

**EU ENLARGEMENT TOWARDS CARTEL PARADISE?
AN ECONOMIC ANALYSIS OF THE REFORM OF
EUROPEAN COMPETITION LAW**

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Abstract

In this paper the reform process of European procedural competition law shall be analyzed from a law and economics perspective, starting with the famous Regulation 17 and ending with Regulation 1/2003 which will enter into force in May 2004 (and will be immediately applicable in the new Member States). The focus lies on the system switch from a centralized authorization system to a system of decentralized ex post control with a broader scope for private court actions. It will be analyzed in how far the system switch affects overall efficiency. Finally, it shall be examined in how far specific provisions of Regulation 1/2003 can contribute to enhancing the efficiency of the procedural law.

Keywords: Regulation 17/62, Regulation 1/2003, Reform of EU competition law, Optimal law enforcement, Notification system, Legal exception system, EU cartel policy.

JEL classification: K21, K42, L40.

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1. Introduction

On 16 December 2002 the Council of the European Union adopted Regulation 1/2003¹ which fundamentally reforms the enforcement mechanism of European competition law as previously laid down in Regulation 17/62.² The adoption of Regulation 1/2003 is the final result of a discussion process within the European Union that has been going on for several years. The reform is widely regarded as one of the most important in the history of European competition policy.³

In this paper, I will first briefly describe the legal framework of the European cartel policy and explain the underlying economic arguments. Then an overview of the reform process and the intense discussion that followed the Commission's White Paper shall be provided.

The focus of this paper is an economic analysis of the implications caused by the switch from a centralized authorization system (as under Regulation 17) to a system of legal exception with decentralized enforcement (as under Regulation 1/2003). Different enforcement mechanisms will be compared with regard to their overall efficiency effects. Policy-makers have the choice between ex ante control through screening, and deterrence through ex post control. Irrespective of this choice, the law enforcement can be implemented in a centralized or in a decentralized way. Furthermore, cartel law can be enforced through administrative agencies or through private court actions. In order to assess the advantages and disadvantages of each choice, the relevant impacts for the concerned actors shall be determined and compared.

In the final section, it shall be analyzed whether the system switch underlying Regulation 1/2003 actually is an improvement and in how far additional procedural provisions contained in the Regulation affect the overall efficiency effect.

2. Legal Framework for EU Cartel Policy

The basic provisions of EU competition law can be found in Art. 81 and 82 of the EC Treaty (ECT) and the Merger Control Regulation.⁵ Art. 81 deals with restrictive

¹ Council Regulation (EC) No. 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, *Official Journal of the European Communities* (hereafter *OJ*) L 1, 04.01.2003, pp. 1-25.

² Council Regulation (EEC) No. 17/62 of 6 February 1962: First Regulation implementing Articles 85 and 86 (now 81 and 82) of the Treaty, *OJ P* 013, 21.02.1962, pp. 204-211.

³ See for example Ehlermann (2000), p. 537; Gustafsson (2000), p. 159; Todino (2000), p. 348; Wißmann (2000), p. 123.

⁴ All references to Articles of the EC Treaty refer to the consolidated version according to the Amsterdam Treaty. Art. 81, 82 correspond to Art. 85, 86 of the Rome Treaty.

agreements and practices of a group of undertakings, so-called cartels, whereas Art. 82 concerns the abuse of a dominant position by a single undertaking or a group of undertakings (collective dominance). Since the reform of Regulation 17/62 does not affect European merger control and only slightly concerns the application of Art. 82, the focus of this paper lies on the reform of the implementation of EU cartel policy.

2.1 Art. 81(1) ECT

Art. 81(1) demands that “[...] all agreements between undertakings, decisions by associations of undertakings and concerted practices⁶ which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market [...] shall be prohibited”. It follows a non-exhaustive list of such restrictive practices: (a) price-fixing or fixing of trading conditions, (b) quantitative restrictions, (c) market sharing, (d) discrimination of undertakings in order to reduce their competitiveness, and (e) tying agreements. According to Art. 81(2) such agreements or decisions are automatically null and void.

The condition that restrictive practices “may affect trade between Member States” serves to draw the borderline between the application of national competition law and EU competition law. When there is no potential effect on cross-border trade, only national competition law can be applied. However, the European Court of Justice (ECJ) has interpreted this notion in a very broad manner. In the *Brasserie de Haecht* judgment the ECJ stated that “[...] it must be *possible* for the agreement, decision or practice [...] to *appear to be capable* of having *some* influence, *direct or indirect*, on trade between Member States [...]”.⁷ Whenever cross-border trade might be affected, EU competition law and national competition laws can be applied concurrently, however the ECJ emphasized the supremacy of EU law over national law.⁸

The prohibition of cartels is grounded on the fact that market forces can have destructive effects on competition. Collusion between undertakings can enable them to charge higher prices and restrict quantities thereby allowing firms to earn higher profits (to the detriment of consumers) than in a perfectly competitive environment. Apart from the redistribution of surplus from consumers to producers the result is a welfare loss due to a too small quantity supplied (deadweight loss). The effects of a

⁵ Council Regulation (EEC) No. 4064/89 of 21 December 1989 on the control of concentrations between undertakings, *OJ L* 395, 30.12.1989, pp. 1-12.

⁶ For the sake of simplicity “agreements, decisions and concerted practices” will hereafter be referred to as “restrictive practices”.

⁷ Case 23/67 *Brasserie de Haecht v. Wilkin-Janssen* [1967] *European Court Reports* (hereafter *ECR*) p. 407, at p. 415, emphasis added.

⁸ Case 14/68 *Walt Wilhelm and others v. Bundeskartellamt*, [1969] *ECR* p. 1 et seq. at paras 3-6.

cartel are thus comparable to those of a monopolistic market. Competition law aims at prohibiting such restrictive practices in order to eliminate sources of inefficiencies.⁹

For the most serious infringements which have as their *object* the restriction of competition, such as price-fixing between potential competitors, market sharing, quantitative output restrictions (quotas) and rigging bids, illegality is presumed by their very nature (similar to the *per se* infringements in U.S. antitrust law).¹⁰ It is thus not necessary to prove that such restrictive practices have a factual negative effect. This can be justified by limiting the costs of a proceeding if such restrictive practices have always or almost always a negative effect on competition.¹¹ It is theoretically possible that an in-depth economic analysis might reveal the fact that a price-fixing cartel had no considerable effect on prices despite the explicit intent of the participants.¹² Since this will be rather exceptional in practice especially if the existence of a cartel over a considerable period of time can be proven, it seems justified to save the costs of a thorough economic analysis.

2.2 Art. 81(3) ECT

Art. 81(3) states that Art. 81(1) may be declared inapplicable for an individual restrictive practice or a category of restrictive practices when the following conditions are met:

- (i) the result is an improvement of the production or distribution of goods or of technical or economic progress,
- (ii) consumers are allowed a fair share of the benefits,
- (iii) the restrictions are necessary in order to obtain the benefits, and
- (iv) do not enable the undertakings to substantially eliminate competition.

Art. 81(3) can be considered as the European equivalent to the American “*rule of reason*” in antitrust cases.¹³ The economic motivation for allowing certain restrictive practices which do not have a restriction of competition as their *object* but only as their *effect* is that social welfare maximization is under certain circumstances realized by limited cooperation between undertakings and not by perfect rivalry.

⁹ See Posner (1998), pp. 309-347; van den Bergh/Camesasca (2001), p. 5, p. 191 et seq.

¹⁰ See van den Bergh/Camesasca (2001), p. 193-195.

¹¹ See Meese (2003), p. 92-93.

¹² Pointed out by van den Bergh/Camesasca (2001), p. 195.

¹³ See European Commission (1999), p. 17 at para 57; van den Bergh/Camesasca (2001), p. 203; The *rule of reason* contains a three-step test: 1. is there any tangible anticompetitive harm? 2. are there pro-competitive benefits that outweigh the harm? 3. is there an equally beneficial but less restrictive alternative? See Meese (2003), p. 79, pp. 94-113.

Examples of such restrictive practices are joint research and development activities, production and specialization agreements, purchasing agreements, commercialization and environmental agreements.¹⁴ Art. 81(3) therefore constitutes a cost-benefit analysis of the pro- and anti-competitive effects of such restrictive practices.

2.3 Regulation 17/62

Art. 83(1) ECT empowers the Council to lay down the details on how Art. 81 and 82 are to be implemented. In 1962 the Council adopted Regulation 17/62 in which these details are formulated.

The allocation of competencies is defined in Art. 9 Reg. 17/62. It empowers the Commission to apply Art. 81(1) and 82 ECT and allows their application by the national competition authorities (NCAs) as long as the Commission has not initiated its own proceedings. Regulation 17 does not mention any competencies of national courts, however the European Court of Justice has applied the doctrine of direct effect on Art. 81(1) and 82 ECT whereby national courts have the power to apply them directly.¹⁵ The power to issue an exemption decision pursuant to Art. 81(3) on the other hand is granted solely to the Commission.¹⁶ In the literature this exclusive competence is called the Commission's *exemption monopoly*.

Regulation 17 specifies the types of decisions that the Commission may take. These are:

- (i) a *negative clearance* decision if there is no infringement of Art. 81(1) ECT,
- (ii) an *infringement* decision in which the undertakings are found in breach of Art. 81(1) ECT and can be ordered to bring the infringement to an end,
- (iii) an *exemption* decision in which the Commission finds that a restrictive practice falls within the scope of Art. 81(1) ECT but decides that the conditions for an exemption pursuant to Art. 81(3) are met,
- (iv) a decision to impose a *fine* for an infringement of Art. 81(1) ECT. The fine can amount to 10 % of the undertaking's worldwide turnover of the preceding business year.

¹⁴ See Commission Notice: Guidelines on the applicability of Article 81 of the EC Treaty to horizontal cooperation agreements, *OJ C3*, 06.01.2001, pp. 2-30 at p. 3, para 10.

¹⁵ Case 127/73 BRT v. SABAM I [1974] *ECR* p. 51 et seq. at para 16.

¹⁶ Pursuant to Art. 9(1) of Regulation 17. National courts may not apply Art. 81(3) unless it is completely obvious that a restrictive practice does not qualify for an exemption, see Case C-234/89 *Delimitis v. Henninger Bräu AG* [1991] *ECR I*, p. 935, at para 50.

In practice, the Commission has in the majority of cases refrained from taking a formal decision and instead issued so-called *comfort letters* which are an informal measure not provided for in Regulation 17. Comfort letters are issued directly by the Directorate General for Competition (DG Comp) stating that the file is closed since no troublesome restrictions are apparent.¹⁷

Art. 4 Reg. 17/62 requires that undertakings notify to the Commission restrictive practices that fall under Art. 81(1) ECT but for which the undertakings seek an exemption decision. For the duration of the proceedings undertakings are granted immunity from fines unless the Commission informs them that a preliminary examination has led it to the conclusion that a restrictive practice does not qualify for an exemption. An exemption can only be backdated to the date of notification. Art. 4(2) Reg. 17/62 contains exemptions from the obligation of notification for certain types of agreements. These agreements can be exempted retroactively to the date when they were concluded.

The Commission can of course start a proceeding not only on the basis of a notification by the concerned undertakings but also on the basis of a complaint (usually by a competitor) or on its own initiative (*ex officio*).

Finally, Regulation 17 contains a number of provisions regarding investigative rights of the Commission and duties of the Member States to cooperate, procedural rights of the parties as well as transitional provisions for restrictive practices already existing when the Regulation entered into force.

2.4 Reform of Regulation 17/62

In the first years after the enactment of Regulation 17, the Commission was confronted with a huge number of notifications of restrictive practices.¹⁸ In order to deal with this problem, the Commission decided to avoid taking formal decisions in every case and instead made intensive use of the above mentioned comfort letters.¹⁹ In 1965, the Council enacted Regulation 19/65²⁰ which empowered the Commission to issue regulations that exempt categories of restrictive practices (so-called *block exemptions*) for types of agreements which by their nature qualify for an exemption pursuant to Art. 81(3). As long as the undertakings implement only those clauses

¹⁷ Either in form of a “negative clearance letter” or an “exemption letter”, see European Commission (1999), p. 12 at para 34.

¹⁸ Since also restrictive practices had to be notified which existed prior to the adoption of Regulation 17, a record number of 37,450 (!) cases was notified in the first five years after enactment, see European Commission (1999), p. 10 at para. 25.

¹⁹ In 2002, only 33 cases were closed by formal decisions as opposed to 330 closed by comfort letters, see European Commission (2003), p. 46.

²⁰ Council Regulation (EEC) No 19/65 of 2 March on application of Article 85 (3) of the Treaty to certain categories of agreements and concerted practices, *OJ P* 036, 06.03.1965, pp. 533-535.

which are legalized by the block exemption, they do not have to notify their agreement to the Commission.

In the following years, the Commission has adopted a number of sector-specific as well as industry-wide block exemption regulations, the most comprehensive one probably being the block exemption regulation for *vertical* restraints.²¹ In order to clarify the application of the block exemptions, the Commission has furthermore issued numerous notices and guidelines. The Commission notice on minor importance (*de minimis* notice²²) sets quantitative thresholds below which also *horizontal* restraints are assumed to have a negligible effect on competition. All these measures have cumulatively reduced the number of notifications considerably.²³

2.4.1 The Commission White Paper

On 28 April 1999 the Commission published its White Paper on the Modernization of the Rules implementing Articles 85 and 86 of the EC Treaty.²⁴ The White Paper proposed a profound reform of the enforcement of European cartel policy. The Commission described Regulation 17 as being designed according to the needs of the early years of the European Community but considers it inadequate for a European Union of 15 Member States and even more so in light of the enlargement process.²⁵ The Commission argued that decentralization efforts have not led to an effective sharing of competence between the Commission on the one hand and the NCAs and national courts on the other hand.²⁶ Furthermore, it is stated that the notification system has consumed a big part of the Commission's resources and has limited the Commission's ability to focus on the most serious infringements of Art. 81 (so-called *hard-core cartels*).²⁷

Therefore the Commission proposed to give up its monopoly to grant exemptions and suggested that the NCAs and national courts should be empowered to apply Art. 81(3).²⁸ Furthermore, the Commission proposed to abolish the notification

²¹ Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, *OJ L* 336, 29.12.1999, pp. 21-25.

²² Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty establishing the European Community (*de minimis*), *OJ C* 368, 22.12.2001, pp. 13-15.

²³ In the years 2000-2002 only 100 notifications were made each year compared to more than 200 per year from 1996-1998, see European Commission (2001), p. 53; European Commission (2003), p. 46.

²⁴ See European Commission (1999).

²⁵ See European Commission (1999), pp. 6-7 at paras 5-9.

²⁶ See European Commission (1999), pp. 13-14 at paras 39-40.

²⁷ See European Commission (1999), pp. 14-15 at paras 43-45.

²⁸ See European Commission (1999), p. 15 at paras 46-47 and pp. 22-24 at paras 83-100.

system altogether and to switch to a system of ex post control (legal exception system).²⁹ In such a system, undertakings have to make a self-assessment of their agreements in order to determine whether they satisfy the conditions of Art. 81(3) ECT.³⁰ Nevertheless, it is proposed that the Commission should be able to issue “positive decisions” stating that an agreement is compatible with Art. 81 ECT. Such positive decisions would not be constitutive (such as exemption decisions) but rather of a declaratory nature.³¹

Other options which aim at improving the authorization system, such as a *rule of reason* test within Art. 81(1), decentralized application of 81(3) by NCAs, restricting the scope of agreements which have to be notified, or procedural simplifications, have been rejected by the Commission.³² In order to minimize the risk of inconsistent application of Art. 81 in a decentralized system, the Commission proposed to create mechanisms for close cooperation and information exchange with NCAs and national courts.³³

2.4.2 The Draft of the New Regulation

In 2000, the Commission published its draft of the new regulation³⁴ whose explanatory memorandum followed the lines of argument already presented in the White Paper. As a new element, Art. 3 of the draft contained the provision that EU competition law and national competition laws should no longer be applied concurrently. Whenever inter-state trade could be affected, EU competition law should be applied *exclusively* by the NCAs and courts. Art. 7(1) of the draft introduced a structural remedy in case of infringement of Art. 81 which would allow the Commission to force undertakings to divest a part of their assets. Art. 8 of the draft empowered the Commission to impose interim measures. A new type of decision is contained in Art. 9 which authorizes the Commission to render commitments of undertakings binding with which they respond to objections of the Commission. Art. 28 gives the Commission general power to issue block exemption regulations.³⁵ Another new element is the possible introduction of an electronic

²⁹ See European Commission (1999), pp. 15-16 at paras 48-49 and pp. 20-21 at paras 76-81.

³⁰ See European Commission (1999), p. 21 at para 77.

³¹ See European Commission (1999), pp. 22-23 at paras 88-89.

³² See European Commission (1999), pp. 17-19 at paras 56-68.

³³ See European Commission (1999), pp. 25-26 at paras 104-107.

³⁴ Proposal for a Council Regulation on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty and amending Regulations (EEC) No 1017/68, (EEC) No 2988/74, (EEC) No 4056/86 and (EEC) No 3975/87, Brussels, 27.9.2000, available at http://europa.eu.int/comm/competition/antitrust/others/modernisation/comm_2000_582/en.pdf

³⁵ Under Regulation 17, the Commission had to be empowered by the Council for each new block exemption Regulation.

registration of agreements. Finally, the draft contains an extension of investigative rights of the Commission and higher penalties for non-compliance.

2.4.3 Regulation 1/2003

On 16 December 2002, the Council finally adopted Regulation 1/2003 which according to its Art. 45 will be applicable as of 1 May 2004 and thus has to be applied by the new Member states immediately after their accession.

Art. 1 Reg. 1/2003 contains the rule that concerted practices which fall under Art. 81(1) ECT are prohibited unless they fulfill the conditions of Art. 81(3) in which case they shall not be prohibited “no prior decision to that effect being required”. It is the last part of the sentence that introduces the legal exception system. Concerted practices that satisfy the conditions of Art. 81(3) ECT are now valid immediately (*ab initio*). The decentralized application of Art. 81 ECT including the power to apply Art. 81(3) is provided in Art. 5 Reg. 1/2003 for national competition authorities and in Art. 6 for national courts.

Article 2 of the Regulation contains rules on the burden of proof. The burden of proof for infringements of Art. 81(1) rests on the alleging party whereas the undertakings have to provide evidence that their restrictive agreements satisfy the conditions of Art. 81(3). The exclusive application of EU competition law as provided in the draft has been removed. Art. 3(1) Reg. 1/2003 now requires that whenever inter-state trade could be affected, national competition law can only be applied concurrently with EU competition law. Art. 3(2) confirms the supremacy of EU competition law which does not apply pursuant to Art. 3(3) to the application of national laws other than competition law.³⁶ The possible introduction of a registration system for agreements as provided in the draft as well as the general power of the Commission to issue block exemption regulations have been removed in Regulation 1/2003. Most of the other provisions have only been slightly modified in comparison with the draft.

2.4.4 Reform Discussion

The Commission’s White Paper and the subsequent draft regulation have caused a very intense discussion mainly among legal experts. German officials as well as a number of scholars have expressed explicit doubts concerning the legality of the proposal.³⁷ They have argued that the switch to a legal exception system would require an amendment of the EC Treaty and could not be enacted by means of a

³⁶ Such as for example national laws on unfair trading.

³⁷ See German Monopolies Commission (1999), at paras 13-21; Deringer (2000), p. 6; Fikentscher (2001), p. 453; Gustafsson (2000), p. 166, 169; Mestmäcker (1999), p. 527; Möschel (2000), pp. 498-499; Paulweber (2000), pp. 30-36; Wißmann (2000) p. 139.

Council regulation. However, the Commission and former officials of the DG Comp did not consider the legality of a legal exception system to be problematic.³⁸ This question will ultimately have to be answered by the ECJ if it will be called by a national court for a preliminary ruling pursuant to Art. 234 ECT.

The Commission's argument that its workload would require abolishing the notification system has been questioned by several authors who argue that a large number of notifications were a problem only in the early years after Regulation 17 was enacted. Recent figures are used in order to demonstrate that the backlog of cases and the number of new notifications have steadily declined.³⁹ Doubts are also raised whether the switch to a legal exception system would at all contribute to a reduction of the workload.⁴⁰

A more general criticism is that the reform is a policy change from a prohibition principle to a (*de facto*) abuse principle that would give equal weight to the freedom of competition and the freedom to form cartels.⁴¹ This would decrease deterrence and encourage restrictive practices. Other authors oppose these critics by stating that in a legal exception system there is no presumption of legality for restrictive agreements and that therefore deterrence would not be reduced.⁴² Furthermore, several authors express doubts whether under a legal exception system the Commission can still issue binding block exemptions as it is expressed in recital 10 of the preamble to Reg. 1/2003.⁴³ If Art. 81 is directly applicable as a whole then its scope cannot be defined by the Commission via a block exemption regulation.

The abolishment of the notification system is regarded unwise by several authors since this would eliminate a valuable source of information for the competition authorities.⁴⁴ Apart from that, a notification system is regarded to serve the public interest by providing information about restrictive practices to other market participants.⁴⁵ The argument of the Commission that a notification system is not useful because it does not help fighting hard-core cartels⁴⁶ has been rejected since

³⁸ See European Commission (1999), p. 8 at paras 12-13; Ehlermann (2000), pp. 553-560; Schaub/Dohms (1999), pp. 1059, 1065-1066; see also Appeldoorn (2001), p. 403.

³⁹ See German Monopolies Commission (1999), at paras 56-58; Fikentscher (2001), p. 447; Möschel (2000), p. 495.

⁴⁰ See German Monopolies Commission (1999), at para 60; Paulweber (2000), p. 42.

⁴¹ See Mestmäcker (1999), pp. 524-525, 528; German Monopolies Commission (1999), at paras 6, 53; Fikentscher (2001), pp. 452-453.

⁴² See Geiger (2000), p. 165; Schaub/Dohms (1999), p. 1066; Wißmann (2000), p. 149.

⁴³ See Deringer (2000), p. 7; Wißmann (2000), p. 142.

⁴⁴ See German Monopolies Commission (1999), at paras 28, 30; Deringer (2000), p. 8.; Möschel (2000), pp. 496-497; Holmes (2000), p. 66; Paulweber (2000), p. 39; Wißmann (2000), p. 149.

⁴⁵ See German Monopolies Commission (1999), at para 29.

⁴⁶ See European Commission (1999), p. 21 at para 77.

hard-core cartels are kept secret under any system. A notification system could nevertheless be helpful for detecting infringements of Art. 81 ECT in the “gray” areas.⁴⁷ Finally, under an authorization system restrictive practices can be prevented ex ante and critical clauses can be modified in a discussion process between the Commission and the concerned undertakings whereas in a legal exception system restrictive practices can only be declared illegal after potential harm has already occurred.⁴⁸

Many authors criticize the loss of legal certainty for undertakings. Whereas they could at least get a relative certainty by obtaining a comfort letter from the Commission under the authorization system, there is no more right for them at all to get an official evaluation of the validity of their agreements.⁴⁹ Only the Commission is empowered to issue positive decisions which the undertakings cannot request. This means that they have to rely purely on their own assessment -which will be difficult if they do not have the relevant market data⁵⁰ - and wait until an NCA decides to examine their case or they are challenged before a court.⁵¹

Another point of criticism is that the decentralized application of Art. 81(3) by courts and NCAs leads to the risk of “forum shopping”.⁵² Decentralization creates the risk that different authorities do not apply Art. 81 in a coherent way. This means that undertakings as well as private litigants will choose the NCA or court that they regard as being most favorable for them. It is also criticized that the mechanisms proposed by the Commission to enhance coordination and cooperation within the network of NCAs and courts are not sufficient to eliminate this risk.⁵³

Furthermore, it is argued that the limited territorial scope of NCA decisions and the limited scope of judgments which are only binding between the parties of the proceeding can lead to multiple proceedings before different NCAs and courts.⁵⁴ This would create a risk of double jeopardy for undertakings thereby significantly reducing

⁴⁷ See German Monopolies Commission (1999), at para 30; Paulweber (2000), p 40.

⁴⁸ See German Monopolies Commission (1999), at para 34; Möschel (2000), p. 497; Wißmann (2000), pp. 148-149.

⁴⁹ See German Monopolies Commission (1999), at para 34; Bartosch (2001), p. 105; Gustafsson (2000), p. 173; Möschel (2000), p. 497; Holmes (2000), p. 59; Paulweber (2000), pp. 37-38.

⁵⁰ See German Monopolies Commission (1999), at para 34.; German Monopolies Commission (2001), p. 49 at para 78; Paulweber (2000), p. 41.

⁵¹ Bartosch (2001), p. 105; see also Wißmann (2000), p. 145.

⁵² See German Monopolies Commission (1999), at para 47; Geradin (2002), p. 24.

⁵³ See Geiger (2000), p. 169; Bartosch (2001), p. 106.

⁵⁴ See German Monopolies Commission (2001), p. 38 at para 61; Kingston (2001), p. 346.; Holmes (2000), p. 62; Paulweber (2000), p. 42; Geradin (2002), p. 24.

legal security. Apart from that, the increased risk of a duplication of proceedings has been criticized for multiplying the transaction costs of the NCAs.⁵⁵

Finally, the dominance of EU competition law over national competition laws as it has been provided by the draft of the new Regulation has been criticized for infringing the *principle of subsidiarity*⁵⁶ and for eliminating *regulatory competition*. Harmonization removes the chance to profit from learning effects created by a variety of different rules.⁵⁷ As a response to this criticism the corresponding Article in Reg. 1/2003 has been amended.

3. Economic Analysis of Enforcement Procedures

3.1 Optimal Law Enforcement

The goal of European competition law should be to encourage only those concerted practices which satisfy the conditions of Art. 81(3) ECT while at the same time all other infringements of Art. 81(1) should be avoided. In order to evaluate how different enforcement mechanisms contribute to guarantee undertakings' compliance with the substantive rules, criteria for optimal enforcement of competition law have to be developed first. Afterwards, alternative enforcement procedures shall be examined in order to assess in how far they satisfy those criteria.

In a perfect world there would be perfect information of all actors (undertakings, law enforcers and third parties, such as consumers and competitors) with respect to the existence and content of restrictive practices, and all actors would have perfect knowledge of the substantial legal rules. Since all information would be publicly available, everyone could distinguish at zero cost and without error whether a restrictive practice constitutes an infringement or not. If furthermore effective sanctions for infringements could be imposed at zero cost and undertakings were rational, no such infringements would occur.

Obviously, reality is far from being perfect. First of all, a substantial *information asymmetry* exists between the undertakings that conclude a restrictive practice and all other actors.⁵⁸ Only the undertakings concerned possess perfect information about the details of their restrictive practice, whereas law enforcers and third parties have to gather this information through a costly procedure.⁵⁹ Not only the law enforcers but

⁵⁵ See German Monopolies Commission (2001), p. 12 at para 15; Geradin (2002), p. 24.

⁵⁶ See Paulweber (2000), p. 36; German Monopolies Commission (2001), p. 15 at para 22.

⁵⁷ See German Monopolies Commission (2001), p. 10 at para 12; van den Bergh (1997), pp. 154-156; van den Bergh/Camesasca (2001), pp. 130-131; Geradin (2002), p. 5.

⁵⁸ van den Bergh (1997), p. 151; van den Bergh/Camesasca (2001), p. 131; Paulweber (2000), p. 41; Geradin (2002), p. 5.

⁵⁹ See Wils (1999), p. 144.

also the undertakings themselves can incur *information costs* of obtaining the relevant data. This is the case if not only the conduct of the undertakings matters for a legal assessment but also facts lying outside their scope, such as market characteristics, or the availability of substitutes.

Secondly, if the substantial legal rules are not clear-cut a costly legal evaluation process is required in order to determine if a certain behavior constitutes an infringement or not. This equally applies to the undertakings who have to hire a legal expert, and to the law enforcers who have to spend human resources on processing the information.

Furthermore, two types of *legal errors* can occur in the evaluation⁶⁰: restrictive practices that satisfy the conditions of Art. 81(3) could falsely be considered an infringement (*type I error*) with the effect that welfare enhancing practices are prohibited, or infringements could erroneously be considered to satisfy Art. 81(3) (*type II error*) having the effect that socially detrimental practices are approved. Apart from this negative welfare effect *ex post*, legal errors also create wrong *ex ante* incentives. If the probability of *type II errors* rises, undertakings could be induced to “give it a try” and hope to remain unsanctioned whereas a higher probability of *type I errors* could discourage socially beneficial practices. The probability of legal errors increases the less complete the available information is and the less familiar a law enforcer is with the substantial rules.

If it is not possible for the undertakings to correctly predict how law enforcers will evaluate a certain practice, they have to bear additional *risk costs*.⁶¹ These risk costs are to be interpreted in an economic sense as the costs of suboptimal decisions taken by risk-averse decision-makers. The larger the number of different law enforcers, the more likely are diverging interpretations of the substantive legal rules, thereby reducing the predictability of the outcome of a proceeding. Finally, if the expected sanctions for an infringement are not sufficiently severe, the concerned undertakings might rationally decide to violate the law and take the risk of bearing the sanction.⁶² Insufficient deterrence will then cause a welfare loss for society.

Given the imperfections of the real world, optimal law enforcement should create adequate incentives for compliance with the law *at the lowest possible cost*. From the set of feasible alternative enforcement mechanisms, that one should be chosen which minimizes the sum of information gathering and processing costs, produces the least legal errors and minimizes risk costs while at the same time sufficiently sanctions violations of the substantive legal rules.

⁶⁰ See Polinsky/Shavell (2000), p. 318; Melamed (1997), p. 94; Wils (1999), p. 144.

⁶¹ See Wils (1999), p. 145.

⁶² See Wils (1999), p. 144.

In the following section, three basic choices concerning the enforcement of legal rules will be examined with respect to the above derived criteria:⁶³

- (i) the timing of law enforcement (*ex ante* or *ex post* control),
- (ii) the level of law enforcement (*centralized* or *decentralized* enforcement), and
- (iii) law enforcement by *administrative* agencies or by *private* court actions.

3.2 Prescreening vs. Deterrence

The first choice that has to be made concerns the timing of law enforcement. Two basic principles can be distinguished: *ex ante* control through prescreening, and deterrence through *ex post* control.⁶⁴ The former principle corresponds to the notification system under Reg. 17/62, whereas the latter corresponds to the legal exception system under the new Reg. 1/2003.

Under the *notification system*, a restrictive practice that fell under Art. 81(1) ECT was void pursuant to Art. 81(2) unless it was properly notified to the Commission and the Commission decided that it satisfied the conditions of Art. 81(3) and could therefore be exempted. Thus the validity of a restrictive practice depended not only on its material content but also on the procedural requirement of notification.

A notification system leads to lower *costs of information gathering* for the law enforcers since the undertakings voluntarily reveal the existence and the content of a restrictive practice. Since an exemption decision can only be backdated to the date of notification, undertakings have an incentive to notify their restrictive practice as quickly as possible in order to avoid civil liability for the time between conclusion and notification (during which the agreement is void) and to benefit from the immunity from fines for the time between notification and Commission decision.

One of the arguments brought against the notification system is that hard-core cartels are never notified.⁶⁵ Indeed, if the restrictive practice is an obvious infringement that could not be exempted, it would not make any sense for the undertakings to notify it to the Commission since this would eliminate the chance of remaining undetected. However, in those cases where it is not clear at first sight whether they constitute an infringement, the information costs of the law enforcer are reduced by notifications. Notifications furthermore provide the competition

⁶³ See also Wils (2002), p. 108.

⁶⁴ See Wils (1999), p. 146.

⁶⁵ See European Commission (1999), p. 14 at para 40.

authorities with information concerning the market structure that might be valuable for the detection of infringements on upstream or downstream markets.⁶⁶

It is surprising to see how the evaluation of the notification system by the Commission has changed within very short time.⁶⁷ While still describing it as “a steady source of information about transactions” which has “triggered a substantial portion of the Commission’s decisions” in the Green Paper on Vertical Constraints in 1997⁶⁸, the Commission made a U-turn in its White Paper in 1999, stating that the notification system only distracted its resources from being spent on investigating the most serious infringements.⁶⁹ As evidence, the Commission provides that only nine cases occurred in 35 years in which a notification led to a prohibition decision without any complaint by a third party being lodged against the restrictive practice.⁷⁰ This figure is however misleading since it suggests that all other restrictive practices which were notified were unproblematic.⁷¹ If one examines the exemption decisions of the years 1999 to 2002, one finds that out of 54 exemption decisions only 14 agreements were granted without modifications, whereas 40 (!) were only approved under obligations or conditions.⁷²

The argument that the Commission’s need for information about market structures is much lower today than 40 years ago and that therefore the notification system is superfluous⁷³ is not very convincing. Since market structures change over time and new markets evolve, the information in the possession of the Commission today might be worthless tomorrow if it is not updated regularly. It seems therefore more appropriate to regard the notification system as an instrument for gathering at least some relevant information at low cost. Although it is true that processing this information requires human resources at the Commission, the significant decrease in the number of notifications from the year 2000 onwards⁷⁴ suggests that these costs were overstated in the White Paper.

The notification system reduces the *risk costs* of undertakings with respect to the validity of their restrictive practices. When the Commission decides to exempt an agreement, this provides the undertakings with legal certainty. Even if the

⁶⁶ See German Monopolies Commission (1999), at para 30; Paulweber (2000), p. 40.

⁶⁷ Pointed out by German Monopolies Commission (1999), at para 32; Paulweber (2000), p. 40.

⁶⁸ European Commission (1997), p. 54 at para 188.

⁶⁹ European Commission (1999), pp. 14-15 at paras 40 and 43-45, p. 21 at para 77.

⁷⁰ European Commission (1999), p. 21, footnote 53; see also Ehlermann (2000), p. 561.

⁷¹ Möschel demonstrates that the Commission’s argument can even be turned upside down by arguing that a low number of prohibitions is the *result* of effective deterrence. See Möschel (2000), p. 496.

⁷² Author’s calculations based on the publication of Commission antitrust cases on the internet: <http://www.europa.eu.int/comm/competition/antitrust/cases/>

⁷³ Ehlermann (2000), pp. 561-562.

⁷⁴ See *supra* note 23.

Commission does not issue a formal decision but only issues an informal comfort letter stating that the conditions of Art. 81(3) seem to be fulfilled this provides the undertakings with at least some legal certainty because the likelihood is significantly reduced that an agreement which has been declared unproblematic by the Commission will be successfully challenged before an NCA or before a court.⁷⁵

Under a *legal exception system* undertakings have to assess the validity of their agreements themselves (with the help of legal experts). The validity of a restrictive practice will only be checked by law enforcers when it is challenged by a competition authority or by third parties before a court. Compliance with the law can thus only be induced by the threat of sanctions. Optimal deterrence requires that the expected sanction for an infringement is higher than the expected benefits that can be obtained by the undertakings from a restrictive practice.⁷⁶ If the expected sanction equals the expected gains, the undertakings would be indifferent between engaging in a restrictive practice or not. However, from a social welfare perspective this result is unsatisfactory. As it has been mentioned above, the socially undesirable effect of a cartel is the creation of a deadweight loss. The harm caused is thus higher than the benefits the undertakings receive and therefore the restrictive practice should be deterred. A possible solution for this problem is to base the sanction on the entire harm caused. This leads to an internalization of the social costs by the undertakings and thus guarantees efficient deterrence.⁷⁷

The *expected* sanction equals the probability of being fined multiplied by the magnitude of the fine. If the probability of detection is smaller than one, the *magnitude* of the sanction has to be increased in order to effectively deter non-compliance with the law.⁷⁸ Whether the feasible sanctions under European competition law which are limited to 10% of the world-wide turnover of an undertaking satisfy this condition can be doubted.⁷⁹ The idea behind the reform of Reg. 17/62 is therefore to increase the *probability* of detecting serious infringements by freeing up human resources at the Commission who before had to deal with processing notifications. Whether this idea will work out depends on whether the legal exception system will allow the Commission to collect more valuable information at lower cost (given that its resource constraint is not altered).

Since the Commission does not receive notifications anymore, one instrument of gathering information is no longer available. This means that the Commission can only collect information by its own investigations (*ex officio*) or by receiving a complaint of a third party. The *information asymmetry* between law enforcers and

⁷⁵ See German Monopolies Commission (1999), at para 34; Holmes (2000), p. 59; Paulweber (2000), p. 37.

⁷⁶ See Cooter (1997), p. 78; Melamed (1997), p. 93; Wils (2002), p. 22.

⁷⁷ See also Wils (2002), pp. 22-24 who provides additional arguments for harm-based sanctions.

⁷⁸ See Polinsky/Shavell (2000), p. 309, Posner (1976), pp. 223-224; Wils (2002), p. 25.

⁷⁹ see Wils (2002), pp. 39-44.

undertakings therefore has to be reduced at considerable *costs*. Moreover, the information asymmetry between the undertakings and third parties, such as other competitors and consumers or consumer unions, persists. Under the notification system this information asymmetry is reduced as well since those notifications which lead to formal decisions are published in the *Official Journal*.⁸⁰

The draft of the new Regulation therefore contained a provision that would have empowered the Commission to set up a registration system under which undertakings were obliged to submit information about the content of their restrictive agreements to the Commission. The information could have been made available to the public via the Internet.⁸¹ This measure would have increased transparency and would have enabled third parties to obtain information about potential sources of harm to them. However, the provision is not contained in Reg. 1/2003 and thus a low cost instrument of reducing information asymmetry has not been used. Compared to the situation under Reg. 17, the probability that a proceeding will be started based on a complaint should therefore be lower under the legal exception system. Thus the resources at the Commission that have been freed by abolishing the notification system now have to compensate for the loss or reduced importance of two sources of information. It seems justified to utter some doubts whether increased ex officio investigations can fulfill this task.⁸²

A second kind of information costs has to be borne by the undertakings themselves. Under a legal exception system, undertakings have to gather a substantially higher amount of information about the market structure and other market characteristics in order to correctly evaluate the effects of their restrictive practices. A self-assessment requires external information that might be difficult to obtain and might require costly external advice by economic experts.⁸³ Therefore at least the undertakings' information costs tend to be higher under a legal exception system.

On the part of the undertakings, the self-assessment under a legal exception system is likely to lead to higher costs due to an increased need for external legal advice. Although drawing up a notification also required some legal advice,⁸⁴ undertakings under a legal exception system have to make sure they do not make any mistakes in evaluating their agreements because this could result in being fined. Still, even the best legal experts will have difficulties to predict how law enforcers will evaluate a certain restrictive practice. The legal certainty that an exemption provided

⁸⁰ The fact that notifications which are closed by comfort letters are not published has been criticized for a lack of transparency, see Wißmann (2000), p. 130; Paulweber (2000), p. 14.

⁸¹ See German Monopolies Commission (2001), p. 48 at para 76

⁸² See also German Monopolies Commission (1999), at para 60; Wißmann (2000), p. 149.

⁸³ See German Monopolies Commission (1999), at para 34.; German Monopolies Commission (2001), p. 49 at para 78; Paulweber (2000), p. 41; Holmes (2000), p. 64.

⁸⁴ Holmes (2000), p. 53 estimates the costs to be around £ 15,000-20,000 per notification.

under the authorization system cannot be perfectly substituted by external legal advice. Therefore it seems plausible that the *risk costs* are higher under a legal exception system.

3.3 Centralized vs. Decentralized Enforcement

A second choice that has to be made concerns the level at which the law should be enforced. Law enforcement can either be centralized at the Commission or the law can be enforced decentrally by authorities of the Member States. Under Reg. 17/62 the enforcement of Art. 81 ECT was allocated in a hybrid way. Whereas the national competition authorities and courts were empowered to apply Art. 81(1), only the Commission was entitled to apply Art. 81(3) and issue an exemption decision. Although this hybrid system theoretically left some scope for application of Art. 81(1) by national authorities, this has only rarely happened.⁸⁵

Apart from the fact that only half of the NCAs were empowered by the national legislator to apply EU competition law,⁸⁶ the exemption monopoly of the Commission is considered to be the main reason for this reluctance of NCAs and national courts. The direct applicability of Art. 81(3) by national competition authorities and courts under Reg. 1/2003 will therefore lead to a switch from a *de facto* centralized law enforcement to a more decentralized law enforcement. In the following section it shall be examined which level is to be recommended from an economic perspective.

If a restrictive practice with cross-border effects originates mainly from undertakings of one Member State or if the effects of a restrictive practice concern mainly one country, it is plausible that the authorities of that Member State are in a better position to collect the relevant information than the Commission.⁸⁷ This does not only concern technical aspects, such as language barriers, but more importantly, a more specialized knowledge of the local market structure.⁸⁸ Therefore the *information costs* of a decentralized enforcement should be lower in such cases.

If instead, a restrictive practice concerns undertakings and markets of a larger number of countries, centralized enforcement is to be preferred since it is necessary to get an overall picture of the implications of a restrictive practice.⁸⁹ Apart from that, centralized enforcement avoids a duplication of proceedings when several Member States are concerned. If NCAs do not share the information they have gathered,

⁸⁵ See European Commission (1999), pp. 13-14 at para 39; Paulweber (2000), p. 15; Geradin (2002), p. 13.

⁸⁶ See Kingston (2001), pp. 341-342; Salord (2000), p. 133.

⁸⁷ See Wißmann (2000), p. 136; Geradin (2002), pp. 5, 19; Wils (2002), p. 143.

⁸⁸ See Geiger (2000), p. 168; Geradin (2002), p. 19.

⁸⁹ See Wils (2002), p. 143.

information costs are multiplied by parallel action.⁹⁰ Under these circumstances, centralized law enforcement leads to lower information costs. Which of the two effects is likely to prevail is hard to say.

The probability of a false assessment of a restrictive practice (a *legal error*) is likely to be higher for decentralized enforcement under the following circumstances:

If *negative externalities* play a role, decentralized enforcement might be inferior since the effects might not be considered adequately by a national authority.⁹¹ For example, if the producers of one Member State have a strong market position within the European Union and they conclude an export cartel that leads to higher prices for the consumers of all other Member States, this is beneficial from a national perspective.⁹² The national producer surplus rises whereas the decrease in consumer surplus affects only foreign consumers. If the authorities of the Member State are subject to a national bias, they might only take the positive effects within their jurisdiction into account while not considering the negative effects abroad.⁹³ A national bias might equally be present at national competition authorities as well as at national courts. The probability of legal errors due to a national bias therefore is higher with decentralized enforcement.

More generally, legal errors will occur more frequently if the law is enforced by authorities that are more prone to the danger of *regulatory capture*.⁹⁴ The risk of regulatory capture depends crucially on the independence of the law enforcer. The more influence political decision-makers have on the enforcement of the law, the higher is the degree of influence that pressure groups, such as producer and consumer unions, have on the outcome of an administrative proceeding. The DG Comp is part of the European Commission which is headed by politicians and therefore the institutional design might favor regulatory capture in the case of centralized enforcement.⁹⁵

The varying political independence of the NCAs among countries has caused critics of decentralized enforcement to point to the risk of “*forum shopping*”. If the institutional design enables national authorities to issue constitutive decisions on the legality of a restrictive practice and these decisions have to be respected by the authorities of other Member States, there is a strong incentive for the undertakings to

⁹⁰ See German Monopolies Commission (2001), p. 12 at para 15; Geradin (2002), p. 24.

⁹¹ See van den Bergh (1997), pp. 156-159; van den Bergh/Camesasca (2002), pp. 132-133; Geradin (2002), p. 6.

⁹² Example taken from Geradin (2002), p. 6.

⁹³ See German Monopolies Commission (2001), p. 27 at para 40; see also Schaub/Dohms (1999), p. 1059; van den Bergh (1997), p. 157.

⁹⁴ See van den Bergh (1997), pp. 165-174; van den Bergh/Camesasca (2002), pp. 132-133; Geradin (2002), p. 26.

⁹⁵ See van den Bergh (1997), pp. 173-174.

select the national authority that is most likely to issue a favorable decision to them. The same logic applies to potential complainants who will lodge their complaint at that authority where the chance of a prohibition is highest.⁹⁶ In those cases legal errors will occur systematically. The question of whether regulatory capture is more likely to occur under centralized or decentralized law enforcement cannot be finally answered theoretically but only empirically.⁹⁷ An optimal solution with centralized enforcement might be the creation of a politically independent European Cartel Office which goes of course beyond the scope of the actual reform. The problem of a national bias and the risk of forum shopping together are at least to some extent likely to increase the probability of legal errors under decentralized enforcement.

The larger the number of law enforcers the higher is the risk of diverging interpretations of the substantial law. Since decentralized enforcement *per definitionem* increases the number of authorities that apply the law, diverging legal assessments are more likely. If the undertakings concerned do not know at the time they conclude an agreement before which authority it might be challenged in the future, predicting the future decision of law enforcers will be much more difficult in comparison to centralized enforcement. *Risk costs* therefore tend to be higher under a decentralized enforcement of the law.

A further problem is the availability of *adequate sanctions*. Whereas the set of feasible sanctions of the Commission is regulated by European law, the sanctions of the NCAs are regulated by the national legislator. If these sanctions are not equivalent, either because an NCA has no power to impose fines or because the maximum amount of a fine is lower than under European competition law, decentralization can lead to under-deterrence.⁹⁸ This problem could only be solved by harmonizing national procedural laws concerning the application of EU competition law by the competition authorities. However, such a step clearly goes beyond the scope of the actual reform.⁹⁹

3.4 Administrative vs. Private Action

A third choice regarding the design of the law enforcement concerns the question whether competition law should be enforced by administrative agencies (competition authorities) or by ordinary courts through private law suits. In this respect there is a considerable difference between law enforcement in Europe and in the United States.¹⁰⁰ Whereas the former relies heavily on administrative acts, the latter is based

⁹⁶ Note that this problem does not only concern decentralized enforcement by NCAs but equally applies for decentralized enforcement by national courts, see Gustafsson (2000), p. 175.

⁹⁷ See also van den Bergh (1997), pp. 174-175.

⁹⁸ For an overview of the current differences in fines across Europe see Jones (2001), pp. 406-413.

⁹⁹ See Jones (2001), p. 406; Todino (2000), pp. 353-354.

¹⁰⁰ See German Monopolies Commission (1999), at para 37; Paulweber (2000), p. 29; Möschel (2000), p. 498; Kingston (2001), p. 349.

on private law suits. In the following section the effects of these two approaches shall be compared from a law and economics perspective while respect shall be paid to the procedural differences between antitrust court actions in Europe and in the United States.¹⁰¹

In civil proceedings in Europe the relevant information has to be supplied by the parties (*submission principle*).¹⁰² Plaintiffs, such as competitors and consumers, will regularly have extreme difficulties in collecting the information that they need in order to prove an infringement.¹⁰³ In the United States these *information problems* are reduced by a so-called *pre-trial discovery* procedure in which the court can order the defendant to supply all the relevant information. Since such a procedure is absent in European procedural law, plaintiffs will be deterred from filing a law suit if they know that they cannot obtain the relevant proof for an infringement.

A competition authority instead has much greater investigative powers.¹⁰⁴ NCAs can force the undertakings to submit the relevant information concerning their restrictive practice by threatening to impose a fine in case not all or incorrect information is supplied.¹⁰⁵ Furthermore, competition authorities have the right to collect evidence by entering the premises of an undertaking without its consent (so-called *dawn raids*).¹⁰⁶

Another major difference between the European and the U.S. procedural law in antitrust cases concerns the possibility of *class actions* in combination with so-called *contingency fees* for lawyers which both do not exist in Europe. If the harm caused by a restrictive practice is spread over many victims (such as consumers), the individual damage tends to be rather small in comparison with the costs of litigation. If a victim is not perfectly sure to win the case the prospect of having to bear these substantial costs deters filing a law suit. Class actions allow a plaintiff to recover not only damages for the harm he suffered himself but also for the harm suffered by other victims.¹⁰⁷

If the number of victims is high, a single plaintiff can thus be awarded huge damages which creates a very strong incentive to litigate. Contingency fee agreements state that a lawyer only has to be paid by the client if she wins the case (the fee is usually a fraction of the damages the client receives) but receives nothing if

¹⁰¹ On this topic see Paulweber (2000), pp. 23-29.

¹⁰² See German Monopolies Commission (2001), p. 43 at para 68.

¹⁰³ See German Monopolies Commission (2001), p. 44 at para 69; Wißmann (2000), p. 132.

¹⁰⁴ See also German Monopolies Commission (2001), p. 43 at para 67.

¹⁰⁵ For the Commission this is contained in Art. 15 (1) Reg. 17/62 and Art. 23 (1) Reg. 1/2003.

¹⁰⁶ For the Commission the provisions are contained in Art. 14 Reg. 17/62 and Art. 17-21 Reg. 1/2003. For NCAs these powers are now laid down in Art. 22 Reg. 1/2003.

¹⁰⁷ See Cooter/Ulen (2000), p. 387; see also Posner (1998), pp. 626, 659.

the case is lost.¹⁰⁸ The client thus bears no trial risk at all. The combination of these two features of U.S. antitrust law therefore leads to a high level of litigation (perhaps too high)¹⁰⁹, whereas the absence of these features in the European system leads to an inefficient low level of litigation caused by the substantial information costs for plaintiffs. Furthermore, if victims have to sue separately, information costs are multiplied due to the higher number of independent court proceedings whereas a class action allows to deal with all potential claims within one single trial.

Administrative proceedings on the other hand are cost-free for complainants who can shift the information costs to the competition authority. Such a cost-free remedy might in principle induce complainants to lodge too many complaints (including strategic complaints by competitors who might simply try to create some trouble). However, it seems plausible that an authority will only start an investigation if the complainant can provide at least some evidence for a wrongful behavior of the alleged undertakings. Therefore the scope for strategic complaints should be limited. Finally, in an administrative proceeding the costs of information gathering and processing are incurred only once, whereas they would be multiplied by independent court proceedings.¹¹⁰ Administrative proceedings therefore are superior to court proceedings in Europe.

A second problem concerns the *probability of legal errors*. Whereas competition authorities have highly specialized personnel that deals with antitrust law everyday, ordinary courts that have to deal with many different areas of the law cannot be specialized to the same extent. Whereas NCAs employ both legal and economic experts, a judge for civil law matters will regularly not have the same level of understanding for a complex economic assessment as is especially required for a correct application of Art. 81(3) ECT.¹¹¹ It is doubtful that this problem can simply be solved by some additional education in economics for civil law judges.¹¹² The probability of legal errors will therefore be higher when a case is dealt with by an ordinary civil court than when it is handled by a competition authority.¹¹³ The situation might however be different if cases involving antitrust law are assigned to specialized courts which can build up expert knowledge in this area.¹¹⁴ This would

¹⁰⁸ See Cooter/Ulen (2000), p. 385; Posner (1998), p. 624.

¹⁰⁹ Due to potential windfalls gains that plaintiffs can obtain from *treble damages* (see below), see Melamed (1997), p. 96; see also Posner (1976), p. 228.

¹¹⁰ See also German Monopolies Commission (1999), para 48.

¹¹¹ See also Fikentscher (2001), p. 454; Paulweber (2000), pp. 42-43.

¹¹² Proposed by Schaub/Dohms (1999), p. 1062.

¹¹³ See also Gustafsson (2000), pp. 175-177.

¹¹⁴ See German Monopolies Commission (2001), p. 47 at para 75; Geiger (2000), p. 169; Schaub/Dohms (1999), p. 1063.

require an amendment to the national procedural laws which goes beyond the scope of the current reform.¹¹⁵

Apart from that it has to be mentioned that even the Court of First Instance of the European Union (CFI), which can be regarded as a specialized court, did not consider itself able to perform the economic analysis required for the application of Art. 81(3) ECT and thus stated that this task could only be performed by the Commission subject to a very limited review by the Court with respect to the scope of the Commission's discretion.¹¹⁶ It is therefore plausible that the application of Art. 81(3) by the courts might lead to a higher probability of legal errors than its application by administrative agencies.

When antitrust law is enforced by civil courts, the number of law enforcers increases dramatically compared with administrative proceedings since in principle any civil court in the European Union could deal with a case. As it has been previously stated, a higher number of law enforcers will tend to lead to a higher degree of diverging interpretations of the substantial law. This makes the outcome of a proceeding significantly less predictable and thus increases the *risk costs* of the undertakings concerned.

In order to efficiently deter unlawful behavior, law enforcement has to provide *adequate sanctions* for non-compliance with the law. In an administrative proceeding these sanctions are the fines imposed by the competition authority. If law enforcement is based on private court actions in which no fines can be imposed, the sanction then consists of the damage restitution that undertakings have to pay to the victims. The damage payments therefore equal the sum of the individual damages. As it has been stated above, optimal deterrence requires that the expected sanction corresponds to the entire harm caused.

Whereas in an administrative proceeding the expected sanction can also consider the deadweight losses that are caused by a restrictive practice, this will be rather difficult in private court actions where the plaintiffs can only obtain damages for the harm they have actually suffered.¹¹⁷ Furthermore, if procedural law does not contain provisions that encourage filing a law suit just a fraction of the victims will sue and try to recover damages. This further reduces the expected sanction and thus makes unlawful behavior more attractive to the undertakings.

U.S. antitrust law provides an additional element that increases the deterrent effect of private court actions by awarding successful plaintiffs not only damage recovery equaling the harm they have suffered but so-called *treble damages* under which victims receive a damage restitution which is three times higher than the actual

¹¹⁵ See Gustafsson (2000), p. 183.

¹¹⁶ Case T-29/92 *SPO and others v Commission* [1995] *ECR II*, pp. 289 et seq., at para 288. Pointed out by Mestmäcker (1999), p. 526; German Monopolies Commission (1999), para 18.

¹¹⁷ See Posner (1976), p. 224; Melamed (1997), p. 95.

harm.¹¹⁸ Multiple damages thus increase the expected sanction and can offset the problem that only a fraction of the victims decides to go to court. Although there is no evidence whatsoever that this is the correct multiplier¹¹⁹ it is clear that the multiplier has to be greater than one. Since such *punitive* damages are not feasible under European procedural law, the expected sanction resulting from private court actions will not have an adequate deterrent effect on the undertakings.

3.5 Summary

The following table summarizes the results derived from the above analysis where a “+” means superior, a “-” means inferior, and a “?” means unclear effect:

	info costs	legal errors	risk costs	sanctions
ex ante control	+		+	
ex post control	-		-	
centralized	?	+	+	?
decentralized	?	-	-	?
NCA action	+	+	+	+
court action	-	-	-	-

4. Economic Analysis of Regulation 1/2003

The reform of Reg. 17/62 that finally led to the adoption of Reg. 1/2003 has as its core the change from a system based on centralized ex ante control by an administrative authority to a system of decentralized ex post control with parallel law enforcement through NCAs and national courts. Taking a look at the summary table, this seems to be a change from a good system to a bad system combining all possible disadvantages. However, in order to fully assess the effects of the new Regulation other elements of the reform have to be taken into account. In the following section these flanking measures will be examined with respect to their suitability to offset the disadvantages from the system switch.

The abolishment of the notification system leads to the loss of an instrument that induced undertakings to *reveal information* to the law enforcers. Although the

¹¹⁸ See Posner (1976), p. 226; Paulweber (2000), p. 23.

¹¹⁹ This would be the case if the fraction of victims who decides to file a law suit exactly demands restitution for one third of the total harm, see Posner (1976), p. 224.

Commission does not regard this information to be very valuable, this source of information might have been a helpful tool to get some information about the existence and content of restrictive agreements as well as some relevant data about the market structure which now have to be acquired by costly investigations. The main motive of the Commission to free resources in order to concentrate on the most serious infringements might induce undertakings to conclude more restrictive practices in the “gray” area which is now less likely to be controlled.

This situation is aggravated by the loss of transparency that the notification system provided for third parties by the publication of a part of the notified restrictive practices. It is to be regretted that the provision of the Draft Regulation which would have allowed to set up a system of mandatory registration for restrictive agreements on the Internet has not survived in the final Regulation 1/2003. It will therefore become more difficult for competitors and consumers to acquire knowledge about the existence of restrictive agreements which might result in fewer complaints and imposes an obstacle for private court actions.

Regulation 1/2003 contains several provisions that aim at limiting the information costs of decentralized law enforcement. Art. 12 Reg. 1/2003 empowers the Commission and the national competition authorities to exchange the information they have collected and use this information as evidence in a proceeding. Such an exchange of information would reduce the information costs of the authorities. A duplication of proceedings can be avoided if the Commission and the NCAs make use of Art. 13 Reg. 1/2003 which allows them to suspend their own proceeding or reject a complaint if the same restrictive practice is already subject to a proceeding before another competition authority within the European Union. Art. 22 Reg. 1/2003 enables an NCA to carry out investigations on behalf of the Commission or another authority. Finally, Art. 15(6) Reg. 1/2003 empowers the Commission to withdraw a case from one or several NCAs. This provision could be used as *ultima ratio* in order to avoid a duplication of proceedings if several NCAs have started parallel proceedings and they cannot reach an agreement on which NCA should proceed with the case.

If the allocation of cases between the NCAs and the Commission is based on the criterion of which authority is in the best position to obtain the relevant information and if NCAs effectively share their information, a reduction of information costs seems at least possible. Whether this can be achieved will finally depend on the degree of voluntary cooperation between the competition authorities since the above mentioned provisions of Reg. 1/2003 empower them but do not oblige them to cooperate.¹²⁰

¹²⁰ It has been heavily criticized that the draft of the new Regulation did not contain objective criteria for the allocation of cases among the competition authorities. Nor did it contain any mechanisms for dispute settlement between NCAs. See German Monopolies Commission (2001), pp. 27-28 at paras 41-42; Bartosch (2001), p. 106. Reg. 1/2003 does not contain such provisions either.

The information costs of plaintiffs before national courts which tend to be rather high can be reduced by Art. 15(1) Reg. 1/2003 which allows courts to request information in the possession of the Commission. Since such a request is not mandatory and cannot be made by the plaintiffs¹²¹ and since there is no corresponding obligation of the Commission to supply the information,¹²² it is not guaranteed that the information will be made available for a court proceeding. Significant information asymmetries between the plaintiffs and the undertakings concerned could therefore persist. Furthermore, since none of the rules governing U.S. antitrust cases is present in European procedural law, the incentive for a victim to litigate is still rather small.

Whether a possible reduction of *information costs* through the planned cooperation between competition authorities will outweigh the informational disadvantages of abolishing the notification system finally remains doubtful.

As derived above, *legal errors* are more likely to occur under decentralized law enforcement and through application of Art. 81(3) ECT by ordinary courts. Reg. 1/2003 contains several provisions in order to reduce the likelihood of legal errors.

Art. 16(2) Reg. 1/2003 obliges NCAs to respect a prior decision of the Commission in the same matter. This creates a clear hierarchy between NCAs and the Commission and eliminates the possibility of conflicting decisions. Art. 11(3) Reg. 1/2003 obliges a national competition authority to inform the Commission about the initiation of formal investigations, and Art. 11(4) Reg. 1/2003 contains the obligation of an NCA to inform the Commission one month before taking a formal decision about the direction it wants to take. This information can be shared with the other NCAs in the network. These measures have the potential of reducing the risks of national bias and forum shopping by creating an early warning system. Art. 11(6) Reg. 1/2003 allows the Commission to intervene and remove a case from the national authority. Apparent legal errors could thus be avoided.

Art. 15(3) Reg. 1/2003 empowers the national competition authorities (and under certain circumstances the Commission) to submit written observations regarding a pending proceeding to a national court. The purpose of these provisions is to let the competition authorities play a role similar to that of an expert witness before court (*amicus curiae*).¹²³ This provision could effectively offset the problem of a lack of expert knowledge at ordinary civil courts and thus limit the probability of legal errors. However, due to the independence of judges, there is no guarantee that a court will follow the arguments of the competition authority.¹²⁴

¹²¹ See Bartosch (2001), p. 106.

¹²² For criticism see German Monopolies Commission (2001), p. 43 at para 68.

¹²³ See European Commission (1999), p. 26 at para 107.

¹²⁴ See Wißmann (2000), p. 147.

Art. 16(1) Reg. 1/2003 requires that national courts respect a prior decision of the Commission in the same matter and avoid conflicting decisions in a case that is pending before the Commission. Once a case has reached the Commission the scope for diverging court decisions is therefore limited. Art. 15(2) Reg. 1/2003 requires the submission of judgments by national courts to the Commission without delay thereby allowing the Commission to monitor whether the courts indeed respect their obligation.

The above mentioned provisions aim at reducing the likelihood of legal errors in a system of decentralized parallel law enforcement by competition authorities and national courts. Due to the strong position that the Commission still has under Reg. 1/2003 the scope of inconsistent law enforcement can be effectively reduced but it has to be noted that this supervisory role will require human resources at the Commission and thus creates considerable costs.

If the Commission is reluctant to intervene in a case, legal errors are likely to persist. Whereas it is possible for the undertakings to appeal against a Commission decision to the CFI, this is not possible for decisions of the national competition authorities. In these cases appeal is only possible to a national court. Legal errors of the NCAs will thus not come under the scrutiny of a court specialized in European competition law. It has therefore been proposed to allow a review of NCA decisions by the CFI but this lies outside the scope of Reg. 1/2003.¹²⁵

An independent mechanism for avoiding legal errors is the possibility of national courts to call the ECJ for a preliminary ruling under Art. 234 ECT if a case requires interpretation of the substantive law and there is no precedent. Pursuant to Art. 234 only the last instance courts are obliged to call the ECJ and it can therefore not be guaranteed that the lower instance courts request an interpretation by the ECJ. Furthermore, the preliminary reference procedure is limited to questions concerning legal interpretation and does not allow an assessment of the facts.¹²⁶ Finally, due to the workload of the ECJ a preliminary reference takes a considerable amount of time to be processed.¹²⁷ The practical contribution of Art. 234 ECT to avoid legal errors is therefore only of a limited scope.

The unavailability of individual exemptions for undertakings under Reg. 1/2003 reduces legal certainty and therefore creates higher *risk costs*. In order to mitigate this problem, existing block exemption regulations remain valid under Regulation 1/2003 and new ones can be issued by the Commission empowered by the Council.¹²⁸ Art. 29 Reg. 1/2003 empowers the Commission and the national competition authorities to “withdraw” these benefits in individual cases where the conditions of Art. 81(3) are

¹²⁵ See Holmes (2000), pp. 64-65; Kingston (2001), p. 46.

¹²⁶ See Bartosch (2001), p. 105.

¹²⁷ See German Monopolies Commission (2001), pp. 46-47 *ata para* 74; Holmes (2000), p. 64.

¹²⁸ Explanatory memorandum of Reg. 1/2003 at para 10.

not fulfilled. Restrictive practices falling under the scope of a block exemption thus only benefit from a presumption of legality that can be reversed by a competition authority. The legal certainty provided by a block exemption is therefore weakened to some extent. However, as long as an NCA does not withdraw a block exemption the national courts have to respect the validity of the restrictive practice.

In order to mitigate the loss of legal certainty, Art. 10 Reg. 1/2003 empowers the Commission to issue a “positive decision” declaring that a restrictive practice does not constitute an infringement. Albeit such a decision has only a declaratory character it provides at least some legal certainty for the undertakings in combination with the duty of the NCAs and national courts to respect prior decisions taken by the Commission.¹²⁹ However, there is no right for the undertakings to request a positive decision. It is therefore at the discretion of the Commission in which cases it will act “on its own initiative”. Since the Commission wanted to reduce its workload by the new Regulation, it is obvious that positive decisions will be the exception rather than the rule. The number of undertakings which will benefit from such a decision will thus be rather small.

To sum up, a further aggravation of the problem of legal certainty due to the decentralization of law enforcement can be mitigated by the above mentioned provisions of Reg. 1/2003 that are designed to reduce the probability of inconsistent application of the substantive law. The risk costs for undertakings will tend to be higher under Reg. 1/2003 than before but will be limited in scope if the Commission effectively monitors the law enforcement by NCAs and national courts.

Since Regulation 1/2003 strengthens the system of parallel law enforcement by competition authorities and courts, the shortcomings of a court-based system concerning the *adequacy of sanctions* can be compensated by the deterrent effect of administrative action. The above described problem that not all NCAs are currently empowered to impose a fine is removed by Art. 35 Reg. 1/2003 which requires the Member States to provide their authorities with this power before Reg. 1/2003 enters into force. Due to the complementary nature of these two enforcement mechanisms a parallel enforcement might indeed increase the expected sanctions.

Furthermore, decentralized enforcement by more than one competition authority could in theory lead to multiple fines being imposed on the undertakings. This could result in an inefficiently high level of deterrence if an authority when imposing a fine does not take into account a fine that was already imposed by another NCA. The ECJ has stated for parallel fines imposed by the Commission under EU law and an NCA under national law that the sanction imposed by a competition authority has to take prior punitive sanctions into consideration.¹³⁰

¹²⁹ See explanatory memorandum of the draft Regulation, *supra* note 34, p. 19.

¹³⁰ Case 14/68 *Walt Wilhelm and others v. Bundeskartellamt*, [1969] *ECR* p. 1 et seq. at para 11.

Multiple prosecutions could then solve the problem of under-deterrence caused by inadequate fines provided for by the national procedural laws. If the maximum amount of a fine in one jurisdiction seems inadequately low it would be possible to have a second NCA impose a further fine up to the level of efficient deterrence.¹³¹ Although it would be favorable to avoid multiple proceedings altogether in order to limit the administrative costs this could at least serve as an interim solution as long as national procedural laws are not harmonized with respect to the magnitude of fines.

However, a legal concept that might be an obstacle for multiple fines is the principle of *ne bis in idem*.¹³² This principle, which means that unlawful behavior may not be punished twice, is laid down in Art. 50 of the Charter of Fundamental Rights of the European Union.¹³³ Pursuant to its Art. 51 this applies to the authorities of the EU and those of the Member States “only when they are implementing Union law”. Since Art. 3(1) Reg. 1/2003 obliges all NCAs when applying their national competition law to apply Art. 81 ECT as well, the Walt Wilhelm rule which allowed multiple fines due to the different ends of national and EU law¹³⁴ might no longer be applicable. If Art. 50 of the Charter of Fundamental Rights prohibits multiple sanctions whenever European competition law is applied,¹³⁵ this would be the case for all national proceedings after Reg. 1/2003 enters into force.

For all cases which are not dealt with by the Commission, the deterrent effect of a sanction for an infringement of Art. 81 ECT would then depend solely on the national procedural law of the Member State whose NCA is the first to impose a fine. This could weaken deterrence significantly and the only solution to that problem would be that the Commission withdraws the case before a final decision by the national authority is issued. This in turn runs counter to the intention of the Commission to decentralize the enforcement of EU competition law.

In order to combine decentralized enforcement and adequate deterrence for an infringement of Art. 81 it is therefore necessary that the maximum amount of a fine is harmonized across Member States.¹³⁶ The principle of *ne bis in idem* would then have the positive effect of disciplining NCAs and the Commission to avoid a costly duplication of proceedings.

¹³¹ See Wils (2003), p. 137.

¹³² In the U.S. this principle is called the prohibition of double jeopardy, see Salord (2000), p. 130; Wils (2003), p. 131.

¹³³ *OJ C* 364, 18.12.2000, pp. 1-22.

¹³⁴ Case 14/68 Walt Wilhelm and others v. Bundeskartellamt, *supra* note 130, at para 3.

¹³⁵ This view is expressed by Wils (2003), p. 146. The question is left open in a recent judgment by the CFI, see Case T-224/00 ADM v. Commission, judgment of 9 July 2003, not yet published in the *ECR*, at para 93.

¹³⁶ See Wils (2003), p. 147.

5. Conclusion

The reform of Regulation 17 that has led to the adoption of Regulation 1/2003 can without doubt be called a major change of the system of the enforcement of European competition law. Although there are some indications that the need for a system switch might have been exaggerated by the Commission, the eastern enlargement of the European Union will be a challenge that requires some sort of adjustment of the current enforcement system.

The purpose of this paper was to examine whether the switch to a decentralized legal exception system which is the core element of Reg. 1/2003 will enhance the efficiency of law enforcement as it has been claimed by the Commission. In the third chapter it has been shown that there are serious doubts that this will be the case. The abolishment of the notification system leads to the loss of an instrument which has induced undertakings to reveal their private information concerning the existence and content of a restrictive practice in the “gray” area to the Commission. Furthermore, the publication of this information has reduced the information asymmetry between the undertakings and third parties and has enabled them to take action against such a restrictive practice.

It is unfortunate that the *registration system* for restrictive agreements which was included in the draft of the new Regulation has not come into existence. This measure could have reduced information asymmetries at low cost and could have compensated for the abolishment of the notification system. Whether increased investigations and the exchange of information between national competition authorities and the Commission will lead to a reduction in information costs that offsets this disadvantage remains doubtful. Due to the absence of mandatory rules for cooperation in Reg. 1/2003 much will depend on the factual willingness of the authorities to cooperate.

The decentralization of law enforcement and the competence of national courts to apply the entire Art. 81 lead to a higher probability of legal errors. It is therefore essential that the Commission fulfills its monitoring task seriously which might in turn absorb a substantial part of its resources.

The concerned undertakings will face higher costs under the legal exception system due to an increased need for external advice. The reduced legal certainty will also lead to risk costs which stem from suboptimal decisions made by risk-averse decision-makers. These costs will finally have to be borne by society at large. Several provisions in Reg. 1/2003 can limit this problem but they cannot eliminate it entirely.

The deterrent effect of sanctions is weakened by the decentralized enforcement if multiple sanctions are prohibited and thus cannot offset shortcomings in the national procedural law with respect to the magnitude of the fines. Should the ECJ decide that Art. 50 of the Charter of Fundamental Rights applies to the enforcement of Art. 81 by national authorities, this would create an urgent need to harmonize the national procedural laws with respect to the magnitude of fines. The principle of *ne bis in idem*

would then induce NCAs and the Commission to avoid a costly duplication of proceedings. Damages awarded by the national courts complement the deterrent effect of fines but due to the absence of provisions in procedural law which encourage victims to litigate it is doubtful whether Reg. 1/2003 will in fact lead to an increased number of private court actions.

Regulation 1/2003 will neither lead to the complete disappearance of cartels nor will it render the European Union into a big cartel paradise. It should be understood as a response to the challenges that the enlargement of the European Union brings about and even though it might not be perfect it should nevertheless be a workable framework for the enforcement of European competition law in the 21st century.

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