The Effective Competitive Constraint Standard

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The consumer welfare standard, which broadly considers higher output and lower prices as its primary goals, is not well equipped to monitor the numerous competitive harms that consumers face in the 21st century. An effective competitive constraint standard would not replace the consumer welfare standard but rather recognize that market forces can reduce competition in various ways that are not always immediately recognizable as harmful, and instead place the burden on the instigators of potentially anticompetitive behaviors to show that their actions does not, in the end, undermine competition or justify their anticompetitive behavior as beneficial to the consumer overall.

The Stigler Center's 2023 Antitrust and Competition conference seeks to answer the question: what lays beyond the consumer welfare standard? In advance of the discussions, *ProMarket* is publishing a series of papers on the infamous consumer welfare standard. This piece is part of that debate.

Both U.S. antitrust law and EU competition law are written in a vague, open-textured language, use conceptually elastic concepts, and rely heavily on economics, a field under constant epistemic evolution. As a result, both systems are bound to remain normatively open. Yet, both systems need to secure their integrity (i.e. principled consistency). For this reason, enforcers, judges, practitioners and academics on both sides of the Atlantic have been employing a wide array of interpretive standards, methods of interpretation, and economic knowledge to tame the law's openness and ensure its integrity.

In this context, the consumer welfare (CW) standard emerged in the 1980s to rationalize an otherwise nebulous area of law and managed to provide a compelling conceptual paradigm to understand and apply antitrust law. Properly understood, CW refers to the area under the demand curve and above the price paid (the consumer surplus) and focuses antitrust intervention on output and price. It proposes that competition law should encourage markets to produce output as high as is consistent with sustainable competition, and prices that are accordingly as low. To a large extent, this standard has been endorsed by both U.S. and EU antitrust institutions, although to various degrees and variations.

The central message of the CW standard—that competition law and policy should focus on ensuring higher output, lower prices, higher quality, and innovation—cannot be easily discarded. The CW standard has pushed antitrust institutions to fully articulate the reasons for taking a decision and to use economic tools to demonstrate competitive harm. Nevertheless, it is becoming increasingly evident that CW cannot function as an all-encompassing framework for the competition law systems that seek to address the challenges of the 21st century.

Current digital capitalism has opened up new possibilities for value creation and extraction and has led to new business models and types of interactions among market participants. Simultaneously, there is growing evidence that the non-price parameters of competition play a key role in firms' competitive decisions and consumers' purchasing choices. Furthermore, there seem to be reasons and ways to incorporate issues that for decades have appeared to be extramural—such as privacy, sustainability, concentration in labor markets, democracy and industrial policy considerations—into antitrust's analytical framework.

Against this backdrop, it is worth asking if there is a way to preserve the benefits of the CW standard while recalibrating competition law for the challenges of the 21st century (in a similar way as our modern economies may require recalibration). To this end, this essay argues for an "Effective Competitive Constraint" (ECC) standard as a compliment to CW. According to this standard, the crucial question is not whether rivals cooperate or undertake exclusionary strategies, thereby harming consumers, but whether rivals' ability and incentives to compete are (or may be) affected to such an extent that the remaining competitive constraints become ineffective.

To reach any conclusions in this regard, competition authorities would have to scrutinize three clusters of indicia (the market context, the particular features of market participants, and the form of the conduct in question), and examine whether an agreement or a practice adversely affects an effective competitive structure by suppressing or removing an effective competitive constraint. The benchmark should not be an abstract ideal of "effective competition," but the competition that would have otherwise existed in the absence of the conduct at hand.

Effective competitive constraints can be removed or marginalized through two archetypical mechanisms: (a) collusion, under which competing firms act explicitly or covertly to suppress rivalry (i.e. reduce through cooperation their incentives to compete); (b) exclusion, under which an agreement or unilateral conduct reduces a rival firm's ability to compete, having a negative influence on the various parameters of competition (i.e. price, production, innovation, variety or quality of goods or services). These two mechanisms could be combined: e.g. firms can collude to exclude a maverick and, thereby, become able to exercise market power to the detriment of consumers.

The ECC standard is not incompatible with CW, since a practice that removes effective competitive constraints—thereby adversely impacting an effective competitive structure—is also likely to affect consumers negatively by leading to lower output and higher prices. Such conduct can harm consumers not only by leading to higher prices or less output, but also by thwarting sustainability or privacy competition or by harming innovation. Hence, consumer harm is likely to follow from competitive harm (as understood here).

Nonetheless, if antitrust authorities focus solely on output and prices or are required to provide evidence of quantifiable consumer harm, their intervention might come too late and be too narrow: competition in the market may be significantly reshaped in the meantime by the relevant conduct and the existing competitive constraints might be significantly suppressed. For this reason, the ECC standard does not require evidence of actual or potential consumer harm to establish an antitrust violation. "Only" reducing effective competitive constraints will suffice to consider a practice presumptively unlawful. Removing or suppressing an ECC, however, may be accompanied by offsetting procompetitive benefits. For instance, it may lead to economies of scale that benefit consumers. Therefore, thwarting an ECC should only entail a rebuttable presumption of unlawfulness allowing defendants to raise countervailing claims.

The remainder of this essay briefly presents the weaknesses of the CW standard; presents the key elements of the ECC standard; and disentangles the relationship between the two.

I. The inadequacies of consumer welfare

According to the CW standard, any antitrust intervention should be limited to circumstances where firm behavior can be shown to have harmed consumers' welfare in the sense of lower output or higher prices. Several scholars have shown that the initial definition of CW—as encompassing both higher prices for consumer *and* lost profits for producers—was misleading and that this standard should be understood in technical economic terms as consumer surplus, i.e. as the difference between the aggregation of consumers' individual reservation prices and the prices that they ultimately pay.

Despite these efforts, however, the CW standard remains notoriously elusive. For instance, contrary to the U.S. approach that primarily focuses on the welfare of final consumers and assesses the impact of a practice (or an agreement) on prices and output, under EU competition law, both final and intermediate buyers are considered "consumers" and their welfare can be harmed not only by conduct that leads to increased prices or reduced output, but also by conduct that leads to sluggish innovation, less choice and diminished quality. In addition, the crucial distinction between "enhancing" and "maximizing" CW is often missed. As a result, competition authorities may announce that their interventions aim at maximizing CW, whereas what they actually do is to clear CW-enhancing arrangements and sanction CW-reducing ones.

Regardless of these intricacies, the advocates of CW can still argue that "merely" securing lower prices for consumers and sanctioning output restrictions—even if considered a shallow goal—can at least lead to predictable, administrable and coherent enforcement. Be that as it may, the CW standard may lead to outcomes incompatible with total welfare; it may be hard to measure empirically; and not necessarily lead to straightforward and fully satisfactory legal tests. In addition, it may be too narrow to account for a practice's long-term effects and impact on quality and innovation. Furthermore, CW may make antitrust institutions lose sight of the problem of monopsony (for arguments against this view see here) not align or even run counter workers' interests (for arguments against this view see here), and downplay the role of competition-relevant sustainability concerns.

If enforcers, following the CW standard, focus on immediate and narrowly defined consumer benefits, they may disregard how certain practices undermine economic competition and generate negative non-price effects. They may also allow for substantial market power concentration without accompanying long-term gains in consumer welfare and lose sight of businesses' novel and more ingenious methods to thwart competition and innovation. In addition, a strict application of the CW may inappropriately heighten the burden of proof for plaintiffs and lead to underenforcement (in support of this view see also here). On this basis, it could be argued that the CW standard cannot provide an all-encompassing ideal or a comprehensive framework for 21st century competition law.

II. The Effective Competitive Constraint Standard

The ECC standard understands competition not as a CW-maximization device, but as a process of rivalry that can be ensured if effective competitive constraints operate in the market. This standard values competition not because of a particular outcome (e.g. CW- or TW-maximization), but because it constitutes a discovery process likely to ensure a plurality of values (e.g. freedom to compete, consumer welfare, decentralization of economic power, efficiency, consumer welfare, innovation). This approach recognizes that competition is an essentially contested concept having various dimensions (e.g. competition *in* vis-à-vis competition *for* the market, ecosystems competition vis-à-vis platform competition, competition within and outside value chains or clusters) and parameters (e.g. price and non-price parameters). Accordingly, it suggests that the objective of the law should be to maintain effective competitive structures, regardless of the overriding various reasons we may have for endorsing economic competition as an abstract ideal.

These overriding reasons for valuing economic competition (e.g. valuing competition because it promotes consumer welfare, innovation, sustainability, privacy, choice, market access, or opportunity to compete) could serve, though, as *intermediary values* providing proxies to pin down under what conditions a competitive structure or a constraint is "effective." For instance, in a market or value chain where innovation is crucial, an authority could use innovation theories to understand the precise nature of competition and draw on innovation-related concepts (e.g. innovation capabilities, incentives, efforts, spaces, pathways, output and diversity) and metrics to make inferences about the consequences of particular conduct. Hence, under the ECC standard, enforcers and adjudicators should operate *heuristically*: use different intermediary values, legal tests, and extra-legal knowledge (e.g. neoclassical, behavioral, innovation or ecological economics) to identify in a particular case, market context or era what is an "effective competitive constraint."

Two observations are due at this point to highlight the pragmatism of the ECC standard. First, in the long history of both U.S. antitrust and EU competition law, antitrust institutions have in fact operated heuristically: they have exploited law's openness to incorporate new knowledge on how markets actually work and materialize law's core mission (i.e. the protection of market competition). Second, even though the "effective competitive structure" concept might seem elusive, in fact it is not. This notion refers to market structures where various players exercise sufficient competitive pressure to each other and requires enforcers to conduct a counterfactual exercise they know well: to compare competition in the market with and without the practice at hand.

According to the ECC standard, harm to competition can be established when a form of collusion or exclusion (or a combination thereof) diminishes effective competitive constraints without any offsetting procompetitive benefits. Under this standard, a conduct that removes or significantly restrains an effective competitive constraint would be considered *prima facie* unlawful, and the defendant would bear the burden of proving countervailing or offsetting procompetitive benefits. The general assumption here is that actual or potential consumer harm is likely to follow from a practice that removes or significantly curtails the competitive options of an important market participant. This assumption should also function as a guiding or limiting principle if antitrust institutions decide to concretize the ECC standard through particular legal tests. In other words, this fundamental assumption that links competitive harm and consumer harm under the ECC standard has to remain credible: antitrust institutions should not apply the ECC standard in a way that denies that a practice that generally enhances consumers' wellbeing amounts to intensification and not suppression of effective competition.

To be sure, the ECC standard—as the CW standard—does not prescribe specific legal tests. For example, it does not say whether a particular type of vertical restraint in a certain market environment needs to be *per se* unlawful or scrutinized under the rule of reason. Economic theory and empirical research are responsible for fleshing out concrete and operational legal tests and specific metrics. The ECC standard simply seeks to reorientate, in a principled manner, antitrust intervention to what really matters: effective competition. In this way, as shown below, this standard aims to preserve the positive elements of the CW standard and remain largely consistent with the paradigmatic practices of antitrust institutions on both sides of the Atlantic, while enriching antitrust analysis.

With regard to concerted practices, the ECC standard would prohibit horizontal or vertical agreements that generate collusive effects in the same way as the CW standard. Yet, it would advise a less permissive approach towards problems of vertical control, since vertical integration by contract (or vertical mergers) can lead to anticompetitive foreclosure by targeting effective competitive constraints. For instance, an exclusive agreement may not exclude a firm altogether, but it may raise its costs in a way that facilitates monopoly pricing, or it may make a price increase profitable by changing bargaining relationships especially if it allows for recapturing profits lost from the price increase. In such cases, understanding how a restraint (or an acquisition) affects the effectiveness of particular competitive constraints "can tell us much more than any information concerning the overall relevant market in which the firms operate," as Herbert Hovenkamp wrote.

In abuse of dominance or monopolization cases, the ECC standard would lead to similar outcomes as the CW standard on several occasions. For instance, it would consider *prima facie* lawful conduct that benefits consumers or increases efficiency. It would also consider *prima facie* lawful conduct that leads to the exclusion of a rival because their product is less attractive in the eyes of consumers in terms of price, choice, quality or innovation, since such a rival in principle is not an effective competitive constraint. In this sense, the ECC standard is in line with several strands of the existing case law. For example, this standard will condemn a dominant firm that uses its exclusive dealing policy to keep rival firms' sales "below the critical level necessary for any rival to pose a real threat to [its] market share;" engages in a profit sacrifice without any procompetitive explanation; misuses the patent system or engages in vexatious litigation to further entrench its market position; strategically hoards capacity; pays its customers to not purchase rivals' products; or concludes pay-for-delay settlements.

The ECC would, however, argue for a more holistic effects-based approach. According to this standard, a dominant firm can restrict competition not only when "it is able to hamper or eliminate effective access of actual or potential competitors to supplies or markets, and as a result is able to exercise substantial market power", but also when "it adversely impacts an effective competitive structure, thus [affecting] negatively the various parameters of competition." Hence, a dominant firm may restrict competition not only when it forecloses as-efficient competitors but also less efficient competitors, in that even less efficient competitors can exercise competitive discipline or intensify competitive pressure, especially on digital markets. Similarly, if a dominant firm raises rivals costs without any offsetting procompetitive benefits, it would be found to violate the ECC standard.

Consequently, the ECC standard, while being in accordance with some exemplary abuse of dominance or monopolization cases, can extend the reach of the law to enable it to deal with the challenges of the digital economy. For example, when powerful digital platforms distort the supply and demand of innovation; eliminate or distort emerging innovators; diminish the quality, diversity and direction of innovation; or use bottlenecks and chokepoints to stifle competitors, they are essentially thwarting ECCs. The same applies when such platforms or ecosystems use "nowcasting technology" to identify and replicate popular and profitable products of their competitors; when they reject apps whose innovation threatens their ecosystem (i.e. strategic exclusion); when they improve interoperability for their own or favored technologies and degrade interoperability for the disfavored technologies (i.e. weaponizing interoperability); or when they copy disruptor's innovation (i.e. copycat strategy). Similarly, when powerful incumbents buy out or intimidate disruptive start-ups, or when they use promotion techniques (e.g. self-preferencing) and default settings to steer demand away from key rivals, they can eliminate ECCs. By eliminating such constraints the winners of the competitive bout can control the process of innovation, and extract maximum value from third-parties and consumers.

With regards to merger control, the ECC standard would point to the same direction as the CW standard when horizontal or vertical mergers generate non-coordinated or coordinated effects without offsetting procompetitive benefits. Nevertheless, this standard would advocate in favor of a more prominent role for killer acquisitions and portfolio theories, since certain strategies (e.g. acquiring nascent competitors; engaging in tying, bundling or conglomerate mergers to exercise portfolio power) can restrict buyer choice and deter entry in the long run, even when they reduce prices—and therefore pass muster under a CW standard— thereby undermining effective competitive structures. Despite potential initial welfare gains, such practices could ultimately have an overall negative effect if they eliminate a sufficient number of key competitors and capacity from the market.

To recap, according to the ECC standard, a practice that leads to collusion; has a systemic exclusionary effect; makes market access impossible or very difficult; or significantly curtails rivals' opportunities to compete on a fundamental competitive parameter will be deemed anticompetitive, except if it has offsetting or countervailing procompetitive effects. For this purpose, enforcers will need to scrutinize three clusters of indicia: the market context, the particular features of market participants, and the features of the conduct at stake. Yet, enforcers will not be required to demonstrate consumer harm to establish a violation. Demonstrating that an effective competitive constraint is removed or significantly curtailed will suffice. Then the defendant would bear the burden of showing that their conduct generates specific and verifiable procompetitive benefits that counteract the established competitive harm.

III. The relationship between the two standards

The ECC standard does not negate the value of CW as a particularly useful standard to identify harms to effective competition. It also agrees with the advocates of CW that a) undistorted demand should drive the competitive game; b) markets should work for competition and benefit consumers; c) a successful competitor, having been urged to compete, should not be turned upon when it wins; d) competition on the merits may, by definition, lead to the departure from the market or the marginalization of competitors that are less attractive to consumers from the point of view of, among other things, price, choice, quality or innovation; and e) not every exclusionary effect is necessarily detrimental to competition, and, therefore, there is a difference between foreclosure and anticompetitive foreclosure.

Nevertheless, the ECC standard does not accept five central tenets of the current CW orthodoxy. First, it denies that the ultimate purpose of the rules that seek to ensure that competition is to increase consumer welfare. Second, it negates the proposition that consumer harm is necessary for establishing a competitive harm. Third, it proposes that consumer welfare should not be understood narrowly in price-output terms but broadly as referring to the well-being of consumers. Fourth, it disagrees with the proposition that the as-efficient test offers the only reliable tool to find anticompetitive foreclosure. Fifth, it disagrees with the view that vertical control and conglomerate mergers lead to competitive harm only when they lead to reduced output.

Conclusion

The ECC standard is in line with fundamental insights of modern microeconomics while also incorporating new economic knowledge. It is also in line with the fundamental principles of both EU competition law and U.S. antitrust. It can inspire a wide constellation of legal tests and incorporate the strengths of the CW without raising risks of false positives or false negatives. Furthermore, it is compatible with various institutional set-ups and it can adapt to the particularities of each competition law system. In terms of legal technique, it can be operationalized via various rebuttable rule-like and standard-like presumptions so as to ensure that the burden of proof is properly allocated between plaintiffs and defendants.

Launching such a standard does not require a radical overhaul of the current analytical framework. Yet, enforcers need to tread lightly. For instance, they could announce it in advance in well-articulated guidelines and run some cases under it and stress test it before the courts. Most importantly, enforcers will need to revisit the results of their enforcement performance. To do so, they will need to identify specific benchmarks on the basis of which they will be able to assert *post facto* that their intervention improved certain parameters of the competitive game without generating unintended consequences. Such an exercise will require *ex post* assessment of the cases where the ECC standard was enforced and re-consideration of the adopted theory of harm and remedies in light of the ensuing market developments.

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