ABUSE OF DOMINANCE

From the viewpoint of the Italian Competition Authority

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The views expressed here are personal and do not necessarily reflect those of the Italian Competition Authority

SUMMARY

- Legal provision (Art. 102 TFUE)
- Notion of undertaking

DOMINANCE

- Definition
- Assessment

ABUSE

- Legal notion
- Types of abuse

EXPLOITATIVE ABUSES

- Excessive pricing
- Italian case: Alitalia (2001)
- Economic issues of exploitative abuses

EXCLUSIONARY ABUSES

- Economic issues of exclusionary abuses
- Tools
- Italian case: Telecom Italia (2013)

Legal provision (Art. 102 TFUE)

- Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States

Pre-requisites

- There must be an undertaking
- The undertaking must hold a dominant position in the relevant market
- There must be an abuse of the dominant position
- The abuse must affect trade between Member States

Notion of Undertaking

- The concept of an undertaking encompasses every entity engaged in an economic activity, regardless of the legal status of the entity and the way in which it is financed (*Hoefner and Elser v Macroton GmbH*, CJ 1991)
- Economic activity consists in offering goods or services in a given market (*Pavlov*, CJ 2000)

  - trade associations, natural persons, public authorities, state-owned corporations, quasi-governmental bodies are undertakings as long as engaged in economic activities
  - no need for a profit-making business for an entity to be considered “engaged in an economic activity”

Dominance

Definition

- “Position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers” *(ECJ in United Brands v Commission, Case 27/76, 1978)*
- For dominance to exist the undertaking must at least have a “**substantial market power**”: the power to maintain prices above the competitive level for a significant period of time and/or to influence the parameters of competition (prices, output, variety or quality of goods and services…) to the detriment of consumers
- Dominance is a prerequisite for intervention, not an offence in itself

Assessment

Factors that may constrain the exercise of market power:

- actual **competitors** (focus on the market position of the dominant undertaking and its competitors)
- **entry** of potential competitors (analysis of expansion and entry conditions)
- customers (**countervailing buyer power**)

Competitors

- Dominance is more likely if the company holds a high **market share** (in terms of turnover, quantities, production capacities) in a fragmented market
- Market shares should be interpreted in the light of market dynamics (durability in fast-moving markets) and product differentiation
- In the case-law of the European Union dominance is not likely if the undertaking's market share is below 40% in the relevant market
- In the United States law two-thirds of the market is a rule of thumb threshold for presuming monopoly power and a market share under 40%-50% is likely to fall within a safe harbour

Entry

- High profits attract entry in the market
- An undertaking can be deterred from increasing prices if the market is contestable
- Likely, timely and sufficient entry
- Low **barriers** to entry
  - regulatory/legal impediments, sunk costs/economies of scale or scope, privileged access to essential inputs, aggressive reputation of the incumbents)

Countervailing Buyer Power

- Market power on the supply side may clash against market power on the **demand side**
- Parameters: size and commercial relevance of buyers, ability to quickly switch to actual or potential competing suppliers
- In the food industry, large retail is very powerful

Abuse

Legal notion

- "*The behavior of an undertaking in a* ***dominant position*** *which through recourse to* ***methods*** *different from those which condition normal competition in the transaction of commercial operators, has the* ***effects*** *of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition*"

  (CJ, *Hoffman – la Roche v Commission*, 1979)

Types of abuse

Exploitative abuse, direct consumer harm

- Excessive pricing

Exclusionary abuse, indirect consumer harm

- Predatory pricing
- Margin squeeze
- Market foreclosure (refusal to deal, exclusive dealing, conditional discounts)

Exploitative abuses

Excessive pricing

- Art. 102 explicitly prohibits a dominant firm from "…directly or indirectly imposing unfair purchase prices or selling prices or other selling conditions"
- In the US case law excludes the possibility to challenge excessive pricing (focus on exclusionary conducts, to prevent market conditions that allow exploitation)

Italian case: Alitalia (2001)

Two domestic routes:

i) Milan-Lamezia Terme (MI-LA)

ii) Milan-Reggio Calabria (MI-RC)

On MI-LA Alitalia was the only player (**monopoly**) and the price was much higher than the price Alitalia itself charged on MI-RC where Alitalia competed with AirOne (**competition**)

Alitalia
I-DISU

Test used

- The “**comparable market**” **test**: comparison between selling price in a monopoly market and selling price charged in a competitive market (the two markets have to be “comparable”….)
- Comparison between **selling price and its costs of production**, which are considered an appropriate proxy of the **economic value** of the service

The procedure confirmed a significant difference between the pricing adopted by Alitalia on the two routes (MI-LA, the monopoly route, and MI-RC, the competitive route) but the evidence was not sufficient to prove that price was unfair

Economic issues of exploitative abuses

Three main reasons for intervention against excessive pricing

- Explicitly provided by Art. 102
- Protects consumer welfare (by fighting monopoly prices)
- In some cases the only possible intervention (if entry barrier are too high)

Three main reasons for non-intervention against excessive pricing

- The temporary opportunity to charge monopoly prices is what justifies risk taking and investments that produce innovation and economic growth
- It is hard to set the threshold: when do prices become excessive? Complex comparison with cost of production and investments
- It is hard to monitor the remedies: risk of a competition authority acting as a quasi-regulator (recurrent analysis at each change of conditions in the industry)

Exclusionary abuses

- Exclusionary abuse is a conduct by a dominant firm that **hampers or eliminates access** of actual or potential competitors to the **detriment of consumers**

- Some jurisdictions apply a *formalistic approach*, based on the presumption of anticompetitive effects
- Other jurisdictions apply an *effects-based approach* that requires a careful and often more complex analysis of the potential effects of a particular behaviour
- Most jurisdictions apply a *hybrid approach* that combines a formalistic approach with varying degrees of analysis of effects

Economic issues of exclusionary abuses

In December 2008 the European Commission issued **Guidance on enforcement priorities** in applying Article 102 TFEU to abusive exclusionary conducts whereby endorsed an effects-based approach

Three main pricipleſ

- Dominant companies too should be free to compete fiercely as long as this competition is ultimately for the benefit of consumers
- The Commission must assess the likely effects of the conduct by sound economic analysis and cogent and convincing evidence
- Dominant firms should be allowed to present evidence that conduct is justified by efficiencies that outweigh the negative effects identified by the Commission

Tools

Consumer welfare

- balances the positive and negative effects that a dominant firm's conduct has on consumer welfare

The *no economic sense test*

- analyzes whether the conduct would make no economic sense but for the intention to exclude

The *as efficient competitor test*

- exclusion should be prevented only if affects rivals that are no less efficient than the dominant firm
- Underlying principle: protect competition, not competitors!

Italian case: Telecom Italia (2013)

Abusive conducts by the incumbent in telecommunications markets, Telecom Italia, in wholesale markets for network infrastructure and broadband access

Two separate and vertically integrated markets

- wholesale market (*upstream*): network infrastructure and broadband access, where Telecom Italia is dominant and holds an essential input (the telecommunications network)
- retail market (*downstream*): narrowband access to large business customers, where Telecom Italia competes with other telecommunications providers

Refusal to supply access to Telecom’s network, through refusal of numerous competitors’ orders

- delivery process (organization and management) used by Telecom to provide wholesale services to competitors was different from the one used internally to serve Telecom

Discounted prices to business customers that were not replicable by an **equally efficient competitor** (margin squeeze)

- economic analysis showed that the difference between the discounted prices set by Telecom and the wholesale prices charged to competitors for the essential inputs was not sufficient to cover the incremental costs incurred by an equally efficient competitor to supply the services