How does the prohibition of abuse of dominance fit with the rest of competition policy?

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Introduction

The prohibition of abuse of dominance in Article 82, which is mirrored in domestic legislation such as Chapter II of the UK Competition Act, is a major piece of the competition policy jigsaw. In other jurisdictions there are similar, but not identical, pieces such as Section 2 of the Sherman Act in the United States. My question is how this piece fits, or should fit, with the other pieces that make up competition policy. As experience at the kitchen table shows, a pleasing overall picture requires a good fit, and it is very unfortunate if any pieces go missing.

What are the other pieces? Most obviously there are

- prohibitions on anti-competitive agreements (e.g. Article 81) and
- merger regulations.

The relationship between these two pieces has been much discussed and is indeed the subject of the well-known exam question: 'A horizontal merger is the ultimate agreement

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between firms, so why is competition policy much more tolerant of horizontal mergers than of horizontal price-fixing agreements?' However, the relationship between these elements and Article 82 has been less thoroughly considered.

An important piece, which has occasionally tended to go missing, concerns

- challenges to government laws, regulations and conduct that have anti-competitive effects.

EC state aids law is a prime example of such measures. Under the heading of 'competition advocacy' they are a core theme of the ICN's work.[2] And in the UK (and elsewhere) they are receiving much more emphasis than in the past in respect of challenge to existing laws and regulations that appear to be anti-competitive, and also systematic *ex ante* competition scrutiny of proposed laws and regulations.

In the UK (and to some extent elsewhere) there are also

- market investigations.[3]

These are investigations undertaken by the Competition Commission, following reference usually from the OFT, into markets whose features are suspected of preventing, restricting or distorting competition. Relevant market features include structural factors and the conduct both of suppliers and customers. The OFT carries out market studies that may lead to references to the Competition Commission and also, more generally, in the exercise of its own powers to keep markets under review, to issue reports and to make recommendations.

Finally, two elements of public policy closely related to competition policy are

- monopoly regulation, notably of pricing, and
- consumer policy.

There is no time here to discuss the last of these, but let me comment in passing that the relationship between competition and consumer policy calls for much more analysis and debate internationally than it has received. There are now welcome moves to redress this neglect.[4]

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[2] See www.internationalcompetitionnetwork.org.
[3] To use the term in the Enterprise Act 2002, the relevant parts of which come into force on 20 June 2003. That Act's provisions for market investigation references replace the provisions of the Fair Trading Act 1973 for so-called 'monopoly' references. In this paper I will use the more descriptive term 'market investigations' in respect of the old, as well as the new, regime.
[4] See the speech by FTC Chairman Tim Muris on 'The interface of competition and consumer protection' given at the 2002 Fordham conference.

The rest of my remarks come under four headings concerning the relationship of the prohibition of abuse of dominance to merger regulation, government activities, market investigations, and price regulation respectively.

Abuse of dominance and merger regulation

Two recent EC developments have highlighted the relationship between abuse of dominance and merger regulation. The first is the ongoing review of the EC merger regulation itself. As things stand both the ECMR and Article 82 are based on the same word – so one would have supposed the same underlying concept – namely 'dominance'.

I am with those who believe that the ECMR test should instead be based on the concept of 'substantial lessening of competition'. This is primarily because there might well be an undesirable and uncertain gap – relating to non-coordinated effects in oligopoly – between 'dominance' wording and the generally accepted SLC policy intention. The obvious concern, if there is a gap, is that some substantially competition-lessening mergers would sail through it. The possible gap has been much discussed over the past year since the *Airtours* judgment, and I will not delve into it here. Following the Commission's proposed amendment to Article 2 of the ECMR, which I shall mention later, the policy debate is now mainly about how best to close it.

Instead I want to argue the separate but reinforcing point that there *should be* a gap between the thresholds for public policy interventions relating to abuse of dominance and to mergers, and hence between the meanings of 'dominance' and 'SLC'.[5]

If they did generally mean the same, then there could be awkward consequences for EC competition law and policy as a whole. Article 82 policy could be too interventionist. Any firm or firms that had market power to a degree the prospect of which would invoke SLC-based merger policy would be 'dominant', and if they engaged in conduct that counts as abusive, then liable to serious penalties and possibly private actions for damages.

Competition policy would then fail to recognise the fundamental difference between the accumulation of market power by successful product market competition and, on the other hand, the acquisition of market power by merger. It is one thing to win customers over time by serving them well in the product market, quite another to acquire them at a stroke in the

[5] I discussed this in my remarks on 'How to reform the EC merger test?' at the EC/IBA conference in Brussels in November 2002. The passage that follows is largely taken from that talk, which is at www.oft.gov.uk. For the avoidance of doubt I should make clear that in favouring SLC I am not advocating more interventionist merger policy than in the past, nor do I believe that that would be the result.

stock market. Policy would also fail to distinguish between *ex ante* measures to maintain competitive incentive structures and *ex post* intervention to curb and penalise abuse of dominant market power.

From the point of view of the economic incentives of firms, and on general grounds, that would seem wrong. The threshold of market power that triggers intervention to maintain competitive incentives by preventing anti-competitive structural changes in markets ought to be lower than that which triggers liability for the breach of competition law prohibitions on firms that have become dominant through successful competition in the marketplace.

Put differently, merger regulation would seem logically to be a closer relative of Article 81 than Article 82. A merger is the ultimate agreement between firms: the focus of merger regulation is therefore about whether such agreements restrict competition substantially, as distinct from questions about abuse of market power. This does not mean that, say, horizontal mergers should be treated as strictly as horizontal price-fixing, since the latter, but not the former, is almost always anti-competitive and without redeeming features. But even leaving aside hard-core anti-competitive agreements like horizontal price-fixing, it would be bizarre to recast Article 81 to apply only to agreements that created or strengthened a dominant position. Policy towards anti-competitive agreements would then be far too lax. This is not to say that merger control should be aligned with Article 81. It is however to doubt that merger control should be based on the same key concept as Article 82.

The European Commission's proposal to meet this concern is to retain 'dominance' wording while saying that its meaning can vary with context. Then the concepts of 'dominance for the purposes of article 82' and 'dominance for the purposes of the ECMR' could bifurcate. Humpty Dumpty, unlike Alice, may have been content for a word to mean different things, but whether it is the wisest or clearest policy approach is another matter. Far better, I believe, to base merger policy directly on SLC.

The second recent development is the Commission's appeal of the CFI's judgment in the *Tetra Laval/Sidel* case.[6] Among other matters at issue is the CFI's requirement that, in such cases, the Commission should consider in its merger analysis:

- the extent to which resulting incentives for anti-competitive behaviour might be reduced, or even eliminated, by the possible illegality of such conduct under law prohibiting abuse of dominance, and the likelihood and consequences of the detection of illegal conduct of that kind; and
- how commitments by the parties as to future conduct might solve such competition problems.

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[6] See paragraphs 154 to 162 of the CFI's judgment of 25 October 2002 in Case T-5/02 *Tetra Laval BV v. Commission*, the notice of the Commission's appeal to the ECJ published in OJEC [2003] C70/3 and the Commission's press release IP/02/1952 of 20 December 2002.

The Commission objects to these requirements on grounds of practicability and inconsistency with the objective of merger regulation to prevent structural changes that may lead to anti-competitive effects that abuse of dominance law is not sufficient to deter. Merger regulation is moreover intended to avoid the need for complex ongoing monitoring of firms' behaviour.

It is not for me to comment on a case before the ECJ, and of course the CFI judgment was given in the context of the facts of the case at hand. But I hope that some general remarks from a UK perspective, where unlike the ECMR the test is SLC, will not be out of order.[7]

To repeat earlier remarks, merger regulation is *ex ante* intervention to maintain competitive incentives by preventing anti-competitive structural changes in markets. That is very different from *ex post* intervention to curb and penalise abuse of dominant market power, and the threshold for the latter kind of intervention should be considerably higher than for the former.

There are all sorts of ways – many perhaps unpredictable – that mergers can substantially lessen competition without dominance being abused or even existing. Moreover, the deterrence, detection, demonstration and remedy of abuse of dominance are necessarily imperfect and/or costly. Generally, then, the control of market structure to preserve competitive *incentives* is far more effective, efficient and certain than attempts to curb or control corporate conduct. So the prohibition of abuse of dominance is almost always of little or no practical relevance to merger policy, and SLC mergers usually call for structural solutions.

But not always. In the rare case where the only ways that a merger might lessen competition would be effectively, efficiently and certainly prevented by abuse of dominance law, then it would be right to take that law into account. Indeed, in such a case and with perfect deterrence there would not be an SLC. Similarly, if behavioural commitments can effectively, efficiently and certainly prevent risks to competition, they might be the right remedy.

In considering merger references at the OFT[8] we pause to consider whether commitments (known as 'undertakings') might avoid the need to refer mergers that raise competition concerns, but this pause is often sensibly very brief. Undertakings in lieu of reference are generally appropriate only where the competition concerns raised by a merger are clear-cut

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[7] The UK merger test has effectively been SLC for some years. That will also be the test in law from 20 June 2003 when the merger provisions of the Enterprise Act come into force. The OFT's guidance on how it will make merger references under the Act was published on 21 May 2003 and is available at www.oft.gov.uk.

[8] The OFT carries out 'stage 1' scrutiny of mergers and the Competition Commission carries out the detailed 'stage 2' examination of the mergers referred to it.

and where the remedies proposed to address them are both clear-cut and proportionate. Moreover, for the reasons above, structural remedies are usually better targeted than behavioural ones. We did however give lengthy consideration to behavioural undertakings in a recent case involving gas storage – *Centrica/Dynegy* – but acceptable undertakings could not be found so the merger was in the end referred to the CC.

Abuse of dominance and government activities

The relationship between competition policy and government activities is perhaps one of the most interesting and potentially fruitful current issues. It has grown in importance as government bodies have increasingly operated in market environments, and as the will and the means of competition scrutiny of aspects of government activities have strengthened – both generally positive developments.

The applicability of the prohibition on abuse to government bodies has been the subject of two recent judgments –

- by the UK Competition Appeal Tribunal in *Bettercare* (a case about purchasing by a health care trust in Northern Ireland), and
- by the CFI in *FENIN* (a case about purchasing by the health service in Spain).[9]

Subject to any exclusions, the competition rules apply to all undertakings irrespective of their legal or ownership status. An entity is an undertaking if it is engaged in an economic activity. In both *Bettercare* and *FENIN* the question was whether *purchasing* by the respective government bodies was an economic activity. The answers, on the facts of each case, were respectively Yes and No.

The UK Competition Act must be applied consistently with European Court jurisprudence. So the CAT's judgment in *Bettercare* must be read in the light of the CFI's judgment in *FENIN*, which came subsequently. This is not altogether straightforward.

From *FENIN* it seems clear that buying on a commercial market, even by an economically powerful buyer, is not necessarily an economic activity. If the purchasing is not to supply goods and services as part of an economic activity – but e.g. for use in meeting a social purpose – then the purchasing might not be an economic activity. In *Bettercare* the health care trust naturally had social purposes but it charged some fees to some patients and it

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[9] *Bettercare Group Limited v. Director General of Fair Trading* [2002] CAT 7. Before 1 April 2003 the CAT was the Competition Commission Appeal Tribunal (CCAT) and OFT decisions were in the name of the Director General of Fair Trading – a creature of statute now extinct. Case T-319/99 *FENIN v. Commission*, judgment of 4 March 2003. See also 'The public sector and the meaning of an

supplied some care services in-house. Whether and how far those or other features differentiate *Bettercare* from *FENIN* is an interesting question of law with potentially considerable practical implications in a context of widespread contracting out by public bodies.

Questions about the substantive application – as distinct from the applicability – to public bodies of the prohibition on abuse of dominance have also been before the OFT recently. For example, the OFT has investigated allegations – but found no evidence – that Companies House, the body which has a statutory duty to maintain a register of company information, engaged in predatory pricing and price squeezing on the commercial side of its operation.

In addition to carrying out our responsibilities under competition law, the OFT, like a number of other competition bodies internationally, is focusing much more than before on possible anti-competitive consequences of government laws and regulations.

Our 2001 report on competition in professions raised a number of questions for government, as well as for the professions themselves, which are being pursued. Our report this year on the system of pharmacy regulation recommended the lifting of entry controls, which block new ways of getting medicines to the public. In relation to England the government has said that it 'favours change to open up the market and improve quality and access, without diminishing the crucial role that pharmacies play'.[10] Our recent report on private dentistry included deregulatory recommendations to government, again to allow new freedoms and opportunities to providers. We have advised the government against conferring upon the Tote, which is being transferred to the private sector, an exclusive right over pool betting. And competition scrutiny is now part of the assessment of new laws and regulations.

Pro-competitive deregulatory analysis of this sort, the results of which are ultimately for government to decide, is largely complementary to enforcement of competition rules such as the prohibition on abuse of dominance. But there is the wider point that undue regulation can naturally bolster the market power of incumbents as well as inhibit the freedom and opportunity of new businesses. More deregulation can mean fewer competition problems.

Abuse of dominance and market investigations

I mentioned earlier that UK competition law provides for market investigation references to the CC in respect of markets whose features are suspected of preventing, restricting or distorting competition. Recent examples of such investigations include new cars,

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undertaking after FENIN and Bettercare', George Peretz, IBC Advanced EC competition law conference paper, April 2003.

[10] DTI press release of 26 March 2003. In Scotland, Wales and Northern Ireland liberalisation has been rejected.

supermarkets, and the supply of banking services to SMEs – all more or less oligopolistic markets.

This provision allows for examination of whether the process of competition is working effectively in markets as a whole and, where remediable competition problems are found, pro-competitive measures can be taken. Those could include, for example, steps to reduce consumer switching costs or recommendations to government on the removal of barriers to competition. In market investigations there is no implication that any firm has broken competition law, and no question of fines or damages.[11]

Market investigation references can therefore address wider competition concerns than the prohibitions of abuse of dominance and anti-competitive agreements, which will be used in preference to market investigation references where applicable. Broadly speaking, the relationship between market investigation references and the prohibition of abuse of dominance is one of complements, not substitutes.

Thus it is likely, as in the past, that market investigations references will concern market-wide features or multi-firm conduct – e.g. in oligopoly. This is not to say that the prohibition of abuse of dominance is inapplicable to multi-firm issues. But case law on what might constitute abuse of *collective* dominance is still developing. Indeed, as current debates about merger policy show, the scope of collective dominance is itself uncertain – in particular whether collective dominance is possible without tacit co-ordination.

It is not the OFT's present intention to make market investigation references based on the conduct of a single firm, whether dominant or not, where there are no other features of a market that adversely affect competition. To return to an earlier theme, anti-competitive government regulations or policies are possible examples of such features.

Abuse of dominance and price regulation

Needless to say, various kinds of pricing behaviour by dominant firms can in some circumstances constitute abuse. Here I want to focus on the issue of excessive pricing. In particular sectors – notably the utilities – there is *ex ante* regulation to cap prices. But what is the role of the prohibition on abuse of dominance in relation to 'high' pricing? Can single-firm exploitative pricing be *sufficient* for a finding of abuse of dominance?[12]

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[11] In relation to an investigation's substantive findings. The Enterprise Act provides for fines to be imposed in case of failure to comply with an investigation.
[12] In some ways this question is a partial counterpart to that posed by Eleanor Fox in her recent paper 'What is harm to competition? Exclusionary practices and anticompetitive effect' in the *Antitrust Law Journal* 2002. She asks whether it is *necessary* for a practice to be exploitative for it to be anti-competitive.

Unlike the position in the US under section 2 of the Sherman Act, the answer under European competition law appears is that it can be. The CAT's upholding of the OFT decision against the pharmaceutical company Napp is a leading case in point.[13]

Napp abused a position of dominance approaching monopoly in the UK market for the supply of sustained release morphine tablets and capsules by charging

- excessively low – predatory or exclusionary – prices in the hospital segment of the market, and
- excessively high prices in the community segment of the market.

As to the latter, the evidence from various comparisons of prices and costs demonstrated (a) that Napp's prices in the community segment were significantly higher than would be expected in a competitive market and (b) that there was no effective competitive pressure to bring them down to competitive levels. Thus the ECJ's test of abuse, as expressed in *United Brands*, was met.

The high pricing in the community segment was in conditions created in part by the exclusionary pricing in the hospital segment – the key potential route for competitive entry into the market. Indeed, the OFT explicitly viewed Napp's pricing policy as a whole and in the appeal case went on to say that it would not wish to maintain the excessive pricing abuse if the pricing to the hospital segment was not judged to be exclusionary. Absent abusive exclusion, the facts and appropriate analysis would have been materially different. But as the CAT made clear (at para 434), 'nothing in *United Brands* suggests that the existence of exclusionary conduct is a prerequisite for a finding that prices are excessive contrary to the [abuse of dominance] prohibition'. The CAT said, moreover, that it would have been 'erroneous in law' to take the view that the excessive pricing was abusive *only* because of the exclusionary conduct.

None of this implies that the prohibition on abuse of dominance is potentially a price capper's charter, and excessive pricing cases under Article 82 have in fact been rare. Moreover, some dominant firms are subject to *ex ante* regulatory price caps anyway, notably state monopolists – or inheritors thereof – in the utility industries. In assessing the appropriateness of such price regulation, again it seems relevant *how* a dominant position arose.

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[13] *Napp Pharmaceutical Holdings Limited and Subsidiaries v Director General of Fair Trading,* [2002] CAT 1. While upholding the OFT's substantive decision, the CAT lowered the fine that the OFT had imposed on Napp.

Conclusion

This last point illustrates a general theme of this discussion. Appropriate public policy towards firms with actual or potential market power depends on the cause of the market power, not least for reasons of economic incentives. It is one thing to gain market power by innovating or otherwise winning customers over time by serving them well in the product market. It is quite another thing to get market power by merger or cartel agreement; or to strengthen market power by exclusionary practices; or to hold or inherit a state monopoly. That is an old point, but its implications for the relationship of the prohibition of abuse of dominance to the other elements of competition policy perhaps warrant more thought.