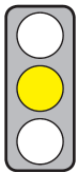
ABUSIVE EXCLUSIONARY CONDUCT BY DOMINANT UNDERTAKINGS

Status: 09.03.09

MAIN ISSUES

Objective of the Communication: The aim of the Communication is to provide "greater clarity and predictability" on the criteria the Commission uses to decide whether to pursue cases of exclusionary conduct. The Commission also wants to give companies clues as to what constitutes exclusionary conduct.

Groups affected: Dominant undertakings, their suppliers and customers, consumers.



Pros: (1) On the whole, it is appropriate to talk of exclusionary conduct only if a given behaviour can be proven to foreclose the market in question.
(2) The tests suggested by the Commission provide useful clues to detect anticompetitive conduct.

Cons: (1) Reduced legal certainty as well as costlier and more complex procedures are the inevitable price for the decision to no longer prohibit certain forms of behaviour "per se", but to evaluate the effects of such behaviour on a case-by-case basis.
(2) At least verbally, the Commission adheres to its plan to examine not only impairments of competition, but also of the allegedly measurable "consumer welfare".

CONTENT

Title

Communication COM(2008) 832 of 5. December 2008 in its revised version **C(2009) 864** of 18. February 2009 on Guidance on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings

Short Summary

- **Subject matter of the Communication**
  The Communication refers to exclusionary conduct leading to the "foreclosure" of markets that are dominated by a single company.

- **Dominant market position**
  - A company is in a dominant market position if it is able – due to low or non-existing competitive pressure – "to behave to an appreciable extent independently of its competitors, its customers and ultimately of consumers".
  - A market share of 40% or more is an important, but not a sufficient indicator of a dominant market position. If the market share of a company is below 40%, it is "not likely" to be in a dominant position.
  - Imminent or expectable market entries or expansions of competitors, as well as the existence of customers with a high level of countervailing buyer power, speak against a dominant market position.

- **Anticompetitive foreclosure**
  - Anticompetitive foreclosure of a market means that a dominant company
    - hampers or elimates, as a result of its conduct, the access of existing or potential competitors to supplies or markets, and
    - is thus "likely" to be in a position to profitably increase its prices to the detriment of consumers.
  - What is decisive for the openness of a market for competition is whether a hypothetical company that produces the respective goods or services as efficiently as the dominant company ("as efficient competitor") could compete on the market.
  - One important variety of foreclosure consists in a company's offering its products below cost in order to keep competitors out ("price-based exclusionary conduct").
    - To find out whether a company engages in below-cost-pricing, the Commission collects information on the costs of such a company or, if the latter is unavailable, cost data of competitors or "other comparable reliable data".
    - Sales prices below the costs the company would have saved if it had not produced a discrete amount of extra output ("average avoidable costs", AAC) indicate that any competitor is foreclosed from the market.
    - Sales prices below the average of all fixed and variable incremental costs a company incurs to produce a discrete amount of a product ("long-run average incremental costs", LRAIC) indicate that an "as effective competitor" could be possibly foreclosed from the market.

- **Frequent types of exclusionary conduct**

Exclusive dealing (exclusive purchasing and conditional rebates)

– Dominant companies use exclusive purchasing obligations to require customers on a particular market to purchase exclusively or to a large extent only from them.
– Exclusive purchasing obligations may in particular have a foreclosing effect if they are stipulated at a moment when competitors are not or not fully able to provide the spectrum of goods and services offered by the dominant company.
– Conditional rebates are granted to customers to reward them for their purchasing behaviour.
– For the Commission, a foreclosing effect of a rebate scheme is the more likely,
  - the higher the rebate as a percentage of the total price is, and
  - the higher the turnover threshold is that must be reached to benefit from the rebate.
– In the Commission's view, a "maximum loyalty enhancing effect" is generated by a rebate that is individually tailored to each customer, depending on the total amount of his purchases.
– But rebates are unobjectionable if the price which a customer would have had to pay a competitor to purchase a certain amount of products ("effective price"), is constantly higher than the LRAIC the dominant company incurs to produce the same amount of products.

Tying and bundling

– Tying consists in requiring a customer, when purchasing one product from a dominant company, to purchase also another product.
– Bundling refers to situations where a company sets the price for a product bundle lower than the sum of the prices of each individual product.
– The Commission considers tying and bundling as possibly anti-competitive when
  - the products in question can be manufactured independently of each other,
  - they are typically bought separately by consumers and are usually not tied or bundled by other companies either, and
  - the practice is part of a lasting tying or bundling strategy of the dominant company.
– Rebates on product bundles may be anti-competitive if "as efficient competitors" that offer only one of the bundled products are unable to compete with the sales price resulting from the rebate.
– If the hypothetical individual price for a product that was made part of a bundle is constantly higher than the LRAIC, the bundling is unobjectionable. For under these circumstances, "as efficient competitors" should be able to replicate similar bundles while covering their costs.

Predatory pricing

– Exclusionary conduct by predatory pricing consists in a dominant company deliberately incurring losses or foregoing profits in the short term so as to foreclose competitors from a market and maintain its market power.
– The measure of comparison is the profit situation that would have resulted from a "reasonable alternative conduct". However, the actual behaviour of the company is not to be compared to "hypothetical or theoretical constellations" that "might have been more profitable".
– The Commission deems a predation strategy harmful if it is to be expected
  - that the prices will subsequently rise beyond their original level, or
  - that a price reduction that "would otherwise have occurred" will be prevented or delayed.

Refusal to supply and margin squeeze

– A refusal to supply a customer can be unlawful if by this means a dominant company wants to:
  - put a customer whose products compete with the company's own on a downstream market, at a disadvantage, or
  - punish a customer for certain behaviour.
– Equivalent to a refusal to supply is the setting of prices for a product on an upstream market that makes it economically impossible for customers to compete with the dominant company's products on a downstream market ("margin squeeze").
– Since a duty to supply would mean a breach of the freedom of contract, and given that the possibility of such interventions is sufficient to reduce incentives to invest and innovate, the Commission thinks such interventions "require careful consideration".
– The supplies withheld must therefore be "objectively necessary" for effective competition to unfold on a downstream market.

- **Defences for dominant companies**

– A company may plead "objective necessity" or efficiency grounds without, below the line, causing harm to consumers to defend a behaviour deemed to have a foreclosing effect. The burden of proof is on the company. By way of example, the Commission discusses as possible justifications that:
  - a rebate scheme is linked to certain turnover thresholds that are not individually set for each customer and whose effect is to increase the quantities of a good that are produced and sold;
  - a product bundle saves customers costs, since they would otherwise have to purchase the components of the bundle individually, or leads to savings in packaging and distribution costs;

- refusals to supply are a necessary condition for innovation and certain investments of the dominant company.

Changes Compared to the Status Quo

Up to now, the Commission has never presented a Communication laying down its principles on dealing with exclusionary conduct.

Statement on Subsidiarity

The Communication does not address the matter of subsidiarity.

Political Context

To prepare the Communication, the Commission has presented a voluminous discussion paper already in December 2005, which drew more than a hundred comments from interested companies and trade associations (http://ec.europa.eu/competition/antitrust/art82/contributions.html).
Since the end of the 1990s, the Commission is working to introduce a "more economic approach" into European competition law. The Commission has already issued guidelines for the assessment of cartels and mergers that are heavily influenced by this idea. The present Communication is to extend this approach to the abuse of dominant market positions. The main idea of the Communication, which is to pursue only cases in which a certain behaviour can be shown to have foreclosing effects, already determined the Commission's stance in the cases Deutsche Telekom (Decision of 21.05.2003 – COMP/C-1/37.451, 37.578, and 37.579), Microsoft (Decision of 24.03.2004 – COMP/C-3/37.792), and Telefónica (Decision of 02.07.2007 – COMP/38.784).

Options to Influence the Political Process

Leading Directorate General: DG Competition

ASSESSMENT

Economic Impact Assessment

Ordo-Liberal Assessment

The concentration of private power in dominant companies puts competition at substantial risk. **A strict control of dominant companies' behaviour is** thus **indispensable. But theses companies have a legitimate interest that competition authorities act in a predictable manner.**
Reduced competition generally also harms consumers. Yet, an alleged "consumer welfare" cannot serve as the main focus of analysing competition, since it cannot be measured.It is not clearly evident to which extent **the Commission is abandoning earlier ideas to make consumer harm the cornerstone for** a possible **abuse of market power**. Although the Commission no longer explicitly calls for complex economic models which hitherto have been related to its concept of a "more economic approach" in competition law, it neither distances itself from it. Applying such models which are based on many assumptions tends to adversely affect legal certainty.
In principle, it is appropriate to speak of exclusionary conduct when a foreclosing effect can be shown to exist in a given case. A rule that prohibits "per se" certain forms of behaviour of a company in a dominant position necessarily includes a number of cases that do not lead to any restriction of competition.

Impact on Efficiency and Individual Freedom of Choice

The criteria proposed by the Commission to evaluate the most important types of exclusionary conduct represent useful clues for anti-competitive behaviour, but do not make decisions easier. Some criteria are imprecise: For example, the scale against which rebates are to be measured does not allow to define the point where exactly unobjectionable behaviour becomes exclusionary conduct. Equally fuzzy is the requirement that refusals to supply and margin squeezes be deemed unlawful when the supplies withheld are "objectively necessary" for effective competition to unfold on a downstream market.
At first sight, the tests the Commission proposes to evaluate whether a company engages in predatory pricing, excessive rebates or selling product bundles too cheaply promise greater precision, since their idea is to measure prices against clearly defined sets of costs. But the quality of decisions based on such rules depends on whether the costs of the dominant company can be plausibly investigated. If the costs of the dominant company are not known, or if the credibility of available cost data is doubtful, the Commission really does not have any reference to compare prices with those of an "as efficient competitor". Data supplied by competitors of the dominant company are questionable since those competitors promote interests of their own.
The intention to do justice to individual cases, which underlies the proposed tests, **could** in the end **force the Commission to resort** even more often **to the confiscation of sensitive business data** at company headquarters. Costlier and more complex procedures, which may also lead to reduced legal certainty, are the inevitable price for the decision to no longer fight certain types of behaviour of dominant companies as such.

Impact on Growth and Employment

Not appreciable.

Impact on Europe as a Business Location

Following the Communication, several differences between antritrust practice in the EU and the United States persist, e.g. in terms of the assessment of predatory pricing strategies. But since competition law rules always apply equally to all companies that are active on the same market, such differences do not affect the quality of the EU as a business location.

Legal Assessment

Legislative Competence

Art. 82 EC lays the enforcement of EU competition law into the hands of the Commission. Therefore, the latter is also entitled to formulate principles that guide its own action in this field.

Subsidiarity

Since the Communication is not binding upon the national competition authorities, it does not constitute a breach of the principle of subsidiarity.

Proportionality

No problem.

Compatibility with EU Law

Strictly speaking, the Communication only concerns the question what use the Commission is to make of its discretion as to the cases of market abuse it wants to pursue. However, the Communication largely appears like a guidance paper regarding the correct understanding of Art. 82 EC, and the ideas laid out therein might well find its way into the jurisprudence of the Court of First Instance and the European Court of Justice (ECJ).
The Communication sometimes deviates from the existing jurisprudence of the ECJ. So far, the ECJ tended to see exclusive purchase obligations of dominant companies as per se unlawful (Case 85/76, Hoffmann-La Roche), while the Commission wants to assess them in a more differentiated manner. To assess predatory pricing, the Commission draws on certain cost categories that deviate slightly from the ones used by the ECJ (Case 62/86, AKZO Chemie). This can lead to different results when several products and not just one product of the dominant company are taken into consideration. So far, the ECJ has rather evaluated rebate schemes of dominant companies in terms of a per se prohibition than in the light of the foreclosing effects they have (Case C-5/94, British Airways).
The proposed opportunity for dominant companies to invoke efficiency grounds for their behaviour should be seen in a differentiated manner: Art. 82 EC does not allow justifying an already established abuse of market power by any efficiency gains resulting from it. What is compatible with EU law, however, is to take efficiency gains into consideration when assessing whether a certain behaviour constitute an abuse. The examples set forth by the Commission show, however, that general statements in this matter are hardly possible, and only case law can gradually shed more light on situations where an efficiency defence may be admissible.

Compatibility with German Law

The Communication cannot prevent the Bundeskartellamt (German Federal Cartel Office) from setting stricter criteria for the prosecution of exclusionary conduct (Art. 3, para. 2, sentence 2 of Regulation 1/2003). If the Bundeskartellamt was to consistently ignore the criteria laid down in the Communication, it is theoretically conceivable that the Commission might use its power to initiative proceedings of its own, thus relieving the Bundeskartellamt of its jurisdiction (Art. 11 para. 6 of Regulation 1/2003). But such a scenario appears improbable, for the enforcement of EU competition law depends on the willingness of national competition authorities to cooperate with the Commission.

Alternative Policy Options

Not apparent.

Possible Future EU Action

Not apparent.

Conclusion

It is reasonable to see behaviour as abusive only if it can be shown to have foreclosing effects. What matters are tests that are adapted to practical needs and allow for a fair assessment of individual cases. However, as an inevitable consequence of a case-by-case approach, costlier and more complex procedures and possibly a reduction of legal certainty are to be expected. All the more important would it be if the Commission clearly rejected to use complex economic models to measure “consumer welfare“, which it originally planned to introduce. However, in its Communication it remains unclear which relevance “consumer welfare“ will have in examining exclusionary conduct.