ABUSE OF DOMINANCE

John Pheasant

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The Competition Laws

Cartels

Abuse of dominance

Control of mergers

Competition Policy Goals

The Protection of:

- Competitive Markets
- Innovation
- Consumer choice at competitive prices

Market Power

What is market power?

Market Power

The ability to raise or maintain prices above competitive levels

US law refers to the ability to exclude competitors

Who Has Market Power?

Cartel members

Monopolists and dominant enterprises

Who Has Market Power?

Cartel members

Combining individual market positions

acting through collusion or conspiracy

Monopolists and Dominant Enterprises

Monopolist: in theory 100% market share but US law applies to market shares below 100%

Dominant enterprise: economic and legal definitions

Defining Dominance

Economic test: sufficient market power

Legal test:

the ability to act, to an appreciable extent, without regard for competitors, customers or the ultimate consumer

The Economic Test

Market power: you know it when you see it!

Top down and bottom up approaches

Effective competitive constraints

Examine all the evidence

The Legal Test

The test does not preclude some competition to the dominant enterprise

It is necessary to examine a range of factors

Effective Competitive Constraints

What is a competitive constraint?

When is it effective?

Effective Competitive Constraints

"I can raise my price by 10% without losing any customers. My customers have no choice but to buy from me".

Effective Competitive Constraints

"I can raise my price by 10% and will risk losing only 10% of my customers to smaller competitors. The additional revenue from 90% of my customers will outweigh the revenue lost to competitors."

Testing for Effective Competitive Constraints

How would you test for the presence or absence of effective competitive constraints?

Testing for Effective Competitive Constraints

Market share?

Number of competitors?

Market structure?

IP rights?

Entry barriers?

Empirical evidence?

Market Share

Company A sells 25 red widgets and 5 blue widgets

Total sales of red widgets = 50

Total sales of blue widgets = 50

What is Company A’s market share?

Market Share

Depends on the definition of the relevant market

One relevant market = widgets

Two relevant markets = red widgets and blue widgets

Market Share

In a widget market, A’s market share is 30%

In a blue widget market, A’s market share is 10%

In a red widget market, A’s market share is 50%

Defining the Relevant Market

- Product or service market
- Geographic market
- Demand-side substitution
- Supply-side substitution
- Actual and potential competitors

Product or Service Market

Products or services considered by consumers as interchangeable by virtue of their

characteristics

price

intended use

Demand-side Substitution

Are there suppliers of existing products considered by consumers to be interchangeable with red widgets?

Are blue widgets interchangeable with red widgets?

(Actual competition)

Demand-side Substitution

Market research shows that blue widgets are not interchangeable with red widgets

So, does A have a market share of 50% of red widgets?

Supply-side Substitution

Are there manufacturers of similar products who, relatively easily and within a relatively short time, could adapt their production to make a product considered by consumers to be interchangeable with red widgets?

(Potential competition)

Supply-side Substitution

If so, add to the size of the relevant market the production capacity which could be switched to make red widgets

Suppose other manufacturers could switch and make 50 red widgets, the size of the relevant market for red widgets would be 100

A's market share would be 25%

Is that correct?

Geographic Market

Company A manufacturers and sells red widgets in India

50% of the manufacturing capacity which could be switched to make red widgets is in India, but

50% is in Japan

What is the size of the relevant product market?

Geographic Market

It depends on whether the Japanese manufacturers could supply red widgets into India and, if so, at what cost in terms of transportation, customs duties, local distribution, etc

Geographic Market

Suppose the combined cost of transport to India and import duties is very high

The Japanese manufacturers are not able to supply the Indian market at a competitive price

India and Japan would be separate geographic markets

Geographic Market

So, the size the relevant market for red widgets in India is:

50 (actual production in India)

+

25 (potential production in India)

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75 (A's market share is 33.3%)

Relevant market: Summary

Define both:

Relevant product or service market

Relevant geographic market

For this purpose, analyze:

Demand-side substitution and, if necessary,

Supply-side substitution

Testing Demand-side Substitution

Cross-price elasticity of demand

Econometric analysis

The SSNIP test

Empirical evidence

Dominance: Other Factors

Market structure

In the widget market in India, A has a market share of 30%

Is A dominant in the relevant market?

Market Structure

A has a market share of 30%

There are 70 other competitors each with a 1% market share

Is A dominant?

Market Structure

Does the structure of the market mean that A has market power even though its market share is only 30%?

Do the 70 smaller competitors exert effective competitive restraints on A?

Presumption of Dominance

In EU law, there is a ***rebuttable*** presumption that an enterprise with a market share in the relevant market of 50%+ is dominant

But an enterprise with a lower market share may be dominant

40% - 50%: possible

25 – 40%: unlikely but still possible

Less than 25%: almost never

Monopoly in US Law

US law tends to require a higher market share to establish monopoly

Dominance: Other Factors

IP Rights

Confer a legal monopoly

But are only one factor in determining dominance

IP Rights

A patent precludes production or sale of the patented product by others

What is the relevant market in which the patented product competes?

IP Rights

In the red widget market, A has a patent on ***dark*** red widgets and a market share of 50%

There are no patents on ***light*** red widgets which compete with ***dark*** red widgets

There are two manufacturers of ***light*** red widgets, one with a 40% market share and the other with 10%

IP Rights

Despite a market share of 50% and a patent on dark red widgets, it could well be that A is not dominant in the red widget market

Entry Barriers

Can potential competitors enter the market with relative ease?

(Also, barriers to expansion by actual competitors)

Entry Barriers: Examples

IP Rights

High R & D costs

High sunk costs

Tariffs

Lack of available distributors

Entry Barriers

If entry barriers are low, potential competitors may exercise effective competitive constraints

Entry Barriers: Example

Enterprise A manufactures red widgets in Kolkata and sells in northern India only

Enterprise B manufactures green widgets in Kerala and exports all of its production outside India

Green widgets are more expensive to produce than red widgets but perform the same function

Entry Barriers: Example

A’s price is 100

B’s cost of manufacture is 95

B cannot compete on price with A in northern India

Entry Barriers: Example

A wants to raise its price to 110

B can sell in India at 105 and make a reasonable profit

There are no barriers to B selling green widgets in northern India

The threat of B entering the market in northern India constrains A which increases its price only to 104

Empirical Evidence

A number of factors are relevant when assessing whether an enterprise is dominant, i.e. whether it has sufficient market power to be able to act, to an appreciable extent, without regard for competitors, customers or the ultimate consumer

In making an assessment, it is important to examine the empirical evidence

Abuse of Dominance

It is not unlawful to be dominant or even a true monopolist

It is unlawful to abuse a dominant position or monopoly

The US Position

Section 2 of the Sherman Act prohibits:

monopolization and attempted monopolization by a single entity unilaterally and

coordinated monopolization by combination or conspiracy

The US Position

It is illegal to acquire or maintain a dominant share of the market by means that unfairly exclude others

A violation requires proof of the possession of (or dangerous probability of achieving) monopoly power and the use of exclusionary conduct to acquire, enhance, or maintain that power

The EU Position

Article 102 TFEU

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

The EU Position

Such abuse may, in particular, consist in:

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions

(b) limiting production, markets or technical development to the prejudice of consumers

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage

(d) making 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

Types of Abuse

Exclusionary

Exploitative

Exclusionary Abuses: Examples

Predatory pricing

Exclusive dealing

Tying and bundling

Refusal to supply

Margin squeeze

Predatory Pricing

Low prices: good for consumers or bad for competition?

Protecting the competitive process

Predatory Pricing

Low pricing by a dominant enterprise may force competitors to leave the market

The dominant enterprise may then increase prices above the competitive level to the detriment of customers and consumers

But when is low pricing abusive?

Predatory Pricing

Can competitors which are as efficient as the dominant company compete on price?

Pricing below average avoidable cost

presumption of predation

Pricing below long-run average incremental cost

evidence of intent required

Exclusive Dealing

Foreclosing competitors

- exclusive purchase obligation
- exclusive distribution
- conditional rebates

Tying and Bundling

Tying

Enterprise A is dominant in product W

A customer who buys product W (the tying product) is required to buy product X (the tied product)

Tying and Bundling

Bundling

Pure bundling: products Y and Z are only sold together

Mixed bundling: products Y and Z are
also sold separately but the total price of
both is then higher than when purchased
together

Tying and Bundling

Are the products distinct products?

Is the tying or bundling likely to lead to anticompetitive foreclosure?

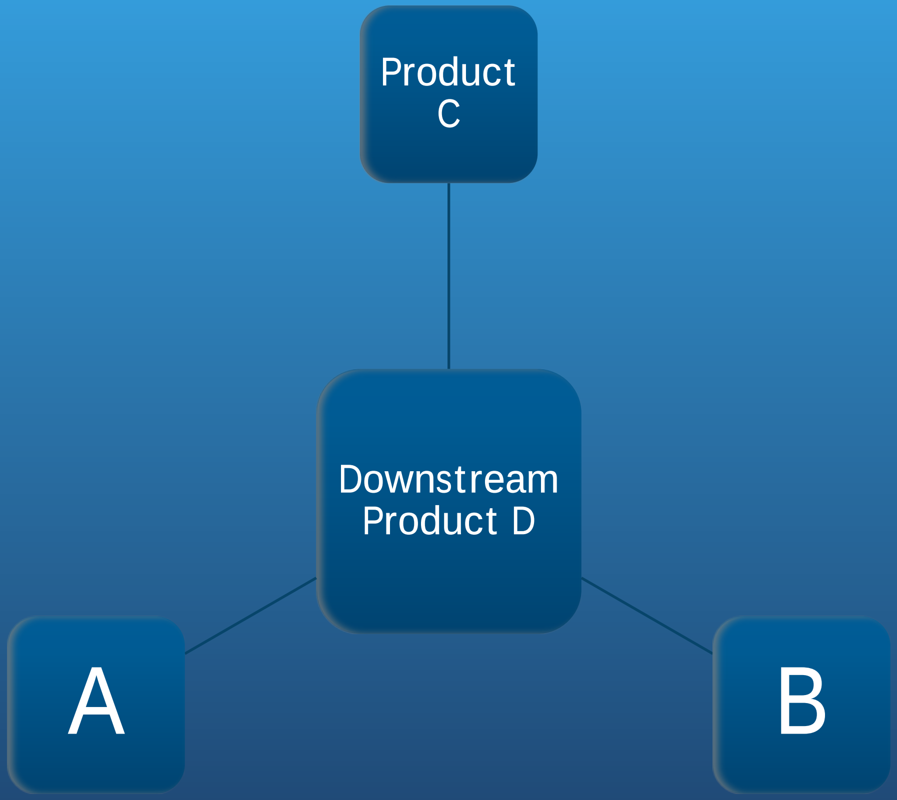
Refusal to Supply

Enterprise A is dominant in product C

Product C is used as an input to Product D in a downstream market in which enterprise B operates

A has sold C to B but now wishes to enter the downstream market and refuses to sell C to B

Refusal to Supply



Refusal to License IP Rights

Generally, the owner of an IP right, even if dominant, is not obliged to license it

But, in exceptional circumstances, compulsory licensing is justified

Refusal to License: Abuse?

Microsoft

- the refusal relates to a product or service indispensable to the exercise of a particular activity on a neighboring market
- the refusal is of such a kind as to ‘exclude’ any effective competition on that neighboring market; and
- the refusal prevents the appearance of a ‘new’ product for which there is potential consumer demand

Margin Squeeze

Enterprise A is dominant in product D

Product D is used in a downstream market in which Enterprise A and Enterprise B compete

A sells D to B at a price which means that B cannot operate profitably on the downstream market

(B is as efficient as A)

Exclusionary Abuse

Justification:

- objective necessity
- efficiencies

Exploitative Abuse: Examples

Excessive pricing

Unfair discrimination

Unfair trading conditions

Excessive Pricing

Difficulties in defining excessive pricing

Pricing has to be unfair

European Commission will only investigate if there are high barriers to entry

Unfair Discrimination

Price discrimination between competing customers in the same position which puts one at a competitive disadvantage

Discrimination based on nationality or residence

Unfair Trading Conditions

The imposition of contractual restrictions on the freedom of action of the other party which is not indispensible for the achievement of the legitimate objective of the contract

e.g. non-essential restrictions imposed by collecting societies on the right of copyright owners to exploit their copyright

India: Abuse of Dominance

DFL

Issues of:

- market definition
- assessment of dominance
- nature of the alleged abuse

Should this be a matter for competition law or consumer protection?

Discussion

Over to you!