

Out Of Court Settlements: The Second Best Solution

BY CÉCILE PHILIPPE

Judge Bo Vesterdorf recently announced that the European Court of First Instance would decide on Dec. 18/20 whether to accept Microsoft's appeal to suspend EU sanctions against the U.S. software giant.

In March 2004, the European Commission ruled that Microsoft had abused its dominant market position and ordered the company to pay a fine of 462 million euro and remove its Media

Player software from the Windows operating system. The sanctions have been suspended until the appeal.

Also discussed was the fact that US based Novell and the Computer and Communications Industry Association (CCIA) recently received multimilliondollar outofcourt settlements from Microsoft.

These settlements have been highly criticized because they seem to make everybody happy, except the consumer. Allegedly, such

out of court settlements will not prevent a company from being in a dominant position, thus harming the consumer.

The neoclassical theory of monopoly pricing is a tool that has proven very efficient for politicians defending the idea that political action and sanctions can defend the interest of consumers against dominant companies.

Having only one seller on the market is harmful because he will automatically take advantage of his position, limiting the quantity of the product available in order to sell at the highest price. He could therefore maximise his revenue at the expense of the consumer.

Despite this rationalisation, the European Court of Justice has repeatedly required better evidence of damage done to consumers.

These are legitimate claims, because antitrust policy based on the theory of monopoly pricing is completely flawed.

This theory ignores how markets work in the real world. In reality, people are free to enter any market. This means that the dominant



A happy settlement but bad news for the rest of us

seller has to be competitive not only compared to existing rivals but also compared to competitors likely to enter the market.

This may be true say the opponents, but a new entrant may not be able to operate

profitably because the dominant company has responded to his entry with predatory pricing, i.e. offers targeted aggressively at the potential customers of the competitor.

It isn't enough that entry is

free: many economists believe that markets are all the more competitive if entry and exit costs are low. To them, free entry means easy access.

However, competition without barriers is nonsensical. As argued in

the last economic note "The Shaky Foundations of Antitrust Policy," by the Molinari Economic Institute, "the common characteristic of all non legal obstacles is that they highlight the threat of losses for potential entrants." So as not to make allocation completely arbitrary, such market barriers as "predatory" pricing and experience are necessary. At stake is the fulfilment of the most "urgent" consumer needs.

Therefore, policies that aim at preventing monopoly pricing are unfounded. True, out of court settlements are not in the best interest of the consumer but not for the reasons commonly suggested by economists.

But they are the best means companies have found to avoid harmful penalties imposed by the court and carried by the consumer. However, they may become unnecessary if the European Court of Justice is ready to make decisions based on sound economics.

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