THE EUROPEAN ANTITRUST UPDATE

Key developments in competition law - Autumn 2007

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WINDOWS CASE OPENS GATES?

EC May Be World's Toughest Antitrust Watchdog



The reputation of the European Commission (EC) as the world's toughest antitrust watchdog has been strengthened by the decision of the Court of First Instance in *Microsoft v Commission*. Commentators are asking if the EC's win will open the floodgates for similar EC antitrust prosecutions. Hard on the heels of the Microsoft decision, the EC has launched investigations of Qualcomm and Intel, also for alleged abuse of dominance. Microsoft itself has now ended its nine year fight with the EC by agreeing not to appeal the CFI decision and to share technical information with other software developers.

The Court Decision

Although the repercussions will be felt worldwide, the CFI decision was linked to the very specific facts of the case. The EC triumphed on all key points challenged in its 2004 abusive dominance decision and the fine of €497 million was upheld.

In March 2004, the EC found that Microsoft had infringed Article 82 of the EU Treaty, which prohibits dominant firms from abusing their market power. It found that Microsoft had abused its power in the market for PC operating systems: (1) by refusing to supply rival vendors with certain technical information that would enable them to interoperate with Microsoft's dominant desktop and work group server; and (2) by tying its Windows Media Player ("WMP") to Windows. The Court's decision confirms that Microsoft's obligations arose from Microsoft's "special responsibility", as a dominant supplier, not to allow its conduct to injure competition.

Refusal to Supply Interoperability Information

Sun Microsystems had initiated proceedings in 1998 by complaining that Microsoft had refused to supply it with information for its work group servers to interoperate fully with Windows. Sun said it needed this to be able to compete in the "work group server market", i.e. the market for servers that provide file, print and user identity management services. The EC and the CFI agreed.

The Court rejected Microsoft's contention that the Commission was, in effect, requiring that Microsoft's competitors be able to "clone" Microsoft's products.

The CFI found that "the aim pursued by the Commission is to remove the obstacle for Microsoft's competitors represented by the insufficient degree of interoperability" so their work group servers could compete on different parameters such as reliability, processing speed or the innovative nature of certain functionalities.

Do IP Rights Protect a Dominant Company?

The Court did confirm that dominant companies may refuse to license protected intellectual property and it is only in "exceptional circumstances" that this would be an abuse. The exceptional circumstances were held to have been made out in this case, i.e. (1) interoperability was "indispensable" for competition in an adjacent market; (2) refusal excluded effective competition; and (3) refusal prevented the appearance of a new product for which there was potential consumer demand.

The Court rejected Microsoft's contention that forced disclosure and licensing of interoperability information would deprive it of its incentive to innovate. The Court noted, among other things, that Microsoft acknowledged that similar disclosures ordered in the US have not prevented it from continuing to innovate.

The Windows Media Player Case

The CFI also confirmed that Microsoft had unlawfully bundled its Windows Media Player with Windows. The CFI upheld the Commission's findings that: (1) Microsoft had a dominant position in the market for the tying product (the Windows PC operating system); (2) the tying product and the tied product (i.e., WMP) were two separate products; (3) consumers had no ability to obtain the tying product without the tied product; and (4) competition in the tied product market (i.e., the market for media players) was "foreclosed".

In other words, Microsoft gained a significant advantage through the near ubiquitous distribution of WMP by only offering Windows bundled with WMP. Rival media player vendors were placed in the position of having to sell customers a product which they already had at no separate charge.

The CFI's ruling on Microsoft's WMP bundling is probably the first occasion, at least in the US or the EC, when Microsoft has been held liable, after appeal, for bundling other software packages into its dominant PC operating system.

The Herculean battle seems to have come to an end in this case, but new battles are only just beginning.

NATIONAL ROUND UP

Czech Republic, Denmark and Spain: Introduction of leniency programmes

The Czech Republic, Denmark and Spain are the latest EU Member States to have introduced leniency programmes reflecting the Model Leniency Programme of the European Competition Network. Cartel participants can obtain immunity or reduction in fines for "whistle blowing".

France: Exchange of information

The Supreme Court partly quashed the Court of Appeal judgment which imposed a record fine of €534 million on SFR, Orange and Bouygues for market allocation and exchange of information. The Supreme Court has held that the exchange of confidential information is not an automatic breach of competition law when it occurs in an oligopolistic market. The Court said that exchanging business secrets is unlawful only if it allows competitors to adjust their conduct on the market.

France: Fines for bid-rigging

The French Competition Council (FCC) imposed fines totalling €47.3 million on 12 companies in the construction sector for anti-competitive bid-rigging. They were found to have shared 88 public procurement tenders between 1989 and 1996. According to the market sharing plan agreed by the parties, each pre-selected company managed to win the tender by disclosing the prices of its bids to other participants who then submitted a deliberately overestimated price. The FCC stressed that the overall agreement caused particularly serious damage to the economy which justified exemplary penalties.

Germany: Air Berlin/LTU merger

The acquisition of the unprofitable German charter carrier LTU by Air Berlin, a discount carrier, was cleared in Germany without any remedies. The merger will give rise to the fourth largest airline group in Europe in terms of traffic. Despite overlaps on many routes in Germany and in other EU countries, including some with high shares for the parties, the German authorities found that the merged entity would face competition, with both individuals and tour operators being able to switch their demand to other airlines.

Germany: Axel Springer won the right to appeal

The Federal Cartel Office (FCO) blocked the merger between Axel Springer and ProSiebenSat1 in 2006 saying the merger would strengthen dominance in TV advertising and newspapers. Although the parties called off the merger, their appeals have now been allowed. They still had standing because the FCO's prohibition would prevent any fresh attempt to acquire ProSiebenSat1.

Portugal: Record fine for abusing dominance

Portugal's Competition Authority has fined Portugal Telecom for abusing its dominant position. The fine of €38 million is the highest fine ever imposed by the authority, as well as the first time it has fined a company for abusing its dominant position. The authority found that Portugal Telecom had denied two rival companies access to its underground cable network.

Sweden: Largest cartel case

In Sweden's largest cartel case to date, the Stockholm District Court imposed record fines of about SEK460 million (approx. €50.2 million) on nine construction companies as a result of cartel activities in municipal and state procurements for asphalt road surfacing. Some defendant companies have announced they will appeal.

Turkey: No carve-out

The Turkish Competition Board (TC) has imposed fines on parties involved in multinational mergers affecting the Turkish market because they closed without waiting for clearance. This is despite the parties agreeing to "carve out" Turkish aspects of the deal by holding them separate. It is expected that the fines will be challenged before the Council of State.

United Kingdom: Dairy cartel discovered

Leading supermarkets and dairy processors in the UK have been accused of fixing prices of dairy products. The Office of Fair Trading (OFT) issued a statement of objections stating the companies conspired to fix prices by sharing commercially sensitive information in 2002 and 2003.

United Kingdom: Safe harbour from merger control proceedings?

The OFT is consulting on plans to increase the safe harbour in merger control proceedings. It intends to review the guidelines to reduce the number of referrals where possible harm to consumers is minimal. Mergers in markets worth less than £10 million a year (compared to £400,000 under the existing guidelines) could now avoid merger control review.

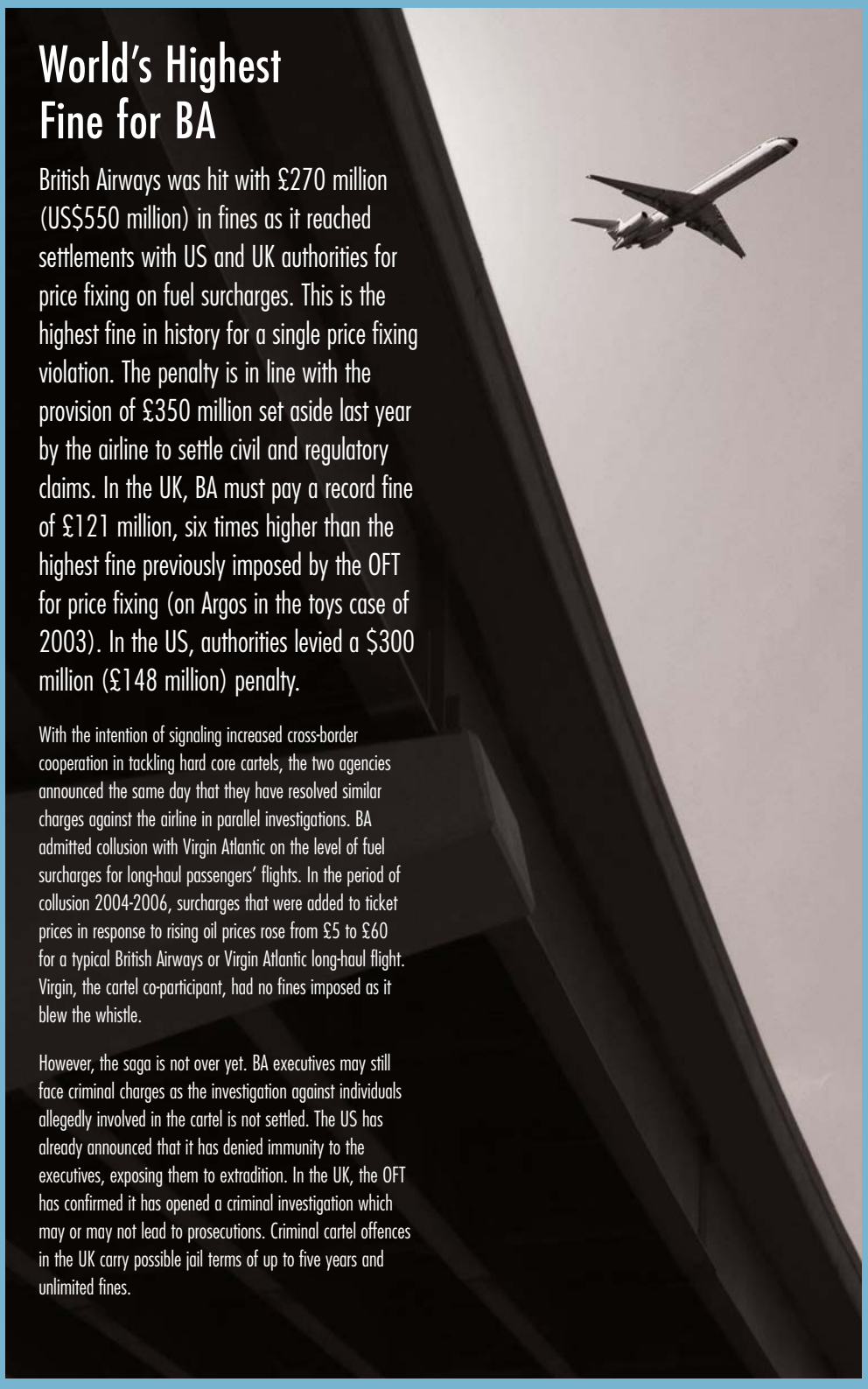


Netherlands: iTunes cleared

The Dutch competition watchdog dismissed a claim by a consumer group that Apple has abused its dominant position by tying its online music service, iTunes, to its iPod media player. It held that consumers who buy music through the internet store of Apple can also play this music on devices other than the iPod.

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Competition Developments in Aviation



World's Highest Fine for BA

British Airways was hit with £270 million (US$550 million) in fines as it reached settlements with US and UK authorities for price fixing on fuel surcharges. This is the highest fine in history for a single price fixing violation. The penalty is in line with the provision of £350 million set aside last year by the airline to settle civil and regulatory claims. In the UK, BA must pay a record fine of £121 million, six times higher than the highest fine previously imposed by the OFT for price fixing (on Argos in the toys case of 2003). In the US, authorities levied a $300 million (£148 million) penalty.

With the intention of signaling increased cross-border cooperation in tackling hard core cartels, the two agencies announced the same day that they have resolved similar charges against the airline in parallel investigations. BA admitted collusion with Virgin Atlantic on the level of fuel surcharges for long-haul passengers' flights. In the period of collusion 2004-2006, surcharges that were added to ticket prices in response to rising oil prices rose from £5 to £60 for a typical British Airways or Virgin Atlantic long-haul flight. Virgin, the cartel co-participant, had no fines imposed as it blew the whistle.

However, the saga is not over yet. BA executives may still face criminal charges as the investigation against individuals allegedly involved in the cartel is not settled. The US has already announced that it has denied immunity to the executives, exposing them to extradition. In the UK, the OFT has confirmed it has opened a criminal investigation which may or may not lead to prosecutions. Criminal cartel offences in the UK carry possible jail terms of up to five years and unlimited fines.



Ryanair/Aer Lingus merger blocked

Neelie Kroes, the EC Competition Commissioner, has used her power to prohibit a merger, for only the second time since taking office in 2004, by blocking a Ryanair/Aer Lingus tie-up. According to the EC, Ryanair is no longer a small, new-entrant airline. The EC analysed the competitive effects of the transaction on individual short-haul routes between Ireland (in particular Dublin) and various European destinations. Ryanair ranked first in 2006 with 40 million international passengers, and Aer Lingus with 8.6 million passengers a year, carry around 80% of all intra-European passengers to and from Dublin. Their activities overlap on 35 routes on which more than 14 million passengers are carried annually. The proposed merger would end the intense competition between the two airlines that has pushed the prices down and brought increased choice, said the Commission.

Ryanair's proposed remedies were considered insufficient. The EC argued that the number of slots Ryanair offered to divest would not have permitted a viable competitor to emerge. Ryanair offered to lower Aer Lingus' short-haul fares by 10% but the EC held that this would be limited in duration and difficult to monitor. The EC went to extra lengths to avoid any possibility of annulment of the decision by the Luxembourg courts. The EC backed its decision with detailed economic evidence and commissioned an independent consultant to carry out a customer survey at the Dublin airport to track travellers' opinions.

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BAA charges should be lower

The UK's Competition Commission (CC) has published its report on charges at Heathrow and Gatwick airports for five years from 1 April 2008. It has a statutory duty to report on price controls. The CC is recommending much lower increases than sought by BAA, the owner of Heathrow and Gatwick. It recommends an increase in the maximum level of airport charges at Heathrow linked to the Retail Price Index (RPI) of RPI+7.5 (7.5% a year above the increase in RPI) and a small reduction below RPI at Gatwick (0.5% below the increase in RPI). A main issue in the CC's inquiry has been the appropriate cost of capital.

The CC also found that Heathrow and Gatwick airports had acted against public interest by failing to manage security and queuing times to minimise delays to passengers, crew and flights. It recommends new conditions for service and security standards.

Airports inquiry continues

The CC is continuing a separate market inquiry into the ownership and operation by BAA of seven airports in England and Scotland, including Heathrow and Gatwick. A consultation document on key issues is expected in early 2008.



EC IN BRIEF

EC approves acquisition of Alcan by Rio Tinto

The EC has cleared Rio Tinto's acquisition of Alcan. The horizontal overlaps between the parties relate to upstream aluminium activities (bauxite mining, alumina refining and primary aluminium). The EC found, however, that these overlaps are limited and that the merged entity would continue to face strong competition from other suppliers with strong market shares in each of these markets. The EC also examined whether the vertical relationship between the production of primary aluminium and the production of flat rolled products could be strengthened. It found that there would be no risk that the merged entity would be able to exclude downstream competitors from access to necessary inputs. The Commission also concluded that the merger would not raise competition concerns in the markets for the licensing of technology, in particular for alumina refining technology and smelter cell technology.

Telefónica – record fine of €152 million for margin squeeze

The EC has fined Telefónica, the Spanish telecoms group that owns O2, a record fine of €152 million for squeezing rival operators out of the broadband internet market. The EC found that the operator charged its competitors excessive wholesale broadband prices which prevented them from competing efficiently in the retail broadband access market. As a result, the EC said that small businesses and consumers in Spain are paying about 20% more for ADSL internet access. In Spain, the penetration rate is 20% below the EU average. The EC began its inquiries into the Telefónica case in late 2003 after Wanadoo's Spanish arm launched a formal complaint. Brussels has defended itself from charges of undermining the Spanish telecommunications regulator, CMT, which found no margin squeeze. "This decision is against Telefónica, not against the Spanish operator", said the EC, which further stressed that the regulator's findings were based on 2001 estimates whilst the iEC used more reliable data. CMT has called on the Luxembourg Court to annul the fine. Telefónica's fine is about 12 times higher than those levied by the EC in 2003 against Deutsche Telecom and Wanadoo for price abuses in the same sector.

Consolidation of UK tour operators

The EC has approved the acquisition of MyTravel Group by KarstadtQuelle and First Choice by TUI. Although reducing the players from four to two, the EC found that the transactions would not lead to excessive market concentration in the UK, and that the remaining two companies would not be able to coordinate their commercial strategies. The EC, however, required TUI to divest its business in Ireland where TUI/First Choice would have become a dominant company. The EC's analysis is at odds with the 1999 acquisition of First Choice by Airtours (later renamed MyTravel). The EC blocked that deal but this was overturned by the Court of First Instance, which ruled that the capacity planning process of tour operators was so complex as to make tacit coordination impossible. When reviewing the KarstadtQuelle/MyTravel and TUI/First Choice transactions the EC abandoned its previous analysis of the UK market and followed the CFI's reasoning.

New Clearance for Sony BMG

The EC has re-approved the creation of Sony BMG, a joint venture combining the recorded music divisions of Sony and Bertelsmann. This joint venture had already been authorised by the EC three years ago, however, the initial clearance decision was dramatically annulled by the Court of First Instance. Following this annulment, the EC re-examined the transaction, taking into account developments since its previous decision (including the exponential growth of online music sales). In particular, the EC analysed all net prices, discounts and wholesale prices for all CD chart albums sold by all major record companies in the EEA between 2002 and 2006. Based on this ground-breaking econometric analysis, the EC concluded that there was no evidence of actual or potential price or non-price coordination between major record companies. The EC has therefore authorised the joint venture without imposing any conditions.

EC launches reform of the energy sector

The EC published a series of legislative proposals aimed at reforming the European energy sector. The EC's proposals focus on the operation of gas and electricity transmission networks, i.e. pipelines and high voltage lines used to transport gas and electricity over long distances.

Under the current regulatory framework, transmission networks can be owned by companies active in the production and supply of energy (although vertically integrated operators are required to grant their infrastructures to third parties and to keep the networks independent with regard to their legal structure, organisation and decision-making). The EC conducted a market investigation showing that energy companies that controlled transmission networks discriminated against other users of the network and impeded new market entries. In order to put an end to these practices, the EC now proposes to "unbundle" the ownership of the networks. This rule would also apply to foreign operators seeking to acquire European networks. The EC has also suggested a possible derogation under which the network would belong to the energy supplier but its technical and commercial operation would be transferred to an independent company designated by the Member State.

The EC's proposals will now be examined by the Council and the European Parliament. France, Germany and several other Member States have already made it clear that they were opposed to the unbundling of energy suppliers as this would imply breaking up "national champions" such as E.ON and Gaz de France.



SEE YOU IN COURT

Akzo case: in-house lawyers beware

Akzo has lost its claim for in-house privilege before the CFI. The ruling has been widely condemned by industry spectators, including the UK Law Society. The long-awaited case concerned whether emails exchanged between Akzo's in-house competition lawyer and its general manager could be seized during a dawn raid. The European Court has held privilege does not apply. The ruling confirms the case law from 1982 which said that in-house lawyers were not independent, regardless of whether the lawyer is a member of a bar or law society. Akzo also lost its claim that privilege should be extended to preparatory notes prepared for the purpose of obtaining legal advice in connection with a competition law compliance programme. The Court said that documents are protected only if drawn up exclusively in the exercise of the applicant's rights of defence, which is not the case for compliance programmes. Akzo, nonetheless, won a small victory on the correct procedure to use in a dawn raid. The CFI found that the EC infringed this procedure by taking a cursory look at certain documents over which the company claimed privilege.

CFI annuls commitments offered by De Beers

The CFI has annulled commitments agreed between De Beers, the largest global supplier of rough diamonds with a 40% market share, and the Commission to settle an abuse of dominance investigation. In March 2002, De Beers and Alrosa notified the EC of an agreement under which De Beers agreed to purchase annually for five years US$800 million of rough diamonds from the Russian state-owned company Alrosa. The EC objected to this agreement and initiated abuse of dominance proceedings against De Beers. In order to settle the case De Beers offered commitments to the EC to terminate its purchase of diamonds from Alrosa from 2009. The EC welcomed this offer which, it said, would free up a viable alternative source for supply of rough diamonds, and took a commitment decision binding on De Beers. Alrosa claimed before the CFI that De Beers commitments were disproportionate. The CFI held that the principle of proportionality required the EC measures not exceed what is appropriate and necessary for achieving the objectives pursued. The voluntary nature of the commitments does not change this need for the EC decision to be proportionate.

Schneider wins action for damages against EC

In 2001, the EC prohibited the acquisition of the French industrial group Legrand by its rival Schneider Electric. Schneider appealed the prohibition decision before the Court of First Instance. At the same time, it agreed to sell Legrand to the consortium formed by Wendel and KKR in the event its appeal was unsuccessful; the sale was at a reduced price because Schneider was granted an option to terminate the agreement. The Court annulled the prohibition decision but the EC opened a new in-depth investigation into the merger and Schneider was compelled to abandon the transaction and divest Legrand.

After selling Legrand, Schneider sued the EC before the CFI claiming damages of €1.6 billion. Schneider argued that these damages were caused by the EC's conduct during the merger control procedure. After almost four years of litigation, the CFI ruled that Schneider was entitled to partial compensation. The CFI held that the EC was liable for the damages caused by the prohibition decision because Schneider had not been given the opportunity to comment on some of the competition concerns identified by the decision. The Court ordered the EC to compensate Schneider for the expenses incurred in relation to the merger control procedure following the annulment of the prohibition decision. The EC must also compensate Schneider for the reduction in Legrand's price that it had to offer to Wendel/KKR in exchange for the right to terminate the sales agreement. The CFI appointed an expert to calculate this reduction in price.

This is the first time that the CFI has awarded damages based on the EC's conduct during a merger control procedure. The EC announced that it would appeal the CFI ruling before the European Court of Justice.

Visa fined €10 million over Morgan Stanley dispute

The European Commission imposed a fine of €10.2 million on Visa Europe after ruling the payment card network operator refused the US bank, Morgan Stanley, access to its network without an objective justification. Visa argued that Morgan Stanley could not join because it owned the Discover credit card network in the US and therefore operated in direct competition. The Commission dismissed the argument saying that Discover was not competing in Europe and that Visa had already admitted Citigroup, the owner of the Diners Club network, which Visa might equally have considered a competitor. The fine follows a six-year dispute between the two companies. Visa said it would appeal the fine.

BSKYB/ITV ACQUISITION MAY RESTRICT COMPETITION

The UK's Competition Commission has provisionally found that the acquisition by British Sky Broadcasting (BSkyB) of a 17.9% share in ITV restricts competition and therefore operates against the public interest.



In its provisional findings, the CC has concluded that BSkyB's shareholding in ITV would likely lead to a substantial lessening of competition (SLC) by giving it the ability to influence ITV's strategy. CC Chairman, Peter Freeman, commented: "The acquisition has made BSkyB ITV's largest shareholder by some margin and whilst our provisional view is that this would not necessarily affect day-to-day operations, BSkyB would be able to influence ITV's key strategic decisions, particularly relating to investment, whether in content, capacity or new technology."

It is key to this provisional finding, that as a pay-TV operator, BSkyB faces competition from the free-to-air TV offer, of which ITV is an important part. According to the CC: "BSkyB would therefore have both the ability and incentive to take advantage of opportunities to weaken ITV or prevent it from taking actions that would threaten BSkyB's interests.

The CC did conclude, however, that the acquisition will have no adverse effect on the sufficiency of plurality. The CC is now consulting on possible remedies to address the adverse public interest finding, including possible divestment of the shareholding.

Other inquiries by the Office of Communications (Ofcom) will have major impacts in the UK's converging communications industry.

Ofcom is investigating whether BSkyB can replace its free-to-air channels with pay-TV services on the digital terrestrial television (DTT) platform, called Freeview. Ofcom has said this may impact competition as Sky may emerge as the main retailer on the DTT platform as well as satellite. Other pay-TV services may therefore find entry more difficult. No final decision has been made.

Broadband in the UK access is also due for a major shake up. Ofcom has announced a consultation on the future of broadband "Next Generation Access" networks. Ofcom has recognised that investment in these networks represents a substantial risk. It is seeking to develop a regulatory framework to appropriately reward risk and encourage faster broadband speeds. Very high speed broadband is seen as critical to the UK's 21st century economy. The first stage of the consultation will run through December.

Fried Frank has acted as a competition law advisor to Virgin Media in relation to these matters.

Contacts

LONDON
99 City Road
London EC1Y 1AX
Tel: +44.20.7972.9600
Fax: +44.20.7972.9602

PARIS
65-67, avenue des Champs Elysées
75008 Paris
Tel: +33.140.62.22.00
Fax: +33.140.62.22.29

FRANKFURT
Taunusanlage 18
60325 Frankfurt am Main
Tel: +49.69.870.030.00
Fax: +49.69.870.030.555

NEW YORK
One New York Plaza
New York, NY 10004
Tel: +1.212.859.8000
Fax: +1.212.859.4000

WASHINGTON, DC
1001 Pennsylvania Avenue, NW
Washington, DC 20004
Tel: +1.202.639.7000
Fax: +1.202.639.7003

HONG KONG
in association with Huen Wong & Co.
9th Floor, Gloucester Tower
The Landmark
15 Queen's Road Central
Hong Kong
Tel: +852.3760.3600
Fax: +852.3760.3611

SHANGHAI
No. 888 Wanhangdu Road
7th Floor, Unit D
Shanghai 200042
(until Spring 2008, when we will be located in Park Place, Nanjing Road West)
Tel: +86.21.2321.0188
Fax: +86.21.6326.6899

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