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Antitrust and sustainability: globally warming up to be a hot topic?

Grant Murray (Baker McKenzie) · Friday, October 18th, 2019

This post explains (i) why there is friction between sustainability initiatives and competition law and (ii) how the EU Commission could take steps to address this.

Recent EU developments suggest a renewed interest in this area:

- In November 2018, the EU Competition Commissioner hinted at a more worldly application of the EU competition rules by emphasising that "businesses should take responsibility, not just for the quality of their products, but for their effect on the world around them".
- Last month, a Finnish judge expressed a similar sentiment at a conference, declaring that it was time to reconsider the relationship between sustainability and antitrust to ensure companies can cooperate on what it is "good for the planet". https://www.mlex.com/GlobalAntitrust/DetailView.aspx?cid=1131289&siteid=190&rdir=1
- The topic seems to be surfacing on the conference circuit. Vestager provides a keynote at an event in Brussels next week (I'm definitely going) https://www.ucl.ac.uk/laws/events/2019/oct/conference-sustainability-and-competition-policy-bridging-two-worlds-enable-fairer and then there is a further one in Oxford early next year. https://www.law.ox.ac.uk/events/competition-law-and-sustainability

The debate around sustainability may also share some characteristics with another hot topic right now, digital and antitrust:

- Stakeholders from all quarters are clamouring for change: government, activists, shareholders and consumers
- Non-price factors lie at the heart of the issue
- The conduct under examination has effects beyond borders, meaning that firms may be exposed to multiple and often incoherent laws
- It makes sense to assess impact over the longer term to ensure dynamic efficiencies are considered
- There may be a political dimension

Here's my take on the debate and some ideas for how to improve things – for us and the next generation.

In **conclusion** (with more detailed reasoning below):

- It makes sense to explore and **explain how the *'Wouters'* line of case law applies in the environmental sector**, making it clear than proportionate attempts to bring about non-economic goals will not fall within the scope of competition law.
- Since sustainability initiatives may increase rather than reduce cost, the EU Guidelines could provide **greater clarity on when qualitative (rather than cost) efficiencies may arise as a result of sustainability efforts**. That should include product characteristics (e.g. biodegradability) but also the way in which goods are produced. For example, the condition in which animals are farmed or the manner in which crops are grown can form part of the product's quality dimension. The Guidelines could usefully clarify when sustainability initiatives may generate such qualitative efficiencies and **how companies might reasonably demonstrate them, including by (but not limited to) showing sufficient consumer willingness to pay** for the improved features.
- Competition authorities should also **explore ways to translate non-economic benefits into economic terms**, for example the economic effects of avoided emissions of harmful gases. This is important to ensure a complete cost-benefit analysis is undertaken. In more difficult cases, it may be worth considering whether there is **a role for wider government to play in balancing the economic benefits against the competitive effects**. This may require some assessment of negative externalities – i.e. environmental costs which are not reflected in the prevailing price (which may be what Commissioner Vestager is getting at when talking about the need for firms to take responsibility for the effects of their products).
- The European Commission should adapt its approach to efficiencies so as to reflect EU case law which actually takes **a broader view of efficiencies, allowing 'out of market' efficiencies to be included in the assessment**. A broader approach is particularly justified for environmental agreements whose beneficial effects may be very widespread (e.g. clean air), reducing concerns about distributional equity (one group paying for another's benefits). There may also be ways to address perceptions of inequity – requiring even greater benefits in order to offset costs borne by others. At the very least the notion of when markets are linked (such that benefits in them are in scope) should be widened for example by describing an expansive view of requisite commonalities between consumer groups.
- Finally, the fact that environmental agreements may only bring about benefits in the longer term (e.g. for the next generation) should not mean they are left out of the cost-benefit analysis. It is essential to include them by **looking further into the future**, with more remote factors being weighted (discounted) accordingly.
- The process is also important. The burden on a company to show qualitative efficiencies should not be more stringent than requiring **good faith estimations of environmental benefits**. Ideally, a workable **mechanism for obtaining ex ante reactions** from a competition authority would be available (like the US Business Review letter).

Why the tension between antitrust and sustainability initiatives?

Companies seek to achieve more sustainable outcomes for a variety of reasons. They may be responding to shareholder preferences or to consumer of even government pressure.

There are a variety of 'sustainability' initiatives and they arise in all sectors. Common examples include arrangements to only bring to market products that are sustainable (in one or more respects); arrangements designed to ensure a living wage further up the supply chain; collective plans regarding an ancillary service (such as collective waste removal systems); or standardization

for the purpose of logistics, distribution or packaging.

Companies can of course pursue these initiatives independently but the incentive to do so may not be there, including because of ‘first mover disadvantage’ or free-rider concerns. Initiatives are obviously more likely to be effective when taken on by a large part of the market.

Pursuing non-economic goals can sometimes reduce product choice (e.g. where non-sustainably produced goods are removed from the supply chain) but may also improve product quality. While sustainability agreements may increase price (since more expensive methods may need to be used), they are not on their face aimed at increasing firms’ revenues. Instead they pursue moral goals and enjoy widespread popular and even government support.

Yet EU competition law does not always provide clear answers for companies contemplating sustainable goals. The tension lies in measuring how non-economic interest such as social environmental aims measure up against price effects. As a result, the law or a perception of the law, may stand in the way of sustainability initiatives. Lack of certainty can be invoked as a reason for opposing calls for change or for challenging legitimate conduct.

Reform of the Horizontals presents an opportunity to address these shortcomings, though reform of the EU 101(3) Guidelines may also be necessary.

Environmental agreements may not restriction competition at all

Under EU law, agreements which restrict commercial conduct may not infringe competition law if, due to their context and objectives, they are necessary and proportionate to realise non-economic goals. While the case law does not relate specifically to environmental protection, there is no reason it should not apply in that context. However, for now, the case law is not conclusive on whether and, if so under which conditions, environmental benefits associated with a horizontal agreement may take the agreement outside the scope of that provision. Extra guidance is needed on when that would be the case.

A modern approach to analysing efficiencies is needed

There are three dimensions in respect of which the Commission could provide greater certainty for sustainability.

Dimension #1: the scope of efficiencies:

The EU 101(3) Guidelines differentiate between cost and qualitative efficiencies. Sustainability projects are likely to increase rather than reduce cost so the latter category of qualitative efficiencies is key (para 69 of 101(3) Guidelines). Benefits falling in this category typically relate to quality, product range or a firm’s service offering. So the question for sustainability projects is whether there is a non-price based value to the consumer? How far does that extend?

The UK competition authority suggested (in its submission to an OECD roundtable on Horizontal Agreements in the Environmental Context) that product biodegradability or ‘rainforest friendly’

coffee might count as direct economic benefits if consumers placed a value on those features. Those aspects would form part of the quality dimension for consumers.

This could be a first area for improvement: a clarification in the Guidelines that direct economic benefits may flow from the *way* in which a product is produced and not just its intrinsic properties (such as biodegradability).

The question is then of course how to measure the value that consumers place on those qualitative factors. Paragraph 104 of the 101(3) guidelines acknowledges that qualitative efficiencies may outweigh an adverse effect on competition but stops short of explaining how that might be assessed. Is the test simply the preparedness of consumers to pay more for the qualitative improvement? This was the approach taken in the Dutch *Chicken of Tomorrow* case. But if that is the right approach, how can that reasonably be measured?

But this is still quite a narrow approach – focussing on the views of purchasers and seeking to monetise qualitative factors. It essentially assumes that there is no tension between competition law policy and sustainability goals and that the latter can always be expressed in monetary terms.

A further question is what to do about non-economic benefits which are likely to be more remote. There is no mention of these efficiencies in the Horizontal or 101(3) Guidelines despite the fact that there have been cases where non-economic issues were taken into account.

Most pertinent is of course the famous EU washing machines case (*CECED*) where the Commission took into account, not just individual economic benefits to customers from lower energy bills, but also the "collective environmental benefits" that would flow from the agreement, referring specifically to the EU's environmental policy in its decision.

Showing that it may be possible to quantify what appear at first to be non-economic factors, the Commission estimated that the "benefits to society" from avoided emissions were more than seven times greater than the increased purchase costs of more energy-efficient washing machines.

But what about cases where the non-economic efficiencies are more remote/harder to put a value on or where they are not obviously valued by consumers? The Commission and EU Courts have been willing to fold in non-economic factors in the past:

- In *Metro v Commission*, the ECJ considered that employment was a relevant factor under 101(3), saying that the agreement was a "stabilising factor with regard to the provision of employment…". https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:61976CJ0026&from=EN (para 43)
- In *Exxon/Shell*, the Commission acknowledged (under "Advantages for consumers") that "…the avoidance of environmental risks … will be perceived as beneficial by many consumers at a time when the limitation of natural resources and threats to the environment are of increasing public concern". https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A31994D0322 (para 71)
- In *Philips/Osram*, the Commission noted that the use of cleaner facilities would "… result in less air pollution, and consequently in direct and indirect benefits for consumers from reduced negative externalities" https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A31994D0986 (para 27)

No-one would deny the difficulties in measuring non-economic efficiencies and yet it does make sense to complete the cost-benefit analysis. So the question should be *how* to analyse the benefits (not whether they should be looked at all). It would be really helpful for competition authorities to explore ways of translating environmental benefits into economic efficiencies which companies could then use to make their case. That said, a stringent requirement that went beyond the companies' good faith intentions and assessment of environmental benefits would run the risk of chilling environmental benefits.

In the hardest cases, where it is too difficult to quantify non-economic benefits, it may be worth considering whether the competition authority could assess the restrictive impact leaving the wider government to balance the costs to competition against the benefits to environment etc.. That analysis may need to include some analysis of the negative externalities of the status quo – i.e. the environmental costs not reflected in price (which seems to chime with what the EU Commissioner said about businesses taking responsibility for their effect on the world around them?).

Dimension #2: to which consumers must the benefits accrue?

The EU Guidelines on 101(3) explain in para 43 that the assessment of efficiencies flowing from restrictive agreements must be made in the relevant markets to which the agreement relates. It goes on to say that "[n]egative effects on consumers in one geographic market or product market cannot normally be balanced against and compensated by positive effects for consumers in another unrelated geographic market or product market. However, where two markets are related, efficiencies achieved on separate markets can be taken into account provided that the group of consumers affected by the restriction and benefiting from the efficiency gains are substantially the same ".

But is the approach really supported by the EU jurisprudence? Back in 2002, the Court of First Instance pointed out in *Compagnie Générale Maritime* that:

"[f]or the purposes of examining the merits of the Commission's findings as to the various requirements of Article 85(3) of the Treaty and Article 5 of Regulation No 1017/68, regard should naturally be had to the advantages arising from the agreement in question, not only for the relevant market, …, but also, in appropriate cases, for every other market on which the agreement in question might have beneficial effects, and even, in a more general sense, for any service the quality or efficiency of which might be improved by the existence of that agreement. Both Article 5 of Regulation No 1017/68 and Article 85(3) of the Treaty envisage exemption in favour of, amongst others, agreements which contribute to promoting technical or economic progress, without requiring a specific link with the relevant market".

A case in point is, again *CECED*: the Commission looked not just at cost savings for purchasers of washing machines but went on to say that "environmental results for society would adequately allow consumers a fair share of the benefits even if no benefits accrued to individual purchasers of machines." It is striking that the Commission made the point that these more remote environmental benefits would, alone, have been enough to satisfy the relevant criterion under 101(3).

More recent cases suggest that the para 43 approach is need of an update:

1. In *Mastercard*, the Court acknowledged that "the appreciable objective advantages to which the first condition of Article 81(3) EC relates may arise not only for the relevant market but also for

every other market on which the agreement in question might have beneficial effects".

2. This ties in with the approach under Article 101(1): in *Groupement Cartes Bancaires*, the Court noted that "[i]n order to assess whether coordination between undertakings is by nature harmful to the proper functioning of normal competition, it is necessary, …, to take into consideration all relevant aspects – having regard, in particular, to the nature of the services at issue, as well as the real conditions of the functioning and structure of the markets – of the economic or legal context in which that coordination takes place, it being immaterial whether or not such an aspect relates to the relevant market." (para 78)http://curia.europa.eu/juris/document/document.jsf?text=&docid=157516&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=5145116
3. In *Star Alliance*, the Commission seemed to extend the test in para 43 of the Guidelines by taking into account 'out of market efficiencies' but was clearly nervous about this approach, pointing out that this was only justified by the facts of that case such as its finding of a 'considerable commonality' between consumers on different markets. https://ec.europa.eu/competition/antitrust/cases/dec_docs/39595/39595_3012_4.pdf (para 58 and footnote 43)

So why this overly narrow approach? The explanation for the Commission's approach seems to be explained in para 85 of the 101(3) Guidelines which says that "the net effect of the agreement must at least be neutral from the point of view of those consumers directly or likely affected by the agreement".

Some principle of distributional equity may be behind this – avoiding one set of consumers paying for benefits enjoyed by another set of users. But that is arguably less of an issue with environmental agreements whose benefits (e.g. clean air) can have a very wide scope (although see observations on time below).

Even if that issue is acknowledged, there may be another way to address this. The UK competition authority asks for example how much greater net benefits might have to be (relative to costs) for an agreement to have a possibility of exemption – e.g. what if benefits to a set of consumers outside the relevant market were 5% higher than the cost to consumers in the relevant market. Would that be sufficient?

Even if the narrow approach were adopted, it would be very useful for the Commission to explain when different consumer groups are sufficiently linked such that 'out of market' efficiencies could be taken into consideration. In CECED, the consumers affected by a possible restriction in competition and enjoying benefits (of lower energy consumption costs) were substantially the same but to, to employ the Commission's term from *Star Alliance*, other "commonalities" may justify this.

Dimension #3: the appropriate time horizon for the analysis

This is an important issue for environmental agreements where the benefits may arise for the next generation. Taking an unduly static view of the market will block arrangements with potentiality enormous future environmental benefits. There is a need of course to address remoteness but the competition authorities have the tools to do this by applying a lower weighting for more remote benefits.

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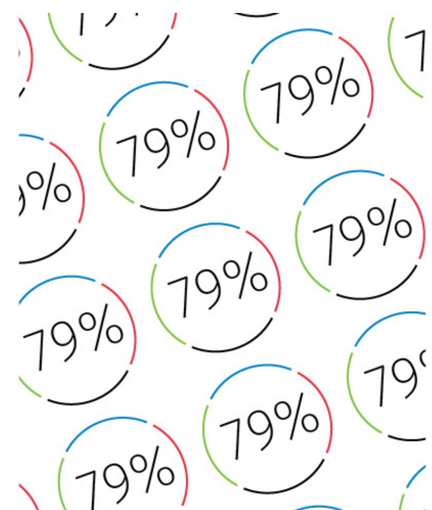

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