U.S. Antitrust and EU Competition Policy:
Where has the Former Been,
Where is the Latter Going?*

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The earliest U.S. antitrust laws were adopted after technological changes — most importantly, the development of a national railway network — made the U.S. political union a single economic market. They were adopted with the stated, and no doubt largely sincere, purposes of preventing collusion and strategic entry-deterring behavior. Early application of the antitrust laws relied on a rule of competition to determine whether business conduct was or was not permitted. This has evolved into an explicit evaluation of the impact of businesses practices on consumer welfare, conceived of and measured in an economic sense. EU competition policy was adopted in advance of economic integration. It differed sharply from the traditional policies of the original EC6 member states toward business behavior. It was adopted with the stated, and most likely sincere, purpose of furthering economic integration, and to this end prohibited practices that were seen as distorting competition. Early applications of competition policy, particularly in the European Coal and Steel Community, may have had perverse effects. There are indications of an evolution towards an economic performance standard in the European Union as well.

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1. Introduction

The earliest U.S. antitrust laws were adopted after technological changes — most importantly, the development of a national railway network — made the U.S. political union a single economic market. They were adopted with the stated, and no doubt largely sincere, purposes of preventing collusion and strategic entry-deterring behavior. Early application of the antitrust laws relied on a *rule of competition* to determine whether business conduct was or was not permitted. This has evolved into an explicit evaluation of the impact of businesses practices on consumer welfare, conceived of and measured in an economic sense.

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2. Foundations

2.1 United States

<table>
<thead>
<tr>
<th>Year</th>
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<th>Population (millions)</th>
<th>Median age</th>
<th>Foreign born (%)</th>
<th>Railroad mileage</th>
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*Table 1*: Selected U.S. descriptive statistics, 1840–2000 (most recent figure for percentage of U.S. population that is foreign born is for 1999). Source: U.S. Bureau of the Census publications.
Between 1860, just before the beginning of the American Civil War, and 1890, the year of passage of the Sherman Act, U.S. railroad mileage increased more than five-fold (Table 1). Westward railroad expansion benefited from massive amounts of what we would now call state aid. This aid included extensive grants of land along railroad rights-of-way. Goodrich (1960, Chapter 5) goes so far as to refer to “An Era of National Subsidy” beginning with the Illinois Central Act of 1850 (a federal grant of land to support construction of a railroad system from Mobile, Alabama to northern Illinois) and ended with an 1872 grant of land by the state of Michigan to the Chicago and Northwestern Railroad. State and federal governments funded between 25 and 30 per cent of the cost of railroad construction before the Civil War, with a much smaller but still substantial contribution in the postwar period (Goodrich, 1960, pp. 270--271). The support was justified, as earlier support for the development of canals had been, by the argument that railroad development would bring extensive external benefits that would benefit the country as a whole, over and above any profit taken by railroad entrepreneurs.

The national railroad network enabled and was in turn enabled by the settling of the agricultural Midwest. It was the foundation for the emergence of a continent-wide single market (Chandler, 1977, Part II). It was also directly and indirectly responsible for structural changes and business conduct that led to passage of the Sherman Antitrust Act.

The independent railroad companies that made up the national railroad network were very often monopoly suppliers of transportation services in regional markets, operating feeder lines that led to the national trunk lines, the Atlantic coast, and world markets. The trunk lines themselves were oligopolies. As economists would expect, rates were often higher for short hauls along monopoly feeder lines than for long hauls along trunk line oligopolies. This discrimination in rail rates was widely resented by farmers. It was one of the factors behind the rise of the Grange and other progressive farm-state political movements.

With the single market came mass production and national firms. With mass production came the labor movement, a movement that was aided by the arrival of working-class immigrants from Europe (Table 1).

Railroads, the resulting reduction in transportation cost, and the rise of national firms broke down regional oligopolies in many product markets. The local suppliers whose positions were threatened sought political protection — in modern terms, they turned to rent-seeking.

For example, in the meatpacking industry, ( McCurdy, 1978, p. 643):1

The refrigerator car not only extended the potential market for dressed beef but, since unsalable parts of the animal need not be shipped, it also permitted the processor to save up to 35 percent on freight costs. By combining refrigeration with mass-processing techniques and a strategic location amidst the Chicago stockyards, the “Big Four” packers were able to ship dressed beef thousands of miles and still undersell local butchers by a substantial margin.

Understandably, local butchers took exception to this development. Their trade group, the Butcher’s Protective Association, proposed model state legislation that would

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1 See also Libecap (1992).
(McCurdy, 1978, p. 644) “[prohibit] the sale of dressed beef, mutton, or pork unless it had been inspected by state officials twenty-four hours before slaughter.” The effect of this legislation would have been to keep the industrial meatpackers out of state markets (other than the state of Illinois, happy home to the city of Chicago).

Laws of this kind were adopted in Minnesota, Indiana, and Colorado. In due course, Minnesota and Indiana defended their laws before the U.S. Supreme Court. Attorneys for the meatpackers argued that if the legislation were allowed to stand, any State could exclude from its own territory any and all products of other States. The Court found the state legislation to be in conflict with the national government’s authority over interstate commerce, and from that decision onward, industrial meatpackers were able to ply their trade where they found it profitable to do so.

In the same way, (McCurdy, 1978) when I. M. Singer & Company set up its own sewing machine sales network, states imposed peddler’s license requirements on its salesmen. Such laws were struck down by the Supreme Court. The court decisions striking down protective legislation laid a legal foundation for the national U.S. market that was just as essential as the national transportation system.

![Figure 1: Major railroad connections with the Oil Regions, 1870. Source: Granitz and Klein (1996, Figure 1).](image)

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2 Minnesota v. Barber 136 U.S. 313 (1890).
3 U.S. Constitution, Article 8, Section 1, Clause 3: “Congress has the power ‘To regulate Commerce . . . among the several States.’ ”
4 These decisions correspond to the EU’s Cassis de Dijon decision (REWE-Zentral AG. v. Bundesmonopolverwaltung für Branntwein 1979 ER 662; 1979 3 CMLR 494).
Railroad oligopolists colluded, with varying degrees of success.\(^5\) Railroads and railroad collusion were behind the rise of the Standard Oil Company.\(^6\)

The Standard Oil Company of Ohio was established by the Rockefeller brothers in 1870. Although it was the largest refiner in Cleveland, it had only about 4 per cent of U.S. refining capacity. Ten years later it controlled 90 per of U.S. refining capacity. It managed this expansion by dint of a symbiotic relationship with the three railroad lines that competed to carry crude oil and refined oil products from the oil regions of Western Pennsylvania to the Atlantic coast for export (Figure 1).

The managements of the three railroad lines saw the advantages of collusion. They operated with high fixed costs and low marginal costs. Their market was prey to price wars during the troughs of cyclical fluctuations, which created excess capacity. They entered into a mutually beneficial arrangement with the Standard Oil Company. Standard policed their cartel for them, by allocating its shipments between lines so that each railroad line carried its agreed share of traffic. The railroads were thus enabled to raise rates, to Standard and to other refiners. But Standard benefited not only from rate discrimination, being charged lower rates than independent rivals, but “drawbacks” as well: Standard received a payment for every barrel shipped by independents.\(^7\)

Standard’s conduct is now recognized as strategic raising of rivals’ costs, and it enabled Standard to acquire control of the refining segment of the oil market. It consolidated its control by conduct which may not have been unusual for the age, but which it seemed to perfect (Dewey, 1959, p. 180):

At one time or another it …employed nearly every unfair tactic denounced by economists, lawyers, and legislators—bribery of public officials, exclusive dealing, the secret railroad rebate, bogus independents, harassing lawsuits against competitors, local price cutting to eliminate small rivals, and possibly arson as well.

America’s federal antitrust law was preceded by state antitrust laws, which enjoyed broad popular support. The state antitrust laws were for the most part ineffective as regards attempted application to national corporations, which could dissolve themselves in one state and reincorporate in another as it served their interest.

This indeed was the case with Standard Oil of Ohio, which reorganized itself as Standard Oil of New Jersey when Ohio antitrust activity became too intense. Thirty-three state antitrust suits were filed against Standard Oil between 1890 and 1911, all unsuccessful (Bringhurst, 1979, p. 102). The inability of state antitrust laws to shackle business conduct like that of Standard Oil was directly associated with passage of the Sherman Act.

A Federal antitrust case against Standard Oil began in April 1909, just one month after President Taft took office. The St. Louis circuit court decision, in November 1909,
was in favor of the government. Standard Oil appealed that decision to the Supreme Court, which heard arguments in the case in March 1910 and January 1911, and issued a decision, again in favor of the government, in May 1911.8 The case gave the Court an opportunity to lay out its interpretation of Section Two of the Sherman Act.

For the Court, what Congress sought to avoid when it passed the Sherman Act was unreasonable restraints on competition (221 US 1 at 58; emphasis added):

the dread of enhancement of prices and of other wrongs which it was thought would flow from the undue limitation on competitive conditions caused by contracts or other acts of individuals or corporations, led, as a matter of public policy, to the prohibition or treating as illegal all contracts or acts which were unreasonably restrictive of competitive conditions…

How does one decide if a particular restraint is unreasonable? By looking at the nature of the contract, the circumstances surrounding it, and the intent with which it had been entered into (221 US 1 at 58; emphasis added):

[E]ither from the nature or character of the contract or act or where the surrounding circumstances were such as to justify the conclusion that they had not been entered into or performed with the legitimate purpose of reasonably forwarding personal interest and developing trade, but on the contrary were of such a character as to give rise to the inference or presumption that they had been entered into or done with the intent to do wrong to the general public and to limit the right of individuals, thus restraining the free flow of commerce and tending to bring about the evils, such as enhancement of prices, which were considered to be against public policy. …

Contracts made to promote trade are seen as being reasonable; contracts made to restrain commerce are unreasonable (221 US 1 at 62; emphasis added):

the criteria to be resorted to in any given case for the purpose of ascertaining whether violations of [Section Two] have been committed is the rule of reason……although the statute, by the comprehensiveness of the enumerations embodied in both the first and second sections, makes it certain that its purpose was to prevent undue restraints of every kind or nature, nevertheless, by the omission of any direct prohibition against monopoly in the concrete, it indicates a consciousness that the freedom of the individual right to contract, when not unduly or improperly exercised, was the most efficient means for the prevention of monopoly … if … no right to make unlawful contracts having a monopolistic tendency were permitted. In other words, that freedom to contract was the essence of freedom from undue restraint on the right to contract.

The Court concluded (221 U.S. 1 at 75):

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8 Standard Oil v. U.S. 221 U.S. 1 (1911).
the unification of power and control over petroleum and its products which was the inevitable result of the combining in the New Jersey corporation by the increase of its stock and the transfer to it of the stocks of so many other corporations, aggregating so vast a capital, gives rise, in and of itself, in the absence of countervailing circumstances, to say the least, to the *prima facie* presumption of intent and purpose to maintain the dominancy over the oil industry, not as a result of normal methods of industrial development…

and found Standard Oil in violation of Section 2 of the Sherman Act. Thus the Standard Oil decision was the vehicle by which the rule of reason was introduced to U.S. antitrust.

The U.S. Congress viewed the rule of reason with some alarm (Senate Committee on Interstate Commerce, 1913, pp. 10–11)

The fair conclusion is that it is now the settled doctrine of the Supreme Court that only undue or unreasonable restraints of trade are made unlawful by the anti-trust act, and that in each instance it is for the court to determine whether the established restraint of trade is a due restraint or an undue restraint. …

The committee has full confidence in the integrity, intelligence, and patriotism of the Supreme Court of the United States, but it is unwilling to repose in that court, or any other court, the vast and undefined power which it must exercise in the administration of the statute under the rule which it has promulgated. It substitutes the court in the place of Congress, for whenever the rule is invoked the court does not administer the law, but makes the law. If it continues in force, the Federal courts will, so far as restraint of trade is concerned, make a common law for the United States just as the English courts have made a common law for England.

…It is inconceivable that in a country governed by a written Constitution and statute law the courts can be permitted to test each restraint of trade by the economic standard which the individual members of the court may happen to approve.

The congressional backlash against the rule of reason helped generate support for the Clayton Act of 1914. A companion piece of legislation was the Federal Trade Commission Act. This product of the Progressive Movement was to continue the information-gathering and disseminating activities of an earlier agency, the Bureau of Corporations.9 The Federal Trade Commission Act established the 5-member Federal

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9 President Wilson’s call for such a commission in a 1914 speech to Congress makes it sound very much like the kind of publicity-based regulatory agency that later obtained a following in some parts of Europe (Wilson, 1925, pp. 85–6):

And the business men of the country desire something more than that the menace of legal process ...be made explicit and intelligible. They desire the
Trade Commission as an independent government agency charged with enforcing the antitrust laws. It had a mandate to enforce the very general prohibition of Section 5 of the FTC Act against unfair competition. The wording of Section 5 of the FTC Act should be enough, in and of itself, to establish that the original goals of U.S. antitrust went beyond maximization of consumer surplus or of net social welfare.

2.2 European Union

2.2.1 National backgrounds

EU competition policy and U.S. antitrust policy have far more in common than one might at first expect. But the backgrounds against which the two policies were put into place are vastly different.

The national business policy traditions of the EU6 member states were, if anything, hostile to reliance on markets as a resource allocation mechanism. From at least an 1897 decision, cartel agreements in Germany were enforceable in courts of law (Marburg, 1964, p. 81):

The [Reichsgericht] decided that the [Saxon Woodpulp Manufacturers Association] cartel agreement did not violate the general clause of the Trade Regulation Act, insofar as it was intended to promote the interests of society in general, and that the personal liberty of the individual was not impaired by the cartel agreement in contravention of the act. The reasoning as to the interests of society in general rested on the premise that ruinously low prices, as occur in a crisis, adversely affect both the individual seller and the national economy, and that, therefore, cartel agreements designed to prevent such low prices are in the public interest. …a court restraint upon cartel contracts would constitute governmental limitation upon freedom of contract.

While the details varied from member state to member state, the general approach conveyed a distrust of markets (Amato, 1997, pp. 39--40):

In traditionally dirigiste France, and in Germany and Italy with their delayed development, State protectionism, publicly owned firms, exclusive rights for public, and private, firms and consortia among private firms were common ingredients in the guidance of the economy.

Cartels assumed a key role in the aftermath of the First World War (Nocken, 1989, p. 35):

advice, the definite guidance, and information which can be supplied by an administrative body, an interstate trade commission. [The opinion of the country] demands such a commission only as an indispensable instrument of information and publicity, as a clearing house for the facts by which both the public mind and the managers of the great business undertakings should be guided....
…the steel cartel helped to … create a balance between the basic industries of Germany and France acceptable to both sides, after Alsace-Lorraine and the Saar were removed from German sovereignty by the [Versailles] treaty.

Cartel-like arrangements became even more firmly entrenched as the world economy slid into depression (Gillingham, 1989, p. 83)

In the 1930s, economic policy-makers in France and Britain, traditionally committed to laissez-faire, became converts to German practices of “organized capitalism.”

and (Gillingham, 1989, p. 90):

The success of these arrangements can be traced back to the discredit cast on liberal economics by the Depression. The era’s “buzzword” was “industrial self-government”, by which was meant that producers, instead of competing, should do business cooperatively through special associations set up to regulate markets and simultaneously promote modernization.

It was hoped that international cartels would keep trade flows going, if at a carefully controlled rate. In the absence of some such arrangement, it was feared (and in the event, this is largely what happened) that Prisoners’ Dilemma imposition of protective tariffs would seal national economies behind walls of autarkic poverty. For the Interparliamentary Union, international cartels were a normal part of the industrial landscape, to be carefully tended rather than weeded out (Interparliamentary Union, 1930):

…cartels, trusts and other analogous combines are natural phenomena of economic life towards which it is impossible to adopt an entirely negative attitude. Seeing, however, that those combines may have a harmful effect both as regards public interests and those of the State, it is necessary that they should be controlled. This control …should simply seek to establish a supervision over possible abuses and to prevent those abuses.

An efficacious means of fighting such abuses and a basic condition for eventual control is to be found in publicity, which implies an obligation for cartels and similar combines to announce their existence and to register in the books of the state.

2.2.2. ECSC

The European Coal and Steel Community was the first step on the road to the European Union. It can be argued that the ECSC was also the first misstep on the road to EU competition policy.
Jean Monnet, the architect of the Schuman Plan, settled on economic integration as an indirect means of reaching his primary objective, which was political rather than economic: in notes from 1950, he wrote (Monnet, 1976, p. 342)

…une autre guerre est proche devant nous si nous ne faisons rien. L’Allemagne n’en sera pas la cause, mais elle en sera l’enjeu. Il faut qu’elle cesse d’être un enjeu, qu’elle devienne au contraire un lien. Seule la France peut actuellement prendre une initiative. Qu’est-ce qui pourrait lier, avant qu’il ne soit trop tard, la France et l’Allemagne, comment enraciner dès aujourd’hui un intérêt commun entre les deux pays…

The coal and steel sectors, upon which Monnet settled as a means of forging ties between France and Germany, possessed historical, symbolic, and practical advantages as choices for economic integration.

There was a history of vertical relationships between French coal and German steel, not to mention the cooperation embodied in the interwar steel cartel. The steel cartel had not been particularly successful, and (evidently) the economic ties it implied had not prevented the run-up to World War II. But one must take one’s history as one finds it.

Symbolically (Gerbet, 1956, p. 542):


There were practical advantages of several kinds.

France, under its first post-war Plan (supervised by Jean Monnet) had substantially expanded its steel capacity. A common market in coal and steel would at once ensure French access to coal for its forges and an outlet for its steel products (Haas, 1958, p. 242; see also Abelshauser, 1994).

The French interest in introducing vertical disintegration between German coal and German steel fit nicely with the American deconcentration and decartelization drive of the early occupation (Berghahn, 1986). Given the dirigiste bent of French microeconomic policy, American hostility toward cartels had the unfortunate aspect of being general rather than specific (Diebold, 1988, p. 26):

So far as Americans were concerned, the cartel issue went beyond Germany. It is not always remembered nowadays that the American interpretation of the interwar experience put considerable stress on the iniquities of international
cartels. Partly that was economic analysis and partly it was a reaction to the Nazi use of German firms, notably I.G. Farben … to penetrate other countries.

Against this background, it is not surprising that the initial reaction of many American observers (including then-Secretary of State Dean Acheson) to the Schuman Plan was that the Coal and Steel Community would simply be a cover for the revival of pre-war cartels (Monnet, 1976, p. 356; Gillingham, 1991, p. 234). The lasting legacy of this reaction sprang from the steps taken by Monnet to assuage American concerns. He contacted the American High Commissioner for Germany and arranged to draw on the services of the American diplomat Robert Bowie. Bowie drafted the first versions of what became Articles 65 and 66 of the Treaty of Paris, and he based them on Sections 1 and 2 of the Sherman Act (Ball, 1973, p. 88; Monnet, 1976, p. 413; Bowie, 1989; Spierenburg and Poidevin, 1994, p. 28). There were changes in language and in nuance, (Lang, 1958), but Articles 65 and 66, the direct ancestors of Articles 85 and 86 of the Treaty of Rome (now Articles 81 and 82 of the EC Treaty), are themselves direct descendents of Sections 1 and 2 of the Sherman Act.

Despite these historical, symbolic, and political advantages, the settling on coal and steel as the lead sectors for European integration carried with it one negative point: from an economic point of view, these two industries were singularly unsuited for integration.

No particular economic studies of the coal and steel sectors were undertaken in advance of the Schuman Plan proposals.10 Their economic characteristics suggest that integration of the Member State markets should have been expected to entail an extended period of disequilibrium, with substantial political and economic costs (Lister, 1960, p. 403):

The coal and steel industries were not the most tractable ones with which to start the experiment of freeing trade and prices because freight costs in both industries tend to create separate markets, because of the structure of ownership and the long history of concerted practices, because individual governments exercise strong influence over the two industries, and because the coal industry is so labor intensive.

The adjustment was indeed a difficult one. The decline of the coal market, and particularly of Belgian coal, began very soon after the formation of the ECSC (Figure 2). As far as the development of EU competition policy is concerned, the decline of coal may be seen as perhaps the first example of the enduring tradition of the granting of massive amounts of state aid, often in violation of state aid rules, for the purpose of delaying as long as possible structural adjustments that are a consequence of market integration and, in fact, a prerequisite for the full benefits of integration to be realized.

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10 Gerbet (1956, p. 542). Milward (1992, p. 105) writes “Monnet, as all who worked with him in the ECSC agree, had little interest in or knowledge of the details of the coal, iron and steel industries. For him, they were merely instrumental to his higher political goals.”
The decline in steel came later than the decline in coal, after the 1973 oil shock (Figure 3). The use of crisis cartels to deal with the steel decline (Heusdens and de Horn, 1980) was an indication of a fundamental unwillingness to rely on the marketplace as a resource allocation mechanism.
Substantive ECSC price policy is laid out in

- Article 4(b), which prohibits “measures or practices which discriminate between producers, between purchasers or between consumers, especially in prices and delivery terms or transport rates and conditions, and measures or practices which interfere with the purchaser’s free choice of supplier;”
- Article 60(1), which
  - bans unfair competitive practices — predatory pricing is given as an example (“purely local price reductions tending towards the acquisition of a monopoly position”); and prohibits
  - “discriminatory practices involving, within the common market, the application by a seller of dissimilar conditions to comparable transactions, especially on grounds of the nationality of the buyer” (thus repeating the content of Article 4(b)).
- Article 60(2)(a), which provides that for the purposes of accomplishing the prohibitions of Article 60(1) “the price lists and conditions of sale applied by undertakings within the common market must be made public to the extent and in the manner prescribed by the High Authority…”. 

Figure 3: Index of crude steel production, 1974 = 100, ECSC6, 1953-1988. Source: Mitchell (1992, Table D9).
There is no clearly stated rationale for the banning price discrimination. It can be understood that a European common market would not permit discrimination based on national identity. But the prohibition of price discrimination contained in the Treaty is a general one. Since price discrimination is a normal form of rivalry (that is, of competition, in the lay sense in which the word is used in the Treaty) in imperfectly competitive markets, it follows that by seeking to prohibit price discrimination in general, the Treaty sought to prohibit a normal form of oligopolistic competition.

For Haas (1958, p. 245), the prohibition of price discrimination had a protectionist purpose:

Monnet’s specific proposals on market rules, prices, access to raw materials, non-discrimination, subsidies, re-adaptation, and exemptions during the transitional period were accepted in essence in the final version of the Treaty, including the rigorous interpretation of Article 60 which make “non-discrimination” almost the equivalent of “no price competition,” a deliberate device to limit the flow of German steel to the French market.

The rationale for publication of prices was to provide consumers with information that would allow them to make the best choice of supplier (Spierenburg and Poidevin, 1994, p. 101, writing of the rules for steel):

Under Article 60, producers were obliged to publish their prices. Accordingly, the High Authority drafted rather elaborate rules to cover not only basis prices but also conditions of sale, delivery dates, standard surcharges for special qualities and discounts for quantity and loyalty. It explained clearly that steel producers ‘must ensure that users are able to ascertain the quality and calculate precisely the cost of the products they are considering buying, and also to compare offers from various suppliers’.

Ensuring that users have the ability to make such comparisons ensures as well that any producer cutting price would know that rivals would be aware of that price cut in advance, and able to match it. This brings out a point which seems to underlie much of US and later EEC, EU competition policy. Very often, of course, policymakers seem to have no coherent vision of markets in mind when they formulate public policy toward markets. When a market model behind policy formation can be inferred, it often seems to be the model of a perfectly competitive market that is in long-run equilibrium. When such policies are applied to imperfectly competitive markets, the consequences can be quite different from those anticipated.

So it proved to be for ECSC steel. The anti-collision provisions of Article 65 applied to agreements restricting competition “within the common market.” In an imperfectly competitive market, one might expect that participation in an export cartel would of necessity affect the home markets of participating firms, but the ECSC High Authority did not take this view. ECSC steel firms formed an export cartel. When the ECSC came into effect and freed producers from national price controls, firms raised prices for the ECSC member states to the higher level set by the export cartel. Further,
under Article 60(2) of the Treaty, steel firms set up a basing point system (Phlips, 1983, pp. 27–30; 1993).

In coal, neither the High Authority nor Member State governments seemed to take the idea of market competition seriously (Lister, 1960, p. 260):

That there is need of centralized regulation of production, prices and sales in order to mitigate the effects of the business cycle is a proposition that goes nearly unchallenged in Europe.

The underlying policy goal (Diebold, 1959, p. 274) was to keep all ships afloat:

For instance, most of the Community’s coal is covered by price equalization arrangements and compensation schemes. Though costs differ, all the mines in the scheme sell at the same price. Part of the return to the more efficient mines is distributed to less efficient ones. This makes it possible to keep prices lower than they would be if they had to be remunerative to the high-cost mines, but prevents any coal being sold at the lowest price the most efficient mines could offer.

Such a policy prevents an efficient allocation of resources (Meade et al., 1962, p. 218):

keeping the prices charged by each basin closely geared to costs prevents the lower-cost producers from realizing the extra profit without which they are unlikely to expand at the appropriate rate, if at all. It follows that if progress towards the attainment of the common market’s basic aim—an improved distribution of resources—is the criterion, then the price-fixing policy of the High Authority and of the member governments is open to question.

By the time initial negotiations and legal skirmishes over the introduction of some form of managed competition for coal had played themselves out, the fact of secular decline in coal had become undeniable (Figure 2). From that point, the task of the High Authority became that of organizing a retreat.

3. United States: Competition to Welfare

U.S. antitrust law dealing with interfirm relations includes Section 1 of the Sherman Act, Section 3 of the Clayton Act (which prohibits tying, exclusive dealing, and requirements contracts, “where the effect …may be to substantially lessen competition or tend to create a monopoly…”), and the Federal Trade Commission Section 5 prohibition of unfair methods of competition.

It is worth quoting Section 1 and 2 of the Sherman Act in full to make the point that they do not contain the word “competition”:11

Section 1: Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or

11 These are the current versions, which differ in minor ways, including adjustments in the maximum amount of fines, from the originals.
with foreign nations, is declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $10,000,000 if a corporation, or, if any other person, $350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

Section 2: Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $10,000,000 if a corporation, or, if any other person, $350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

“Competition” was read into the Sherman Act by Supreme Court interpretation. In the 1904 Northern Securities decision, Justice Harlan summarized the Court’s reading of the not quite 15-year-old Sherman Act as follows (193 U.S. 197 at 33, emphasis added):

We will not incumber this opinion by extended extracts from the former opinions of this court. It is sufficient to say that from the decisions in the above cases propositions are plainly deducible and embrace the present case. Those propositions are: …

That Congress has the power to establish rules by which interstate and international commerce shall be governed, and, by the Anti-Trust Act, has prescribed the rule of free competition among those engaged in such commerce;

That every combination or conspiracy which would extinguish competition between otherwise competing railroads engaged in interstate trade or commerce, and which would in that way restrain such trade or commerce, is made illegal by the act;

From that time forth, the principle of competition was key to applying many elements of U.S. antitrust (Letwin, 1965, p. 227):

Harlan’s opinion served for years as the great synthesis of all previous interpretations of the statute. The rule, as it now stood, was that “restraint of trade” meant any direct interference with competition.

The principle of competition arose in a simpler age. Among other aspects of this simplicity, the models that academic economics could offer courts for guidance were the models of monopoly and of perfect competition. Against this background, reliance on a prohibition of strategic interference with competition is a practical way to implement antitrust policy.

The principle of competition sustained the per se rule against collusion. It was extended to cover a wide variety of interfirm contracts that were condemned because they

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were seen as interfering with competition. This extension was heavily criticized by students of the Chicago School of economics, particularly as regards interfirm contracts between a manufacturer and a distributor.

For example, the 1966 *Schwinn* decision\(^\text{14}\) involved a manufacturer of bicycles that had seen its market share fall from 22.5% in 1951 to 12.8% in 1961. In response, it reorganized its distribution system around a network of 22 wholesale distributors was assigned a territory, and authorized to sell only to franchised retail dealers in that territory. Franchised retailers were to sell only from authorized locations. Shipments of bicycles were often direct from Schwinn to retailers, on the basis of orders placed through wholesalers. In some cases Schwinn retained ownership of the bicycles until they reached the final consumer, with the distributors acting as Schwinn’s agents. In other cases, the distributors took legal ownership of bicycles before possession was taken by the final consumer.

In 1958, the government challenged this distribution system as a restraint of trade in violation of Section 1 of the Sherman Act. In its 1965 decision, the District Court found territorial restrictions to be illegal per se where Schwinn sold bicycles to its distributors, but found no violation where Schwinn retained ownership of bicycles.\(^\text{15}\) The District Court did permit Schwinn’s customer restraints — the requirement that authorized wholesale distributors limit their sales to authorized retail dealers.

The government appealed this part of the District Court decision to the Supreme Court, and asked that the customer restrictions be considered an unreasonable restraint of intrabrand competition among Schwinn’s dealers.

In its decision, the Supreme Court accepted that Schwinn’s motives were to achieve commercial success (388 U.S. 365 at 374): “the reasons which induced [Schwinn] to adopt the challenged distribution program were to enable it and the small, independent merchants that made up its chain of distribution to compete more effectively in the marketplace.” For the court, the question was not Schwinn’s motive, but the impact of its strategy on competition (388 U.S. 365 at 375):

> Our inquiry is whether, assuming nonpredatory motives and business purposes and the incentive of profit and volume considerations, the effect upon competition in the marketplace is substantially adverse.

The Supreme Court gave the government a partial victory: it condemned the customer restrictions if Schwinn sold the bicycles to dealers, not if Schwinn retained ownership and employed the dealers as agents.

The *Schwinn* decision was heavily criticized. The essential element of the criticism was that, whatever the effect of the restrictions was, it was the same whether the bicycles were sold to the dealers or marketed by the dealers as agents. What should be evaluated, in this view, was the impact of the restrictions on market performance, not on the competitive opportunities of distributors.

\(^\text{13}\) The *per se* rule appeared in an 1898 Circuit Court opinion written by William Howard Taft, *U.S. v. Addyston Pipe and Steel* 85 Fed 271, and was later endorsed by the Supreme Court (*Addyston Pipe and Steel v. U.S.* 175 US 211, (1899)).


A further element of this debate was that vertical restrictions might sometimes improve market performance. One example would be to combat successive marginalization; another would be to prevent free-riding. In later decisions (notably, Continental T.V. Inc. v. GTE Sylvania), indeed, the Supreme Court moved away from the per se approach implied by the principle of competition to an explicit evaluation of the welfare impact of a challenged practice on market performance. There may be debate over whether the welfare measure that is to be maximized is consumers’ surplus or net social welfare, but the principle that it is a welfare standard that is to be applied, rather than the principle of competition, is now accepted.

4 EU: Competition to ?

As amended by the Maastricht Treaty, Article 3 of the EC Treaty now includes the statement that

…the activities of the Community shall include…

(g) a system ensuring that competition in the internal market is not distorted;…

The same commitment to undistorted competition appears in Article 81 of the EC Treaty, paragraph 1 of which reads in part (emphasis added)

The following shall be prohibited as incompatible with the common market:

all agreements between undertakings, decisions by associations of undertakings and concerted practices 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…

These commitments to undistorted competition correspond to the principle of competition set out by the U.S. Supreme Court in the Northern Securities decision. But the EU’s commitment to the maintenance of competition is explicit in the documents that lay out its legal foundation, not dependent on judicial interpretation.

The rest of Article 81(1) includes as examples of prohibited agreements those that

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;
(b) limit or control production, markets, technical development, or investment;
(c) share markets or sources of supply;
(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

16 The extreme Chicago school position is that vertical restraints can never harm market performance, so that their effects must be positive and they should, therefore, be permitted per se. This argument fails in imperfectly competitive markets with imperfect information; see Rey and Tirole (forthcoming).
18 The welfare standard appears in other antitrust applications, as, for example, the cautious consideration now given to efficiency under Department of Justice-FTC Horizontal Merger Guidelines.
Subparagraph (a) prohibits explicit price-fixing; (b) and (c) prohibit indirect price-fixing. (d) prohibits price discrimination, as did the ECSC Treaty and as does Section 2(a) of the U.S. Clayton Act. While the formal provisions of EU and US law correspond, in application EU competition policy has always been fundamentally affected by the overriding goal of promoting market integration. The Commission has, therefore, consistently opposed vertical restraints that have the effect of splitting the Single Market along national boundaries.

An earlier decision held, similarly, that legal trademarks could not justify exclusive distribution systems that divided the common market along national boundaries. The background to the 1966 Consten & Grundig decision\(^{19}\) was the exclusive territorial right that Grundig granted Consten to market Grundig consumer electronics products in France. When challenged by the European Commission under what is now Article 81, Consten and Grundig appealed to the European Court of Justice, making the kinds of efficiency arguments that had appeared in *GTE Sylvania*: an exclusive territory was a restriction on intrabrand competition, but it served to promote interbrand competition. The European Court of Justice would have none of this, for two reasons (Amato, 1997, p. 49):

The explicit [reason] is that the need for intra-brand competition is based on protection not of an individual right (freedom of trade) but of a general and objective principle (competitiveness of the market in all its segments). The implicit [reason] is …to protect another principle, a higher one in 1966, that of market integration. For the territory protected by Consten’s rigid exclusivity coincided with that of the French State, and both the Commission and the Court saw this protection as persistence of the segmentation of economic activities along national frontiers…

In the same way, national resale price maintenance systems do not come under the authority of EC competition law, since they do not affect trade between the member states. But the Commission has held that existence of a legal national resale price maintenance system cannot be used to block shipments of a manufacturer’s product from one Member State to another. If a German record producer supplies a retail distributor in France, the French distributor must be allowed to sell in Germany if it is profitable to do so, even if such sales are at a price below the fixed German retail price.\(^{20}\)

In later decisions, the European courts have shown a willingness to accept what might be called grants of permeable territorial exclusivity: a franchisee may receive an exclusive territory, provided parallel imports are permitted.\(^{21}\) The same position is laid out in the 1999 vertical restraints regulation. Thus the EU shows signs of evolving from a maintenance of undistorted competition standard toward a willingness to take some efficiency aspects of interfirm contracts into account. Unlike the US, however, this willingness is tempered by the weight the EU gives to the promotion of market integration.

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5. Conclusion

Starting from very different backgrounds, U.S. antitrust and EU competition policy have come to share the same basic principles. The EU now appears to be moving along the same path trod by US antitrust a quarter of a century ago: from a reliance on maintaining the ability of equally efficient competitors to compete as a way of getting good market performance toward an explicit, case-by-case assessment of the impact of a business practice on market performance, or of a proposed merger/structural change on expected market performance.

Economists can only applaud such a development. It must be admitted that movement away from “the principle of competition” toward explicit welfare evaluation places a particular responsibility on the economics profession. Under a welfare evaluation standard, what the rules of competition policy are comes to depend on the ingenuity of economists in the analysis of market performance, and in the explanation of those analyses to courts.

There is one thing that U.S. antitrust policy and EU competition policy have in common. Economists conceive of both in economic terms. In doing so, being economists, they disagree about both premises and conclusions, but the debates are about the economic rationales for and consequences of public policy toward business behavior and market performance. At their foundations, however, neither U.S. antitrust policy nor EU competition policy were principally economic policies. Their bases can at most be said lie in political economy, and even that may be forcing the point. The analytical framework, and it is an economic framework, that now shapes antitrust and competition policy is grafted onto political economy roots. Those roots dictate divergences of policy from a strictly economic approach, and as the political roots differ in the U.S. and the EU, they dictate continuing differences between the two jurisdictions.

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