

Considerations of Non-price Vertical Restraints under the Rule-of-Reason Standard and within the Legal Structure of the Fair Trade Act

Abstract

Key Words: non-price vertical restraints, the Fair Trade Act, rule of reason

This project re-examines the current regulatory framework for non-price vertical restraints under the Fair Trade Act. Tying, territorial and customer restrictions, and exclusive dealing are the main types of arrangements that will be studied. The project begins with a review of the economic rationale underlying the need to regulate non-price vertical restraints under competition law as well as its limits. Using comparative-law approach, we then compare the U.S. and EU competition laws on non-price vertical restraints and investigate whether useful policy guidelines could be drawn from this study. The tentative research results will then be applied to inspect how the problems arising from the current regulatory framework under the Fair Trade Act could be improved or solved. We conclude this project by providing specific factors that could assist the Taiwan Fair Trade Commission (TFTC) to determine the legality of non-price vertical restraints under the rule-of-reason standard and within the legal structure of the Fair Trade Act (FTA).

As the FTA has mandated the application of the rule of reason to vertical non-price restraints, we did not observe the transformation of reviewing standards in Taiwan as was experienced in the United States and the European Union. However, unlike the approaches adopted by the United States and European Union, the TFTC has never reviewed a non-price case under the typical antitrust provision, Article 10 of the FTA. In fact, there appears to be a tendency for the TFTC to apply the more conduct-based Article 24 to vertical cases. Although it could significantly alleviate the burden of delineating relevant market and measuring market power by the TFTC, such an enforcement trend could cause legal uncertainty in the long run. We suggest that the TFTC should refocus on using more effect-based approaches to evaluate the legality of vertical restraints under the FTA. We also suggest that Article 19 be revised to abandon the requirement that limits the reviewable conducts to arrangements between “enterprises.”

Based on our preliminary findings, we propose the following factors that should be taken into accounts when operating the rule of reason in cases regarding vertical non-price restraints. Among those factors, we argue

that the defendant's market power should be the

primary concern for the TFTC and need to be assessed first. The various methods of defining and measuring market power introduced in this project offers the TFTC a start point to conduct market-power evaluation. Alleged violations passing the market-power threshold will then be reviewed to discover whether they have the anti-competitive effects suggested by the foreclosure and cartel-facilitating theories. The factors need to be considered in the foreclosure investigation include:

1. the ease of market entry;
2. the existence or non-existence of minimum efficient scales for firms to engage in effective competition;
3. countervailing power on the buyers' side;
4. the plausibility for competing rivals to adopt counterstrategies.

For cartel-facilitating investigation, the factors need to be considered include:

1. the number of competing firms and the percentage of rivals who adopt same types of vertical restraints;
2. market entry barriers
3. product homogeneity
4. the differences in scales and cost structures among competitors;
5. the frequency and regularity of transactions with downstream firms;
6. the importance of downstream firms to upstream firms;
7. the degree of restrictiveness of the vertical restraints employed.

With respect to the evaluation of pro-competitive justifications, the TFTC should focus on the plausibility of the presumptions that the asserted justifications are based. For example, the justification of avoiding free-riding behavior would be less persuasive when the products involved do not need presale services. Finally, we suggested that the "intent" or "purpose" requirements should play a supplementary role in the analysis of vertical non-price restraints. The TFTC needs to consider this subjective requirement only when the previous effect-based investigations fail to provide definite answers. In addition, we also propose that the TFTC may adopt the "price-cost" test employed in price-predation cases to determine the existence of intent in vertical cases.