2009 (Act No 51 of 2009). Before this amendment, the rules on superior bargaining positions were to be found mainly in General Designation of Unfair Trade Practices of 1982, paragraph 14 (see, eg, Akira Inoue *Japanese Antitrust Law Manual: Law, Cases, Interpretation of Japanese Antimonopoly Act* (Kluwer Law International 2007) 77-79; ICN Task Force Report, note 1, *at* 7). Three of the alternatives mentioned in the former paragraph 14 of the General Designation have now been moved to Article 2(9)(v) AMA (see text following this footnote), the remaining designation has moved to No 13 of the General Designation of Unfair Trade Practices of 1982, Public Notice No. 15 of 18 June 1982, as revised with effect from 4 January 2010 (in the following: the 'General Designation').

9 For overviews, see, eg, Sayako Takizawa & Koki Arai 'Abuse of Superior Bargaining Position: the Japanese Experience' (2014) 5 *Journal of European Competition Law* 557; Etsuko Kameoka *Competition Law and Policy in Japan and the EU* (Edward Elgar 2014) 86-95; Hiroshi Oda *Japanese Law* 3rd edn (OUP 2009) 344 ff, 350-351.

enumerated forms of abuse in Article 2(9)(v) AMA, both with actual and hypothetical ('supposed') examples.[10]

These Guidelines also explain when a 'superior bargaining position' exists. It is not necessary for the party to be dominant on the relevant market; it is enough that the party has a 'superior bargaining position' relative to the other (dependent) party.[11] Such a superior bargaining position exists where the second, allegedly dependent, party would have to accede even to 'substantially disadvantageous' requests by the first party, because it would otherwise have 'difficulty in continuing the transaction with [the first party] and thereby [the second party's] business management would be substantially impeded.'[12] Whether or not this is the case is determined by a comprehensive analysis of (1) the degree of the second party's dependence on the first party as measured by the proportion of sales with the first party compared to the total amount of the second party's sales; (2) the position of the first party in the relevant market, as determined by the market share and ranking; (3) the possibility of the second party switching its demand or supply from the first party to another partner, in particular considering transaction-specific investments made by the second party; and (4) other factors, such as the absolute amount of transactions between the first and second party, the growth potential of the first party, the differential in the business size between the first and second party, or the reputational effects for the second party by being associated with the first party's brand.[13]

The Guidelines emphasize that a superior bargaining position may not only exist between a large and small or medium-sized enterprises (SMEs), but also between two large enterprises or two SMEs.[14]

In addition to the conduct enumerated in Article 2(9)(v) AMA, the Japan Fair Trade Commission (JFTC) may designate further conduct as 'unfair trade practices' under Article 2(9)(vi) AMA, namely:

> (vi) Any act falling under any of the following items which tends to impede fair competition [...] other than the acts listed in the preceding items:
> (a) Unjustly treating other enterprises in a discriminatory manner;
> (b) Engaging in transactions at an unjust price;
> (c) Unjustly inducing or coercing the customers of a competitor to deal with one;
> (d) Dealing with another party on such conditions as will unjustly restrict the business activities of said counterparty;
> (e) Dealing with the counterparty by making use of one's superior bargaining position unjustly;

[10] In the following: 'Guidelines on Superior Bargaining Position 2010'; a tentative English Translation is available at <http://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines.files/101130GL.pdf>. A very brief overview of the rules on superior bargaining position is also contained in Part II Chapter 5 of the 'Guidelines Concerning Distribution Systems and Business Practices Under the Antimonopoly Act', last revised 30 March 2015, tentative English translation available at <http://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines.files/150330distribution.pdf>.

[11] Guidelines on Superior Bargaining Position 2010, note 10, *at* 5. But see the criticism of this approach by Tadashi Shiraishi, note 5, (2013) (5) *UT Soft Law Review* 1 *at* 3-6, available at <http://ssrn.com/abstract=2246558>, and below Part II xxx.

[12] Guidelines on Superior Bargaining Position 2010, note 10, *at* 5.

[13] Guidelines on Superior Bargaining Position 2010, note 10, *at* 5-6, with examples from case law *at* 7-9.

[14] Guidelines on Superior Bargaining Position 2010, note 10, *at* 5. Given that the differential in size is a (though not necessarily the decisive) factor in finding a superior bargaining position, it may on the margin be more likely that a large firm will be found to be in such a position vis-à-vis an SME.

(f) Unjustly interfering with a transaction between an enterprise in competition with one in Japan or a corporation of which one is a shareholder or an officer and another transaction counterparty; or, if such enterprise is a corporation, unjustly inducing, instigating or coercing a shareholder or officer of such corporation to act against the corporation's interests.

The JFTC has made designations under Article 2(9)(vi) AMA in the General Designation[15] and in sector-specific special designations, for example for newspapers and large scale retailers in their relationship to their suppliers.[16] In the General Designation, only paragraph 13 refers explicitly to a 'dominant bargaining position'.[17]

However, several other forms of 'unfair trading practices' enumerated in other items of Article 2(9) AMA and in the General Designation also concern 'unilateral conduct of non-dominant firms', such as discriminatory conduct,[18] sales below cost,[19] or refusals to deal.[20] These provisions – while not considered to be part of the rules on 'superior bargaining positions' in Japan – are relevant to the legal comparison in this contribution.[21] They are explained and illustrated in separate Guidelines, such as the 'Guidelines Concerning Distribution Systems and Business Practices Under the Antimonopoly Act', last revised 30 March 2015,[22] or the 'Guidelines Concerning Unjust Low Price Sales Under the Antimonopoly Act' of 2009.[23]

[xxx insert section on Subcontract Act, Service Transactions (http://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines.files/servicetransactions.pdf) and on enforcement practice]

Germany

The rules on unilateral conduct of non-dominant firms, or in the German terminology 'relative and superior market power' (*relative und absolute Marktmacht*), which are today contained in § 20 of the Act against Restraints of Competition have not always been part of the ARC. In the original ARC 1958, there were no rules on economic dependency at all. In 1973, a provision on

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15 Supra note 8.

16 For newspapers, the special designation is the one on 'Specific Unfair Trade Practices in the Newspaper Business' (Fair Trade Commission Notification No 9 of 1999). For retailers, the special designation is the one on 'Specific Unfair Trade Practices by Large-Scale Retailers Relating to Trade with Suppliers' (Fair Trade Commission Notification No 11 of 2005); Takizawa Sayako and Arai Koki indicate that this special designation is now 'de-facto invalid' (Sayako Takizawa & Koki Arai, 'Abuse of Superior Bargaining Position: the Japanese Experience' (2014) 5 *Journal of European Competition Law* 557, 559 in fn 15).

17 Paragraph 13 of the General Designation provides that it is an unfair trade practice to 'caus[e] a corporation which is one's transacting party to follow one's instruction in advance, or to get one's approval, regarding the appointment of officers of the said corporation [...], unjustly in light of the normal business practices by making use of one's dominant bargaining position over the party.'

18 AMA Article 2(9)(ii) (price discrimination) and General Designation paragraphs 3 and 4 (discrimination in other cases than those covered by Article 2(9)(ii) AMA).

19 AMA Article 2(9)(iii) (continuous supply of goods or services far below the cost incurred to supply them) and General Designation paragraph 6 (unjustly low price sales in other cases than those covered by Article 2(9)(iii) AMA).

20 General Designation paragraph 2 (refusal to deal).

21 See also, eg, General Designation 10 (tying) and 11 (exclusive dealing).

22 Supra note 10.

23 Tentative English translation available at <http://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines.files/unjustlowprice.pdf>.

relative market power, similar to what is now contained in § 20(1) ARC, was introduced into the Act. The reason for the introduction was the simultaneous prohibition of resale price maintenance (RPM) for branded goods. The anticipated mischief was that manufacturers of branded goods would *de facto* continue their RPM schemes by unilaterally terminating their agreements with distributors who undercut the former minimum, now recommended, prices. The provision on relative market power was, in other words, an attempt to address the *Colgate* problem – how to reconcile the prohibition of an agreement to adhere to vertically fixed prices with the freedom to terminate distribution relationships unilaterally.

Subsequent revisions of the ARC added more and more restrictive provisions, in particular with regard to relative market power on the demand side and to superior market power in the horizontal relationship, culminating, at least for now, in what is today § 20 ARC with the scope described below.

As in Japan, the German rules on unilateral conduct of non-dominant firms have been rearranged since the ICN Task Force Report was published, without however having been changed in substance since then.

The rules are now essentially contained in one provision, § 20 ARC 2013. § 20 ARC provides for two separate categories of alleged 'market power' below the threshold of dominance, so-called 'relative market power' in a vertical relationship between an undertaking and either its suppliers or customers; and 'superior market power' in the horizontal relationship between a large undertaking and its SME competitors.

Relative market power

The first category, 'relative market power', is the subject of § 20(1), (2) ARC.[24] 'Relative market power' refers to a differential in power in the vertical relationship between a 'powerful' undertaking on the one hand, and its 'dependent' suppliers or customers on the other. The powerful undertaking is prohibited from unfairly impeding dependent suppliers or customers, and from discriminating between them without objective justification, § 20(1) ARC. § 20(2) ARC was specifically introduced to address concerns of demand-side market power and prohibits the so-called 'tapping' of dependent suppliers by 'powerful' customers, that is, requests to grant, or causing the granting of, advantages that are not objectively justified. Some see the purpose of the

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[24] § 20(1), (2) ARC provide (author's translation):

'(1) § 19(1) in combination with § 19 (2) no 1 [scil: the prohibition of abuses by a dominant undertaking, in particular by directly or indirectly unfairly impeding another undertaking or directly or indirectly treating another undertaking differently without objective justification] also applies to undertakings and associations of undertakings to the extent that small and medium undertakings, as suppliers of or customers for a particular kind of goods or services, are dependent on the undertakings or associations in such a way that sufficient and reasonable opportunities to switch to other undertakings are unavailable to the small and medium undertakings (relative market power). The dependence on a customer, in the meaning of the first sentence, of a supplier of a particular kind of goods or services is presumed where this customer is regularly granted particularly advantageous conditions over and above the usual discounts on the price or other forms of consideration which are not granted to equivalent customers.

(2) § 19(1) in combination with § 19(2) no 5 [scil.: the prohibition of abuses by a dominant undertaking, in particular by using its position to request from other undertakings advantages without objective justification, or to cause other undertakings to grant such advantages] also applies to undertakings and associations of undertakings in the relationship to undertakings that are dependent on them.'

Note that, first, the presumption in the second sentence of subsection 1 only applies to the dependence of a customer on a supplier (and not vice versa), and, second, that in subsection 1 the dependent undertaking has to be an SME, while in subsection 2 the dependent undertaking may also be a large undertaking.

'tapping' provision primarily in the distortive effects that the granting of special conditions had on the horizontal relationship between the undertaking with relative market power and its competitors; others extend the protective purpose to the vertical relationship between the dependent supplier and the undertaking with relative market power.[25]

Whether or not relative market power exists is determined decisively by the question whether the allegedly dependent undertaking has 'sufficient and reasonable opportunities to switch to other undertakings' on the relevant product and geographic market. The crucial question is what outside options are considered to be 'sufficient and reasonable'. From a competition policy perspective, it would make sense to consider sufficient and reasonable outside options to exist whenever there is effective competition on the relevant market. This, however, would reduce the scope of § 20(1), (2) ARC to cases of dominance. Clearly, this is not what the ARC has in mind; otherwise, all cases covered by § 20(1), (2) ARC would already be covered by § 19 ARC. Instead, § 20(1), (2) ARC require an enquiry into the sufficiency and reasonability of outside options from the perspective of the allegedly dependent undertaking. On the other hand, however, an allegedly dependent undertaking may not rely on a dependence that is 'self-inflicted'.[26]

This creates the following dilemma: Where there is 'effective competition' on the relevant market, which presupposes that customers or suppliers on the relevant market generally have sufficient and reasonable outside options, and yet the undertaking in question has no sufficient or reasonable outside options, this lack of outside options necessarily must be owed to path-dependencies resulting from choices previously made by the undertaking in question. They could therefore be said to be self-inflicted. The case law seems to resolve this dilemma by stating that such self infliction will be disregarded if the choice leading to the subsequent dependency was also in the interest of the other undertaking, for example where the dependent undertaking makes transaction-specific investments that are desired by the other undertaking.[27]

Relative market power is considered in particular in three case categories:

(1) where a distributor, especially a retail outlet, is dependent on 'must stock products' by a given supplier, in particular where customers expect 'any decent retailer' to stock these products, because they are the 'top brand' or one of a group of top brands (or, conversely, a supplier is dependent on a particular distributor);[28]

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[25] See the discussion in *Bundesgerichtshof* (Federal Court of Justice), 24 September 2002, KVR 8/01, WuW/E DE-R 984 – *Konditionenanpassung* with a case note by Florian Wagner, 'Konditionenanpassung', (2003) *Entscheidungen im Wirtschaftsrecht* 331 § 20 GWB 1/03.

[26] xxx Nothdurft in Langen & Bunte § 20 para 35.

[27] xxx

[28] The paradigm example for this case category is the *Rossignol* case: The ski manufacturer Rossignol terminated a business relationship with a sports shop. The sports shop claimed that customers expected any decent retailer to stock Rossignol skis. Rossignol had a market share of only about 8%, and the Court found there to be 'considerable competition' between suppliers. Nevertheless, the court decided the sports shop depended on stocking Rossignol skis because of the customers' expectations, raised by Rossignol's advertising 'which can give branded goods a specific market position with the result that the customer feels unable to substitute the goods with other goods', and that Rossignol had a duty to deal with the sports shop. *Bundesgerichtshof* (Federal Court of Justice), 20 November 1975, KZR 1/75, (1976) *Neue Juristische Wochenschrift* 801, 802 (an English translation of an extract of the decision is available at <http://www.utexas.edu/law/academics/centers/transnational/work_new/german/case.php?id=1488>). In interpreting this case, one should bear in mind that Rossignol's stated reason for refusing to deal with the sports shop in question was that

(2) where dependence is 'scarcity induced';[29] and

(3) where the dependence is owed to the 'unique relationship' between the supplier and the distributor, in particular where the parties have made transaction-specific investments.

However, this list of case categories is not exhaustive. In particular with regard to relative market power on the demand-side, in particular the relationship between powerful retail chains and their suppliers, none of the categories above are directly pertinent, and the Bundeskartellamt, following proposals in the literature, has proposed to add a further category of 'demand-side dependence'.[30]

In contrast to Japanese law, § 20(1) ARC only protects dependent undertakings if they are SMEs.[31] However, § 20(2) ARC, like Japanese law, protects both SME and large dependent suppliers against requests for advantages by customers with relative market power.[32]

Superior market power

The second category is 'superior market power' in § 20(3), (4) ARC,[33] where the alleged 'market power' is in the horizontal relationship between the undertaking and its small or medium-sized competitors. Undertakings with superior market

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the shop was selling Rossignol skis too cheaply. This case therefore directly involved the mischief which the legislator had sought to avoid by introducing the prohibition, namely the circumvention of the prohibition of resale price maintenance by unilaterally cutting off undertakings that undercut the recommended resale prices. See above xxx.

29 The paradigm example, which was already mentioned in the report accompanying the introduction of the provision on relative market power (*Bundestagsdrucksache* 7/765 *at* 10), was the supply of independent petrol stations during the oil crisis. Because independent petrol stations in an oil crisis have no sufficient outside options, vertically integrated petroleum companies were said to have a duty to apportion the available supplies in a non-discriminatory manner between its own branded petrol stations and independent petrol stations.

30 See, eg, Bundeskartellamt, 3 July 2014, B2-58/09 – *EDEKA*, available at <http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Entscheidungen/Missbrauchsaufsicht/2014/B2-58-09.pdf?__blob=publicationFile&v=4> (in German); Nothdurft in Langen & Bunte, xxx, § 20 paras 57-63.

31 This was not always the case. From its introduction in 1973 to the 5th Amendment of the ARC in 1989 (Fünftes Gesetz zur Änderung des Gesetzes gegen Wettbewerbsbeschränkungen, 22 December 1989, (1989) *Bundesgesetzblatt* Part I 2486 (entry into force 1 Jan. 1990); see the explanatory memorandum, *Bundestagsdrucksache* 11/4610 *at* 21-22), large dependent undertakings were also protected by the predecessor provision of today's § 20(1) ARC.

32 Again, this was not always the case. Before 2007, the predecessor provision of today's § 20(2) ARC was limited to the protection of dependent SME suppliers. In 2007, the SME-requirement was struck out on a temporary basis; a sunset provision in the 2007 Act led to the reinstatement of the SME-requirement on 1 January 2013, before the 8th Amendment struck out the SME requirement on a permanent basis (contrary to the initial Bill for the 8th Amendment). xxx

33 § 20(3), (4) ARC provide (author's translation):

(3) Undertakings with superior market power vis-à-vis small and medium-sized competitors may not use their market power to directly or indirectly impede such competitors unfairly. An unfair impediment in the meaning of the first sentence exists in particular where an undertaking

1. offers food products [...] below the purchase price, or
2. offers other goods or services more than occasionally below the purchase price, or
3. demands a higher price for goods or services from small and medium undertakings with which it competes on a downstream market for the distribution of these goods or services than the prices it offers itself on the downstream market,

unless there is an objective justification. Offering food products below the purchase price is objectively justified where it helps to sell them sufficiently quickly to prevent the goods from perishing or becoming unsalable, or in similarly serious cases.

(4) Where specific facts give rise to an inference that an undertaking has abused its position in the meaning of subsection 3, it is for that undertaking to refute the inference and to disclose circumstances in its sphere whose pleading is impossible for the competitor in question [...] but easily and reasonably possible for the undertaking.

power are prohibited from selling below the purchase price they paid themselves and from margin squeezing.

[xxx insert sections: § 20(5) ARC; UWG; enforcement practice; § 20 ARC: public enforcement – administrative/fines procedure, private enforcement; § 3 UWG private enforcement)

United States of America

According to the ICN Task Force Report, the United States' response to the questionnaire was adamant that the US had neither specific provisions on abuses of superior bargaining positions, nor any provisions in its competition law or general legal provisions that would be applicable to abuses of superior bargaining positions.[34] Further, the US response was clear that controlling unilateral conduct below the threshold of dominance would be bad policy.[35]

This is arguably due to response bias: the question, which explicitly sought functional equivalents to provisions on abuses of superior bargaining positions, was apparently misunderstood. It is true that there is no separate provision in US antitrust law which deals specifically with abuses of a position with some level of market or bargaining power below the threshold of monopoly power, or at least a dangerous probability of acquiring monopoly power. And yet, there are numerous provisions that apply to situations in which jurisdictions such as Japan or Germany would apply their provisions on abuses of superior bargaining positions.

Some situations may be caught by § 5 FTC Act. Others may fall under the Robinson-Patman Act. Yet others may fall under sector-specific or general Franchisee Protection Statutes, either under federal or under state law. State law also provides for various sales-below-cost (or even sales-below-cost-plus-markup) statutes. *[xxx expand]* These functional equivalents will be discussed in the context of the hypothetical case scenarios in the following section.

The case scenarios

1. P is a medium-sized supplier of car parts, and has for the past 30 years supplied parts to the large car manufacturer C, which accounts for 60 per cent of P's sales, and to the smaller car manufacturers D and E, which account for 20 per cent of P's sales each. For some of the car parts, P has made investments in transaction-specific equipment that have not yet amortized. On the selling market for cars of the type in question, C has a market share of 15 per cent; D, E, F, G, H and I have about 10 per cent each, with the remainder being dispersed among smaller customers. The car manufacturers' requirements for car parts are proportional to their shares on the market for selling cars. P is considered a reliable supplier by its customers in part because its car parts are used by the market leader C.

[34] ICN Task Force Report *at* 10.
[35] ICN Task Force Report *at* 17.

When negotiating the renewal of the distribution agreement, C informs P that P has to grant C a 'volume discount' of 20 per cent, even though C has received reliable intelligence that D and E receive a discount of only 5 per cent, and even though C knows that the greater volume of its orders at most leads to additional cost savings in the magnitude of 5 percentage points. P sees no other way than to agree and puts the scheme into practice.

In all jurisdictions, the first question would be whether the car parts for the different car manufacturers belong to the same product market. If this were not the case, C would be a monopsonist for the demand of 'car parts for C cars', and the various provisions on abuses of dominant positions would apply. Assuming, however, either that the car parts are sufficiently identical to be interchangeable from the buyers' perspective, or that suppliers could sufficiently easily switch their production processes for the car parts for all manufacturers to be in the same product market, C's market share of 15 per cent on this market would prevent a finding of dominance. Accordingly, the question arises whether the jurisdictions have applicable rules on unilateral action of non-dominant firms.

In Japan, C would very likely be considered to be in a superior bargaining position relative to P due to (1) the high proportion of P's sales that are made from transactions with C, (2) the fact that C is the car manufacturer with the highest market share and accordingly has a 'high ranking'; (3) the transaction-specific investments, (4) the size differential between C and P, and (5) the fact that P's reputation is partly based on its association with C.

It is possible that demanding the 20 per cent discount would be considered an abuse of C's superior bargaining position. C has arguably made use of its 'superior bargaining position over the counterparty unjustly, in light of normal business practices, ... reducing the amount of payment, or otherwise establishing or changing trade terms or executing transactions in a way disadvantageous to said counterparty' (Article 2(9)(v)(c) AMA).

This conclusion is not entirely free from doubt: the Guidelines mostly discuss unilateral ex post opportunism contrary to an existing contract to which the other party agrees out of necessity – in other words: where, without the coerced *modification* of contractual obligations there would be a breach of contract. Here, in contrast, the parties have negotiated a renewal of their agreement, that is, they are not presently under any contractual obligations. However, Article 2(9)(v)(c) AMA covers both 'changing' *and* 'establishing' terms, and under the heading 'unilateral decision on a consideration for transactions', the Guidelines do not seem to require that there is a contract currently in place.[36] According to *Shiraishi Tadashi*, there is a consensus among 'practitioners and scholars [...] that the majority of cases fall into one of two categories of abuse [...]. The first category is, to be sure, a contractual breach or "unforeseeable disadvantage". [...] The second category is "excessive disadvantage" for future

[36] Guidelines on Superior Bargaining Position 2010, note 10, *at* 28; see also the hypotheticals [4]-[6], ibid, *at* 30, although the facts are not sufficiently detailed to give an unambiguous answer. If the provisions only applied to renegotiations during the duration of an existing contract, there would be an obvious incentive for parties with superior bargaining powers to negotiate short-term contracts. See xxx. For examples of ex post unilateral price reductions contrary to an existing contract, see, eg, the *Sanyo-Marunaka* and *Toys'R'Us* cases, discussed in Takizawa & Arai, note 9, (2014) 5 *JECLAP* 557, 558-9 and passim.

trade. [The Sumitomo Mitsui Banking Corporation (SMBC) case] is an example of excessive disadvantage because SMBC made the unwanted tie a condition of receiving a *new* loan.'[37]

Whether the request for a 20 percent 'volume discount' would constitute an abuse is 'determined after comprehensively considering the method for deciding on the consideration, such as whether or not the entrepreneur conducted sufficient discussions with the transacting party when deciding on the consideration, as well as whether or not the consideration is discriminatory in comparison to the consideration for other transacting parties, whether or not the consideration is lower than the transacting party's purchase price, the difference between the normal purchase price or selling price, and the supply-and-demand relationship of the goods or services subject to the transactions.'[38] There is no abuse where the request is motivated by a meeting-competition constellation or where the consideration is a 'just reflection on the difference in the trade terms.'[39] In C's case, it would appear that there was no sufficient discussion between C and P,[40] and the 20 per cent discount exceeds the 'just reflection on the difference in the trade terms', because the higher volume is said to justify a volume discount of at most 5 percentage point over and above the 5 per cent granted to D and E, i.e. 10 per cent.[41]

[xxx to be inserted: Germany (§ 20(2) ARC?) & US (Robinson-Patman Act; *Gorlick Distribution Center*) plus the following examples:

2. P is a producer of confectionery. 50 per cent of its sales go to a large supermarket chain (S), which has a 15 per cent market share on the retail level. When S merges with a small competitor (with a 5 per cent market share), S asks P for a 'wedding present' – a retroactive rebate of 10 per cent on all sales in the past year. [Japan: ASBP(+); Germany: Konditionenanpassung & EDEKA]
3. D has been a car dealer exclusively for the car manufacturer C for the past 30 years. C plans to restructure its distribution network to direct sales, and terminates the dealership agreement with D with a notice period of one year.
4. S is a large supermarket chain with a 20 per cent market share. S competes with various 'Mom and Pop stores' in the neighbourhood and other supermarket chains. S offers its organic milk for US$1 per litre, even though the it buys the milk from its dairy processor for US$1.50 per litre. Mom and Pop stores buy for US$1.80 per litre due to the smaller quantity they require.]

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[37] Tadashi Shiraishi 'A Baseline for Analyzing [sic] Exploitative Abuse of a Dominant/Superior Position' (2013) (5) *UT Soft Law Review* 1 *at* 6, available at <http://ssrn.com/abstract=2246558> (emphasis added). Similarly Takizawa & Arai, note9, (2014) 5 *JECLAP* 557, 561 (also using the dichotomy unforeseen disadvantage/foreseeable 'remarkable disadvantages')

[38] Guidelines on Superior Bargaining Position 2010, note 10, *at* 29.

[39] Guidelines on Superior Bargaining Position 2010, note 10, *at* 29.

[40] For the importance Japanese authorities put on the (procedural) element of discussion between the parties in order to be able to find (excessive) disadvantage without having to delve too deeply into the substantive disadvantage see Shiraishi, note xxx, (2013) (5) *UT Soft Law Review* 1 *at* 6-7, citing the TEPCO case xxx.

[41] It is possible that the fact that the price discrimination (the price between P and C differs from the prices between P and D, and P and E, respectively) is also taken into account. See text accompanying note 38 and example [6] in Guidelines on Superior Bargaining Position 2010, note 10, *at* 30. The Guidelines mention discrimination as a factor, but it is not clear whether they consider only price discrimination *by C* (the entrepreneur in a superior bargaining position), or also the case where, as here, the party in a superior bargaining decision (C) induces price discrimination by the dependent party (P).

Part II: Should unilateral conduct by non-dominant firms be subject to competition law?

Error costs compared

Subjecting unilateral conduct to competition law scrutiny is always costly, because procompetitive conduct may falsely be categorized as anticompetitive (false positive), or because the uncertainty about the standard or the mere possibility of a false positive may chill conduct that would have been procompetitive. Prohibiting or chilling procompetitive conduct leads to competitive harm; competition law can become self-defeating.

This is true even in the case of competition law scrutiny of unilateral conduct of *dominant* firms. In the case of dominant firms, however, there would also be a high cost to refraining from scrutinizing unilateral conduct. While we want the dominant firm to compete vigorously, we want to avoid exclusionary (or possibly exploitative) conduct. The scrutiny of unilateral action is always torn between the Scylla of false positives, in which case procompetitive conduct is prohibited or chilled, and the Charybdis of false negatives, in which case competitors may be excluded and competition restricted.

In the case of *non-dominant* firms, however, it is very unclear at best what the competitive harm of inaction would be. There are clear downsides but no upsides.

Sales below cost

This is most clearly the case where prohibitions of sales below costs are concerned. Even in the case of predatory pricing by a dominant firm it is sometimes argued that while consumers benefit from the low prices during the predation period, it is far from certain that the scheme will ultimately be successful, so that it may never come to the recoupment stage or to consumer harm.[42] Still, however, there is at least a plausible theory of harm: if the dominant firm's scheme does succeed, competitors would be excluded, competition would suffer, and consumers would ultimately be harmed. Competition law regimes try to balance the pros and cons carefully in these predatory pricing cases.

The calculation changes dramatically where sales below costs of non-dominant firms are concerned. First, the lower the threshold of market power, the higher the number of addressees, and the higher the costs of false positives: while a prohibition of predatory prices for dominant firms may chill some price-reductions by firms close to the dominance threshold, a prohibition of firms with superior market power will catch many more firms (in particular many supermarkets), and a prohibition of sales below costs without any market share threshold will affect the conduct by every market participant: low pricing will be chilled to the detriment of the consumer. Second, the theory of harm, becomes speculative at best. Most cases of sales below cost concern a loss leader –

42 This is the combined argument from *Matsushita*: '[T]here is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful' and 'cutting prices in order to increase business often is the very essence of competition. Thus, mistaken inferences in cases such as this one are especially costly, because they chill the very conduct the antitrust laws are designed to protect.' Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 589, 594 (1986).

customers are meant to be attracted to a store and do their one-stop shopping there. Overall, the store's costs are covered because the losses from the loss leader are (more than) compensated by profits from the sale of other products.

Because the quasi-predatory-pricing narrative of harm is obviously lacking in persuasiveness, alternative justifications have been advanced. Sales below costs statutes are said to protect suppliers of typical loss leaders such as milk and milk products. Again, however, the argument is unpersuasive: if 'powerful' supermarkets are not allowed to sell below cost, but want to offer milk cheaply, they have to depress their costs – in other words, they have to exert monopsony power to bring prices down. Sales below cost statutes, if anything, hurt suppliers. Yet another alternative theory of harm is the consumer protection narrative: precisely because loss leaders entice customers into the store to buy other products as well, they are said to be 'deceptive'. And yet few consumers would think that because milk is cheap in a store that therefore all other goods have to be cheap as well.

Instead, sales below cost statutes are a form redistribution of money from consumers to sellers. It is a legislative form of restricting price competition. It should be noted that it is not necessarily SMEs that benefit. Because the large retailers usually have lower costs (because of efficiency of scale and possibly monopsony power), it will usually be enough for the large retailers to sell *at* cost to undercut the 'mom and pop' stores. Where the prohibition of sales below cost applies even to the mom and pop stores (which is true in some US states and possibly in Japan, but generally not in Germany, where at least superior market power is necessary), the mom and pop stores are additionally deprived of the possibility to compete at least by selling below their own cost.

Freedom of contract and Coase theorem

While the costs and lack of benefits are particularly clear in the example of sales below cost, similar considerations apply in all the cases of scrutiny of unilateral conduct of non-dominant firms. Ex post control of the content of negotiated contracts impinges on the freedom of contract. Where transaction costs are sufficiently low, free negotiations result in the efficient allocation of resources. Where the freedom to negotiate is restricted, the parties have an incentive to circumvent the restriction. If, for example, retroactive rebates are prohibited, there is an obvious incentive for the parties to contract for short-term contracts. Where the protection of the dependent supplier or distributor becomes too onerous for the firm in a 'superior' position, it may choose vertical integration even in circumstances where, in the absence of the interference from competition law, vertical integration would have been considered inefficient.

Protection of the weaker party, outside options and proper market definition

The protection of the weaker party may seem a worthy goal. Nevertheless, it is surprising that competition legislators and authorities go to great lengths to interfere with the adequacy of consideration where firms in a superior bargaining position are concerned. Even in consumer law, there is no equivalent tendency to interfere directly with the terms of the contract to the same extent. The reason why the legislator presumably goes along with this is arguably to be found in public choice reasons: SMEs have a powerful lobby, and SME arguments additionally sound good to voters (who may not realise that the protection is financed out of their pockets).

The reason why competition authorities play along is, as Professor Shiraishi has put it: 'they can enjoy a loose requirement for prosecuting illegal conduct. They also tend to focus on protecting small- and medium-sized enterprises (SMEs) under political pressure.'[43]

The question really is under what conditions one party is 'weaker' than the other. It would be a mistake to assume that just because one firm is large and the other is small the former need necessarily be more powerful. Whether a firm has a strong or a weak bargaining position does not depend on its size, but on its outside options. Where there is effective competition in the market, even a single consumer may have equal bargaining power to a large retailer. Only where there is no effective competition is there a disparity of 'bargaining power'. Whether or not there is effective competition is determined by the presence or absence of a (single or collective) dominant position in that market. Where there is effective competition, the 'smaller' party has sufficient outside options and is therefore not dependent on the other party.

Conceptually, then, dominance is a necessary condition. Whether dominance exists depends on the area of effective competition – the market definition.

As mentioned in the introduction, Professor *Shiraishi* has argued that in superior bargaining position cases, the market may often have to be defined very narrowly, justifying the result even as an abuse of a dominant position.

He exemplifies this with two examples: the *SMBC* case and the *Seven Eleven* case. In the SMBC case, a bank had tied interest rate swaps to loans for SMEs. The SMEs were said to have had no outside options for loans. From this, the JFTC had deduced the bank's superior bargaining position; Professor *Shiraishi* deduces from the same facts that 'the relevant counterparts were specific SMEs distinguishable from general SMEs, and the relevant market was not the whole loan market, but the loan market for those SMEs captured by SMBC.'[44] Similarly, in the *Seven Eleven* case, a franchisor had imposed an onerous requirement on its franchisees. The franchisees were subject to a one-year post-contractual non-compete obligation and were therefore considered to be dependent by the JFTC. Professor *Shiraishi* considers that '[t]he relevant trading counterparts were Seven-Eleven franchisees, and distinguishable from general convenience store franchisees.'[45]

From a comparative perspective, it is noteworthy that the same result had been achieved in an American franchise case, *Newcal*,[46] precisely based on the lock-in argument proposed by Professor *Shiraishi*.

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43 Shiraishi, note 5, *at* 3.

44 *Ibid*, *at* 5.

45 *Ibid.*

46 Newcal Ind., Inc. v. Ikon Office Solution, 513 F.3d 1038 (9th Cir. 2008), cert. den., 129 S.Ct. 2788 (2009) (Rule 12(b)(6) decision); followed by In re Apple & AT&TM Antitr. Lit., 596 F.Supp.2d 1288, 1302-1306 (N.D. Cal. 2008); distinguished in In re ATM Fee Antitr. Lit., 768 F. Supp.2d 984, 997 (N.D. Cal. 2009) (no monopoly power conferred by alleged lock-in where switching costs were low). For a critical discussion of *Newcal* see Philipp Areeda & Herbert Hovenkamp, 2B *Antitrust Law* 3rd edn (Aspen 2007) with supplement 205-2010 (2013).

However, the label 'lock-in' should not substitute for a proper market definition. As explained above, the difference between 'market dominance' and a 'superior position' is important in those cases in which there is generally effective competition on the market, but some market participants are locked in, for example due to transaction-specific investments.

Simply focussing on the locked in customers and defining the market accordingly would be akin to the 'toothless fallacy' in *United Brands*, which focused on the 'old, the very young, and the sick', who could only eat bananas and could not switch to other fruit, to hold that the relevant market was the market for bananas; or akin to the simplistic approach to aftermarkets without considering the possibility of systems competition.[47]

The question has to be whether the market for *Seven Eleven* franchisees or the market for loans for the locked in SMEs in *SMBC* was worth monopolising. Would it have been profitable to raise prices on the so defined narrow market? First, there is the question if arbitrage would be feasible – if these SMEs could not get loans from other banks, and the bank raised its prices for loans for the locked-in SMEs, would it be possible for an arbitrageur to get a loan elsewhere and offer a new outside option to the (in that case only apparently locked-in) SMEs? Second, and perhaps more importantly, what would the reputational effects be? If the general market for loans is competitive, and new customers can observe that the bank opportunistically takes advantage of locked-in customers, the opportunistic behaviour may not be a profitable venture – provided the proportion of new customers being deterred from entering into a relationship with the bank is sufficiently large.

Summary

To reiterate:

(1) Only in cases where a market is dominated, so that there is no effective competition providing sufficient outside options for the 'weaker' party, is there a credible theory of harm that can justify the (administrative and type I error) costs associated with the control of unilateral conduct.

(2) A finding of 'superior bargaining power' is usually based on factors that constitute or imply a 'lock in', reducing the price elasticity of demand for the locked-in group. These considerations may justify defining the relevant market more narrowly.

(3) However, a lock-in does not *automatically* justify defining the market narrowly so as to comprise only the locked-in consumers. In particular, it is possible that consumers that are not (or at least not yet) locked in and therefore have a higher price elasticity of demand make raising prices on the market for locked in consumers unprofitable. Whether this is the case will depend, among other things, the proportion of locked in to 'free' consumers.

Proof of dominance and superior bargaining positions

Watering down the threshold from market dominance to an ill-defined 'superior position' or 'relative/superior market power' standard is intellectually lazy.

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However, abolishing these lower thresholds and relying exclusively on a finding of dominance may present practical problems. In particular, even in cases in which there actually is market dominance and where a credible theory of harm can therefore be advanced, it may not always be possible for the plaintiff or authority to *prove* dominance. This could lead to significant type II error costs. One of the reasons why the concept of relative market power was introduced in Germany was precisely to enable private enforcement: while private plaintiffs are able to demonstrate why they are dependent on an undertaking with relative market power, they will often lack the information necessary to prove dominance on the relevant market, in particular in light of the weak disclosure regime in German procedural law.

If this, however, is the motivation for retaining the lower thresholds, then they should be reduced to mere prima facie indicia or presumptions. If the intention is to allow enforcement only in cases of actual dominance, then it should always be open to the 'relatively powerful' firm to prove that it is not dominant.