IBM v. Commissioner: The Effects Test in the EEC

Margaret Lo

Follow this and additional works at: http://lawdigitalcommons.bc.edu/iclr

Part of the Antitrust and Trade Regulation Commons, and the Jurisdiction Commons

Recommended Citation
Margaret Lo, IBM v. Commissioner: The Effects Test in the EEC, 10 B.C. Int'l & Comp. L. Rev. 125 (1987), http://lawdigitalcommons.bc.edu/iclr/vol10/iss1/8

This Notes is brought to you for free and open access by the Law Journals at Digital Commons @ Boston College Law School. It has been accepted for inclusion in Boston College International and Comparative Law Review by an authorized editor of Digital Commons @ Boston College Law School. For more information, please contact nick.zyndowsky@bc.edu.
**IBM v. Commissioner:** The Effects Test in the EEC

I. INTRODUCTION

The competition rules of the European Economic Community (EEC) date back to the very inception of the EEC thirty years ago.¹ This Note will consider the effectiveness of these rules with an analysis of their enforcement by the EEC Commission (Commission).² In examining the effectiveness of the EEC competition rules, this Note will focus on the EEC’s jurisdiction in this area. In *IBM v. Commissioner, (IBM)*³ the Commission and IBM reached a settlement which avoided jurisdictional objections by IBM.⁴ The settlement presents issues concerning the jurisdiction of EEC institutions over multinational corporations which violate the competition rules of the EEC. In addressing these issues, this Note will begin with a background examination of the EEC competition rules. Next, this Note will consider the history and suspension of the Commission’s investigation into IBM’s practices within the EEC. The jurisdictional issues presented by IBM will be analyzed through a comparison of the two different approaches to the "effects test" taken by the United States and the EEC.⁵ This Note will first show that the EEC has evolved a concept of jurisdiction akin to the "effects test," but which remains based in territorial principles. IBM, therefore, is significant as an example of the limits of EEC jurisdiction under current theory. Finally, this Note will conclude from the IBM undertaking that the EEC, in cases involving large multinational corporations, will probably try to settle cases to avoid jurisdictional problems.

¹ The EEC was formed on March 25, 1957 with the signing of the Treaty Establishing the European Economic Community. March 25, 1957, 298 U.N.T.S. 3 done at Rome, Jan. 1, 1958 [hereinafter Treaty of Rome]. The EEC currently consists of twelve Member States: Belgium, France, Italy, Luxembourg, the Netherlands, West Germany, Ireland, the United Kingdom, Denmark, Spain, and Portugal.

The EEC is one of three organizations which together form the European Communities. In addition to the EEC, there is the European Coal and Steel Community (ECSC) and the European Community of Atomic Energy (EURATOM). See *generally ABA ANTITRUST SECTION, ANTITRUST LAW DEVELOPMENTS* (2d. ed. 1984) [hereinafter ABA ANTITRUST].

² All three communities are under the administration of the Commission of the European Communities. See *generally Treaty of Rome, supra* note 1, at arts. 155–63. See Regulation 17, art. 15(1), *reprinted in 1 Common Mkt. Rep. (CCH) § 2541 (Council Feb. 6, 1962)*. The Commission consists of fourteen members from the Member States and has power to enforce EEC antitrust policy by investigations, proceedings, and fines. It may issue cease and desist orders and impose fines to enforce these orders.


⁴ See *infra* text accompanying notes 52–60.

⁵ See *infra* text accompanying notes 45–60.
II. BACKGROUND OF COMPETITION RULES IN THE EEC

In 1957, the Treaty of Rome established the EEC. The principle objective in establishing the EEC was to unify the economies of Member States into an integrated Common Market. This objective is evident in the EEC competition rules. Articles 85(1) and (2) of the Treaty of Rome declare agreements and concerted practices between businesses void if they are intended to restrict competition and consequently affect trade between the Member States of the EEC. Article 86 bans abusive practices by enterprises enjoying a "dominant position" within the EEC.

To discern whether the ban in Article 86 applies, it is necessary to consider first, whether an enterprise's practices are abusive, and second, if the enterprise holds a dominant market position. If an activity is found to be an abusive practice, the next issue is whether the entity in question maintains a dominant position in the EEC. The European Court of Justice (European Court) has held that a dominant position exists if certain factors are present. For example,

6 See supra note 1.
7 Id.
8 Article 85(1) states:
   1. 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 objective or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:
      (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.

   Treaty of Rome, supra note 1, at art. 85.
9 Id. at art. 86.
10 Article 86 of the Treaty of Rome prohibits practices which consist of the following:
   (a) the direct or indirect imposition of any inequitable purchase or selling prices or of any other inequitable trading conditions;
   (b) the limitation of production, markets or technical development to the prejudice of consumers;
   (c) the application to parties to transactions of unequal terms in respect of equivalent supplies, thereby placing them at a competitive disadvantage; or
   (d) the subjecting of the conclusion of a contract to the acceptance, by a party, of additional supplies which, by their nature or according to commercial usage, have no connection with the subject of such contract.

   Treaty of Rome, supra note 1, at art. 86.
11 See infra note 13.
12 The European Court of Justice in Luxembourg is the final interpreter of the Treaty of Rome and has the power to review the decisions of the Commission. See ABA ANTITRUST, supra note 1, at 975.
if an enterprise controls up to forty-seven percent of the market for its product when the next nearest competitor has a significantly smaller market share, that enterprise may be in a dominant position. In addition to market share, the enterprise's technological lead over its competitors, its sales network and an absence of competition are factors relevant to determining dominance. If an enterprise's activity is found to be an abusive practice of its dominant market position, such a practice is void and will not fall within the exemption from competition rules allowed in Article 85(3). Article 85(3) allows the Commission to exempt an enterprise from Article 85(1) if the enterprise's practices have certain beneficial consequences, though these practices have restrictive effects on trade. The Commission may also grant a negative clearance to the enterprise. The negative clearance declares that its practices do not contain the grounds necessary for the Commission to act under Articles 85 and 86.

The Treaty of Rome, through the centralizing of administration, has advanced towards its goal of a unified system of trade within the EEC. Many of the largest corporations active in the EEC, however, are subsidiaries of multinational corporations with origins outside of the EEC. This situation presents

---


14 See Hoffman-La Roche, supra note 13, at 219.

15 Id.

16 Article 85(3) of the Treaty of Rome allows the Commission to grant an exemption from Article 85(1) if certain conditions are satisfied. Article 85(3) provides:

3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of:
   - any agreement or category of agreements between undertakings;
   - any decision or category of decisions by associations of undertakings;
   - any concerted practice or category of concerted practices;
   - which contributes to improving the production or distribution of goods or to promoting technical or economic progress while allowing consumers a fair share of the resulting benefit, and which does not:
     (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
     (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

Treaty of Rome, supra note 1, at art. 85(3).

17 Id.

18 The "negative clearance" is a declaration from the Commission that an agreement provides no grounds for it to act under Article 85(1) or Article 86. The Commission issues such letters pursuant to Article 85(3) and its powers under Regulation 17, art. 2.

19 Id.

a jurisdictional problem for the EEC because an enterprise’s activity, which affects trade within the EEC, may occur partially or completely outside EEC territory. For example, International Business Machines (IBM), a United States corporation, has a market share of two-thirds of computers sold in the EEC.\textsuperscript{21} IBM’s status as a multinational corporation presents the issue of the extent of the Commission’s jurisdiction over an activity which affects trade within the EEC, but which occurs partially or completely outside EEC territory.\textsuperscript{22}

III. \textit{IBM v. Commissioner}

\textit{IBM v. Commissioner} began with a letter sent to IBM from the Commission on December 19, 1980. This letter contained a Statement of Objections, by the Commission’s Director General for Competition to IBM.\textsuperscript{23} The Statement charged IBM with violating Article 86 of the Treaty. In particular, the Statement alleged that, in marketing its System/370 mainframe computer, IBM: 1) failed to supply other manufacturers with technical information quickly enough to allow them to produce competitive products for use with the System/370; 2) offered its System/370 central processing units (CPU) with a memory in excess of what was needed for testing and that extra memory was included in the purchase price; 3) offered the System/370 CPUs with software in excess of the basic requirements, which excess software IBM included in the purchase price; and, 4) refused to offer software installation services to customers who used a competitor’s CPU with IBM software.\textsuperscript{24}

IBM applied to the Court of Justice of the European Communities for permission to appeal.\textsuperscript{25} IBM objected to the Commission’s investigation on three grounds. First, the Commission failed to consider international comity where many of the acts concerned occurred outside of the EEC and in the United States.\textsuperscript{26} Second, the Statement of Objections breached the rights of the defendant by reserving to the Commission the power to make further objections.\textsuperscript{27} Finally, the full Commission did not adopt these charges against IBM.\textsuperscript{28} The Court dismissed IBM’s application and refused to hear an appeal until the

\textsuperscript{21} See, \textit{Coming to Terms with Big Blue}, \textit{Time}, Aug. 13, 1984 at 73.

In the area of high technology, Western Europe had a trade deficit of ten billion dollars in 1982. The U.S. and Japan together hold 80% of the world market in electronic microprocessing. See \textit{Falling Back in a Critical Race}, \textit{Time}, Aug. 13, 1984, at 72.

\textsuperscript{22} See infra text accompanying notes 41–60.


\textsuperscript{25} See \textit{supra} note 23.

\textsuperscript{26} \textit{IBM, supra} note 23, at 638–39.

\textsuperscript{27} \textit{Id.} at 638.

\textsuperscript{28} \textit{Id.}
Commission reached a final decision. Consequently, the issue of jurisdiction over IBM’s actions in the United States was never addressed.

Formal hearings before the Commission began in February, 1982 and again in June, 1983. Negotiations between IBM and the Commission took place after the first hearing and led to an agreement on August 2, 1984. On August 2, 1984, Commissioner Andriessen announced in a letter that the Commission would accept marketing policy changes proposed by IBM in an undertaking and would suspend the ten year investigation of IBM.

According to the Undertaking,

> [if IBM first announces a new System/370 product outside the EEC, for which it is or will be seeking orders for delivery within the EEC, then IBM will either announce such product within the EEC on the same date as such announcement outside the EEC, or treat that date as if it were the date of announcement within the EEC for the purpose of this Undertaking.]

In addition, IBM will make available its System/370 central processing units without main memory, or with only such memory capacity as is strictly required to allow testing of the CPU. IBM will make “interface” and “attachment” information available within 120 days of its announcement of a new or modified product. The Undertaking will not require IBM to respond to requests for information before expiration of the relevant time period and after expiration, IBM will have fifteen days to respond to requests. IBM will reserve the right to supply interface information subject to “certain conditions” necessary to ensure the protection of “IBM’s legitimate interest.” IBM will also supply information to the Commission, at the Commission’s request, to allow the Commission to determine the extent to which IBM is implementing the Undertaking. Finally, the Undertaking will not be enforceable by the Commission or any other national authority or agency and any future actions against IBM would rely exclusively upon Articles 85 and 86 of the Treaty.
IV. Development of the Effects Test of Jurisdiction in the EEC

The first provision of the Undertaking, concerning introduction of new products, is the most significant concession from IBM for the purposes of analyzing the development of jurisdiction doctrine in the EEC. In this provision, IBM agreed to treat System/370 products announced outside of the EEC as if the announcement occurred inside the EEC. This removes, by agreement, potential nullification of the timetable for information release to which IBM agreed. Without this concession, IBM, by introducing its products outside of the EEC and allowing the interface information to trickle into the EEC, could delay the introduction of information into the EEC. This result would be detrimental to its competitors in the EEC. Given the current development of principles of EEC jurisdiction, such an action would place IBM beyond Commission jurisdiction. Although the Commission has asserted its jurisdiction over actions outside of the EEC which have effects on trade within the EEC, this view has not yet been accepted by the European Court. Instead, the European Court has developed a jurisdiction test which is in essence a modified effects test more limited in reach than the effects test used by the United States.

In the United States, the “effects test” for jurisdiction originated in United States v. Alcoa, where Judge Learned Hand held that U.S. courts may assert jurisdiction over actors and actions outside of U.S. territory if they create anticompetitive effects within the United States. This use of jurisdiction derives from the objective territorial principle. Commentators, however, do not consider it to be a legitimate use of that doctrine. U.S. courts have used the “effects test” to claim jurisdiction over foreign parties acting outside the territory of the United States if these actions have effects within the United States.

40 Id. at 152.
42 See supra note 21, at 73.
43 See infra text accompanying notes 52–60.
44 See infra note 56.
45 See infra text accompanying notes 45–60.
46 148 F.2d 416 (2d Cir. 1945).
47 Id. at 443.
48 See J. Atwood & K. Brewster, Antitrust and American Business Abroad (2d ed. 1981) 157. Traditionally, territorial inhibitions were overcome only when the State itself was the victim of the unlawful conduct, or when the conduct was commonly accepted as criminal by the nations concerned and, for some reason, the criminal had not been subject to prosecution by the state where the offense occurred. It was thus questionable whether exception to the general presumption of territoriality could be readily stretched to include matters of economic policy on which nations differed.
49 Id.
50 In re Uranium Antitrust Litigation, 617 F.2d 1248 (7th Cir. 1980).
While the broad scope of this principle was recently narrowed in *Timberlane Lumber Co. v. Bank of America*, the test has produced considerable objections from outside the United States.

In the EEC, the Commission has begun to assert its jurisdiction by using the effects test. The Commission, in *Commission v. Imperial Chemical Industries*, asserted that if the practices of an enterprise had an effect on EEC trade, there was "no need to examine whether the enterprise which is the cause of these restrictions of competition have their seat within or outside the Community." In its initial decision, the Commission decided that the practices in question constituted a conspiracy to fix the price of dyes sold within the EEC. The Commission claimed that it had jurisdiction, in making its decision, over a corporation which was based outside of the EEC. In an appeal to the European Court, the Commission used the effects doctrine as an alternate ground for jurisdiction. It claimed, as a primary ground for jurisdiction, that the foreign corporation was constructively present in the EEC through its subsidiaries. The Court agreed that the defendant was present in the EEC through its subsidiary and found that the Commission had jurisdiction over the parent located outside of the EEC.

Further, in *Europemballage Corp. v. Commission*, Continental Can, a U.S. corporation, incorporated Europemballage as its subsidiary in Europe. Continental Can, through Europemballage, engaged in a series of takeovers of companies in the EEC. Due to these takeovers, the Commission charged Continental Can with violating Articles 85 and 86. In an appeal to the European Court, the Court held, as it had in *Imperial Chemical Industries*, that the parent corporation

---

51 549 F.2d 597 (9th Cir. 1976). The Court suggested a conflicts-of-law analysis by which U.S. courts could determine whether they have jurisdiction over foreign parties. Id. at 614. Subsequently, the Third Circuit adopted the *Timberlane* approach in *Mannington Mills v. Congoleum Corp.*, 595 F.2d 1287 (3d Cir. 1979). Some factors the Third Circuit considered important to a court contemplating asserting jurisdiction were: “1. Degree of conflict with foreign law or policy; 2. Nationality of the parties; and 3. Relative importance of the alleged violation of conduct here compared to that abroad . . . .” Id. at 1297-98.

52 See J. Atwood & K. Brewster, supra note 47 at 102-06. U.S. assertion of jurisdiction has resulted in foreign legislative action designed to block discovery connected to U.S. proceedings. Id.


54 Id. at 593.

55 Id. at 628.

56 Id. at 628-30.

57 Id. The Court did not adopt the Advocate General’s position in favor of the effects test but rested its judgment on the conclusion that the defendant acted within the territory of the EEC through its subsidiaries.


59 Id. at 202.

60 Id. at 202-05.
was constructively present in the EEC through its subsidiary and consequently, that the Commission had jurisdiction over the foreign defendants.61

The European Court, by holding a parent corporation to be constructively present in the EEC through its incorporated subsidiary, was able to expand the Commission's jurisdiction over foreign corporations, while theoretically maintaining adherence to the territorial principle of jurisdiction. Under such a modified effects test, the Commission probably could have successfully asserted jurisdiction over IBM. Specifically, the Commission could have claimed that IBM, through its act of introducing the System/370 in the EEC was constructively present in the EEC. A difficulty with this solution, however, is that it is limited in effectiveness to the product at issue. For example, if IBM introduced a new computer system outside of the EEC it is likely that this system will enter Europe at some point. Probably, orders for IBM products from the EEC will introduce the new product to EEC consumers.62 This is likely because IBM is the largest computer maker in the world, and has two-thirds of the EEC computer market.63 But by introducing a system abroad, IBM can argue that the Commission has no jurisdiction over it because it is a foreign corporation acting outside of EEC territory.64 The Commission may not be able to attain jurisdiction over IBM, though IBM's actions may have significant effects within the EEC, because the Court has yet to adopt the effects test.65

V. CONCLUSION

The Commission and the European Court, in order to acquire jurisdiction over IBM when its actions occur abroad, may have to widen the scope of its jurisdiction test to a degree approximating the scope of the effects test used by the United States. This expansion will probably weaken the link the European Court has maintained, in its decisions to date, with traditional territorial principles. A move away from the territorial principles of jurisdiction, however, is not one that the European Court is prepared to undertake despite the Commission's arguments on its behalf.66 By remaining with the premise that action must take place within the territory of the EEC to confer jurisdiction on the Commission, the Court is limiting the jurisdiction of the Commission. The Commission has avoided this limit in jurisdiction by agreement with IBM. IBM has agreed to treat products announced outside the EEC as if they were an-

61 Id. at 221–22.
62 See supra note 41.
63 See supra note 21.
64 See supra note 40, at 195–95.
65 See supra text accompanying notes 52–57
66 Id.
ounced within the EEC. In essence, IBM has agreed that the Commission has jurisdiction over computer products it introduced outside the EEC. Until the European Court formally adopts the effects test of jurisdiction, the Commission may, in the future, seek other such agreements to its jurisdiction from multinational corporations based outside of the EEC and whose activities affect trade in the EEC.

Margaret Lo

67 See supra text accompanying note 29.