

Pricing abuses

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- Pricing is a key element of competitive strategy
- In general, companies are and should be free to price how they want. However, some practices can fall afoul of competition law.
- Two broad areas:
 - Collusive agreements – no ‘safe harbours’, so any firm could be in breach
 - Abuse of dominance (“monopoly situation” in Mauritius) – only above market share thresholds

Do we prohibit conduct or outcomes?

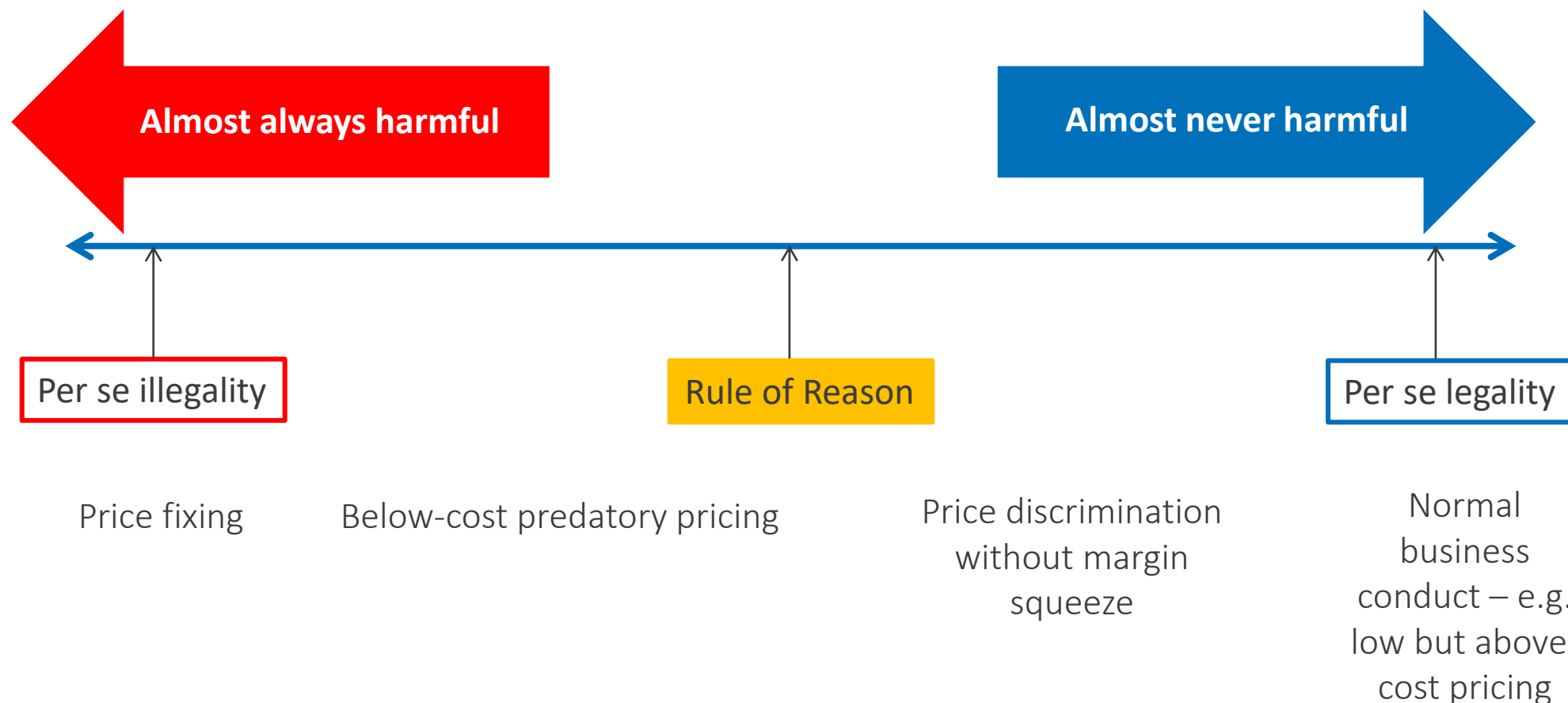


- Much of the law relating to monopoly situations relates to effects:
 - “has the object or effect of preventing, restricting or distorting competition”
 - “actions or behaviour that have or are likely to have an adverse effect on the efficiency, adaptability and competitiveness of the economy of Mauritius, or are likely to be detrimental to the interests of consumers.”

- So what behaviour is actually prohibited?

LEGAL STANDARDS – RULES OR ASSESSMENT OF EFFECT?

Partly a matter of history – but some logic too, depending on whether there is a high cost of wrongful inaction (because the conduct is almost always harmful) or a high cost of wrongful action (because the conduct is almost never harmful).



Collusive agreements



- Price fixing
- Resale price maintenance

AGREEMENTS TO FIX PRICES ARE PROHIBITED

A horizontal 'agreement' (with one or more competitors) on prices is simply prohibited.

- Note that 'agreement' in this sense does not require a formal agreement
- Businesses whose employees fix prices would also be liable
- If in any doubt – consult a lawyer! And consider applying for leniency.

Vertical agreements by which a supplier prevents a retailer or other business customer from reducing prices also prohibited

- Recommended prices are permitted
- Very clear prohibition. No market share threshold, dominance test: all businesses must comply. No assessment of effects etc.

In Mauritius, offenders face a fine of up to 10% of turnover for the entire period of the breach, to a maximum of five years

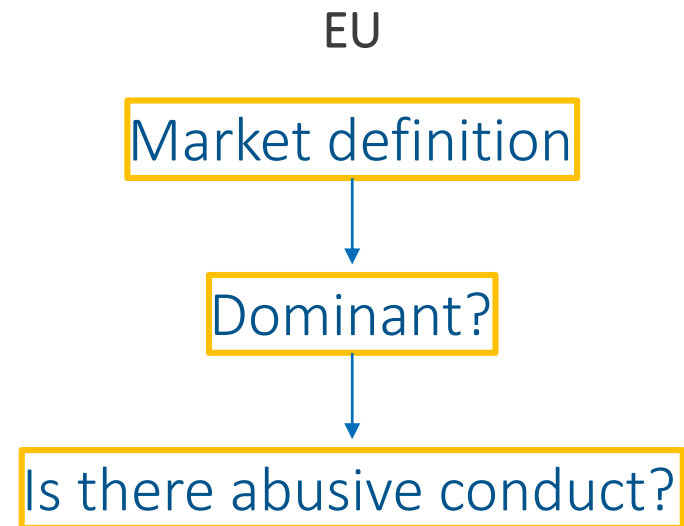
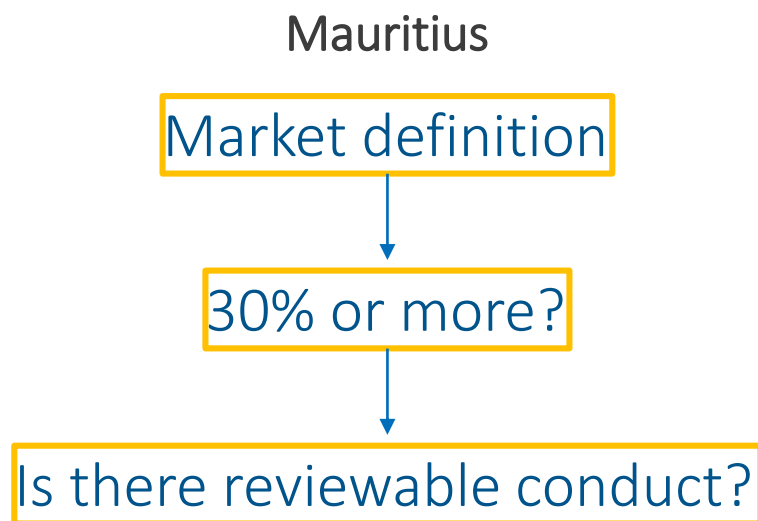
Monopoly situations (1): definition of monopoly/dominance



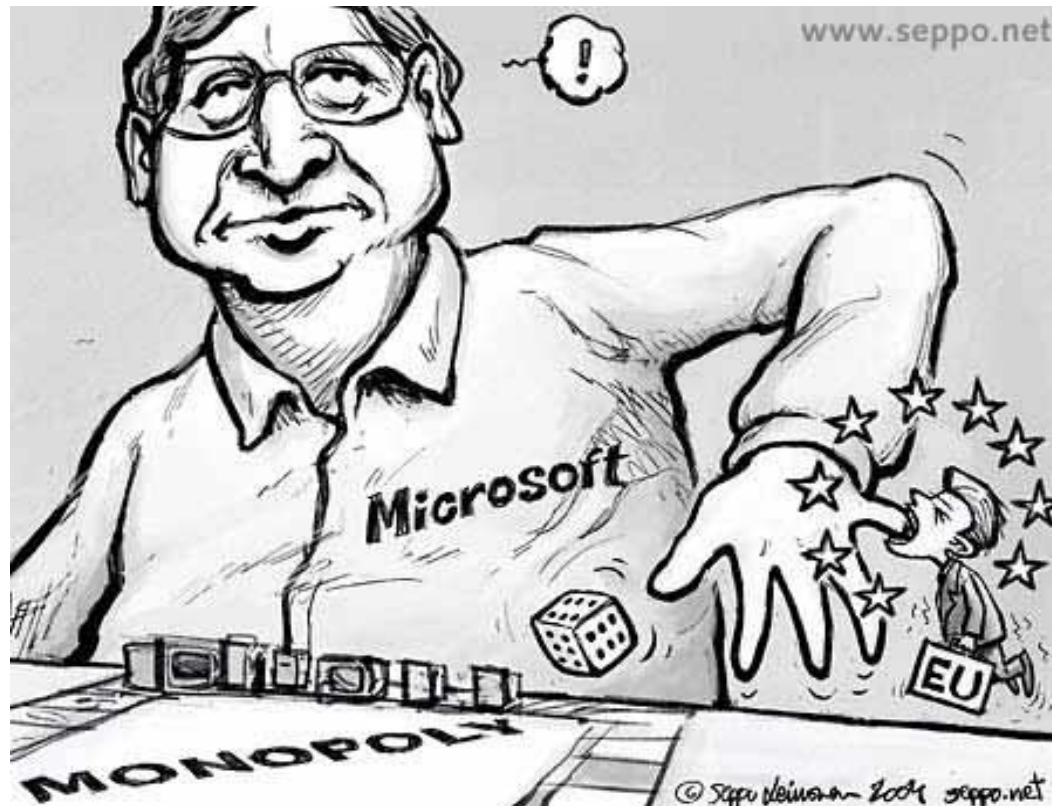
EXISTENCE OF A MONOPOLY SITUATION

Where:

- a) 30 per cent or more of those goods or services are supplied, or acquired on the market, by one enterprise; or
- b) 70 per cent or more of those goods or services are supplied, or acquired on the market, by 3 or fewer enterprises.

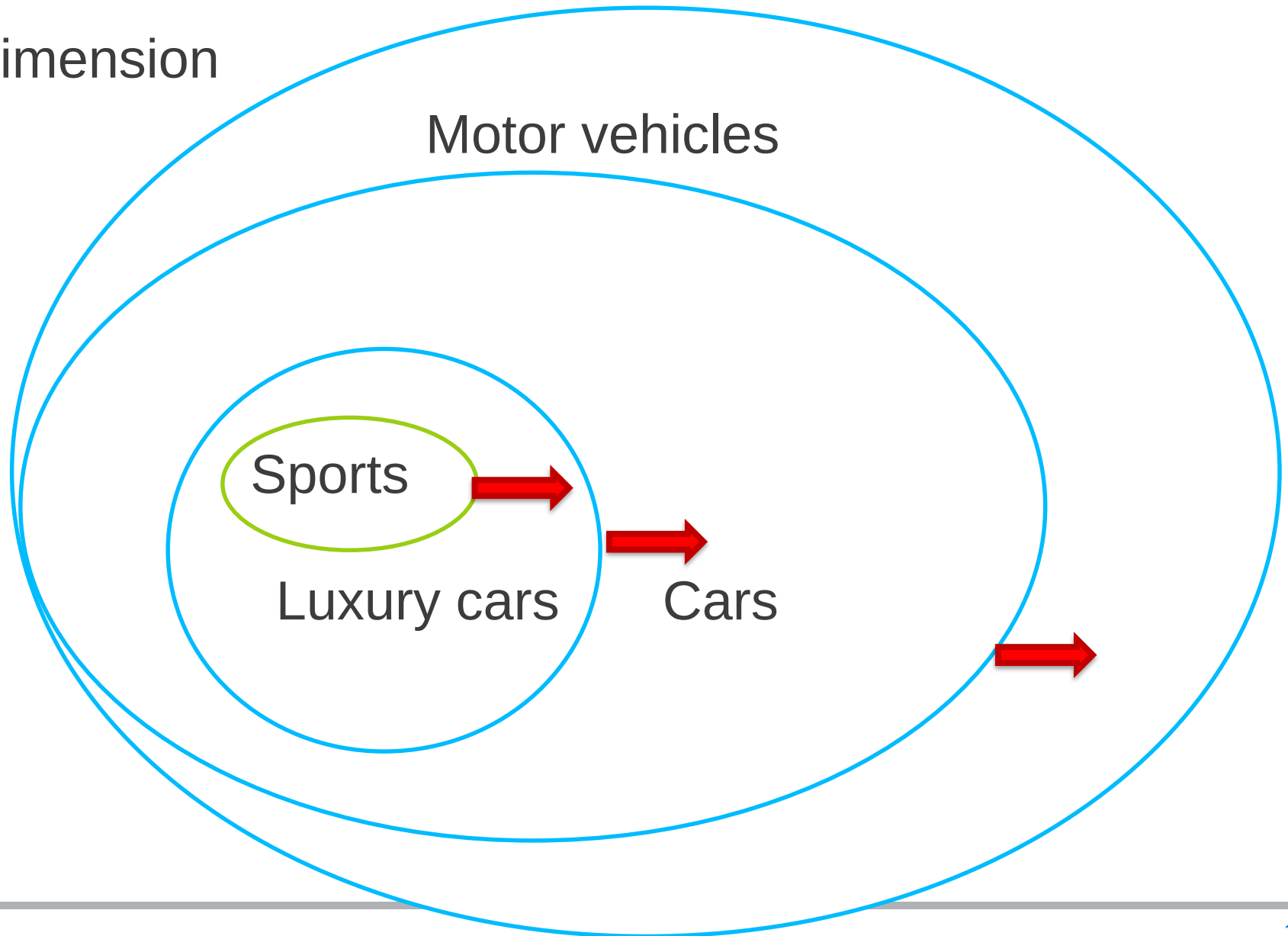


What do we mean by a “monopolist”?



100% market share? **No.**

Product dimension



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Mauritius

Market definition



30% or more?



Is there reviewable conduct?

EU

Market definition



Dominant?



Is there abusive conduct?

On the face of it, Mauritian law looks more mechanical: 30% rule, instead of dominance

However, in Mauritius the concept of dominance comes in in the review criteria

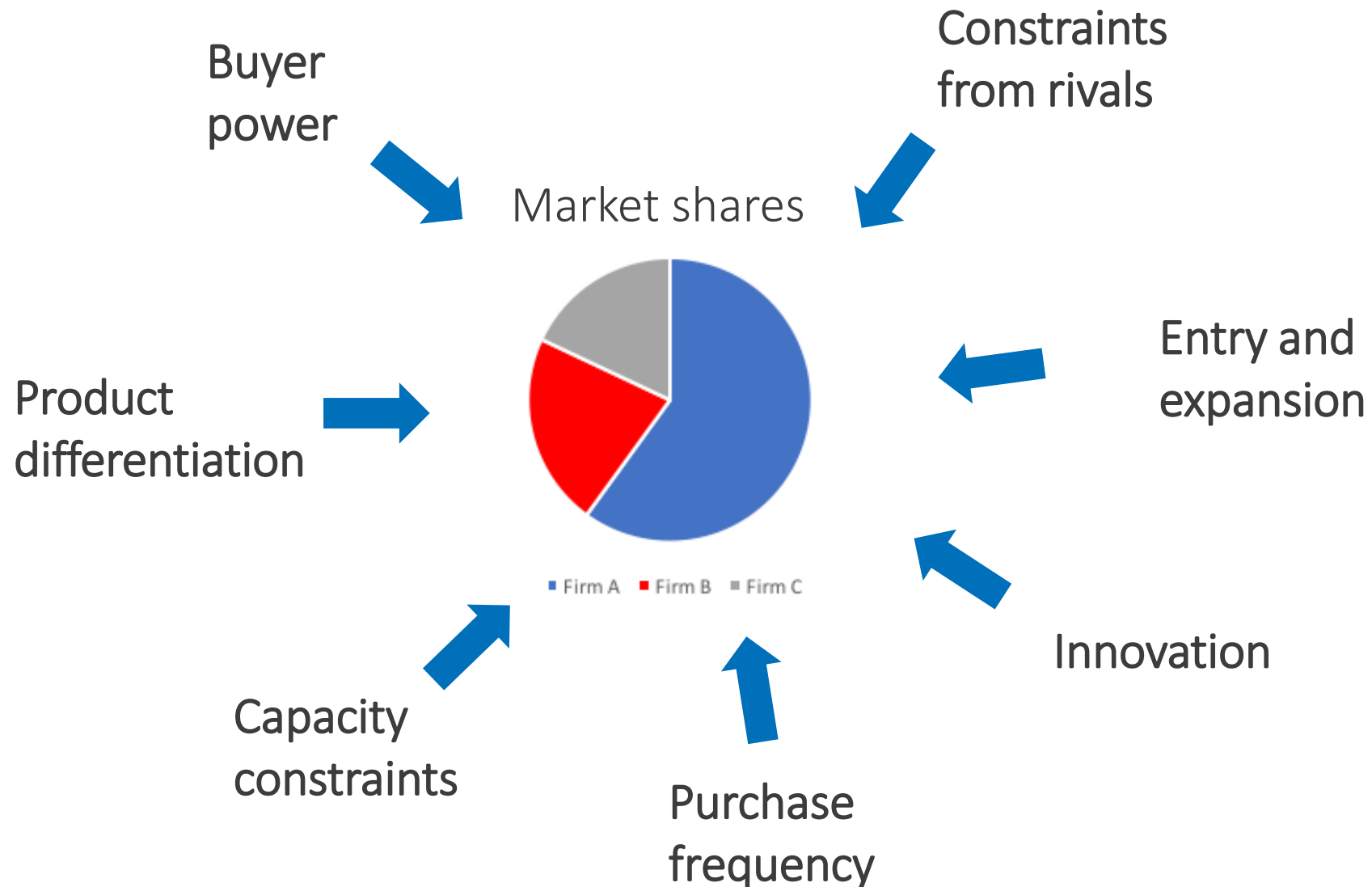
DOES MAURITIUS HAVE A 'DOMINANCE' SCREEN?

- In the EU, companies can only be investigated for 'abuse of dominance' if they are 'dominant', defined as *"a 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, its customers and ultimately of the consumers."*
- In Mauritius, 46(3) requires

"In reviewing a monopoly situation, the Commission shall take into account -

 - (a) the extent to which an enterprise enjoys or a group of enterprises enjoy, such **a position of dominance** in the market as to make it possible for that enterprise or those enterprises to operate in that market, and to adjust prices or output, **without effective constraint from competitors** or potential competitors;
 - (b) the availability or non-availability of **substitutable goods or services to consumers** in the short term;
 - (c) the availability or non-availability of nearby **competitors to whom consumers could turn** in the short term; **and** "

ECONOMIC ASSESSMENT OF DOMINANCE



Monopoly situations (2): conduct



- Predatory pricing
- Rebates
- Price discrimination and margin squeeze

Dominance or monopoly is **not** prohibited, only “abuse of dominance” which comes in two forms (in EU):

- **Exclusionary** – several different forms of conduct

- Predatory pricing
- Rebates
- Margin squeeze

Important to understand legal precedents for each but economists focus on the similarities by considering **effects** – whether any of them leads to **foreclosure**

- **Exploitative**

- “Excessive prices” – rare (except recently in pharma!), not at all in US
- Price discrimination

- What conduct *does* ‘restrict, prevent or distort competition’?
- Difficulty: if a dominant firm drives out a competitor is that **anti-competitive**...or is it **competition**?
- The economic approach seeks to assess likelihood of **foreclosure**:

“a situation where effective access of actual or potential competitors is hampered or eliminated as a result of the conduct of the dominant undertaking, whereby the dominant undertaking is likely to be in a position to profitably increase prices to the detriment of consumers.”

EC Guidance on ‘Enforcement priorities’

PREDATORY PRICING CAN PRICES BE ‘TOO LOW’?

- Competition Authorities need to be careful in assessing ‘predatory’ pricing. We want firms to price low, to undercut each other, to seek to win customers from another through vigorous, fierce competition. Companies will always complain about their competitors’ prices!
- Evil plan: (1) cut prices, (2) drive out competitors, (3) profit!
- EU case law establishes several hurdles to proving this:
 - Dominance (market power)
 - Harming **equally efficient rival**: “If the data clearly suggest that an equally efficient competitor can compete effectively with the pricing conduct of the dominant undertaking, the Commission will, in principle, infer that the dominant undertaking's pricing conduct is not likely to have an adverse impact on effective competition, and thus on consumers, and will therefore be unlikely to intervene.” *Guidance*
 - ‘No economic sense’ without exclusionary effect – not required in EU jurisprudence (is in US) but likely to be relevant
- ‘Rule of thumb’ cost benchmarks provide safe harbours.

Case law

Prices below **average variable costs** (that is to say, those which vary depending on the quantities produced) by means of which a dominant undertaking seeks to eliminate a competitor must be regarded as abusive. - *ECJ, AKZO, 1991*

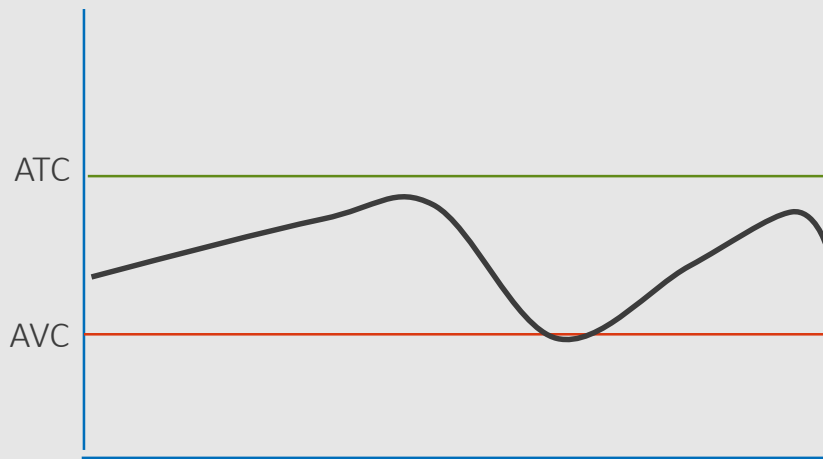
Prices below **average total costs**, that is to say, fixed costs plus variable costs, but above average variable costs, **must be regarded as abusive if they are determined as part of a plan** for eliminating a competitor – *ECJ, AKZO, 1991*

*Company sells 10,000 units, has variable cost of €2 and fixed cost of €5,000.
Average variable cost = €2, Average total cost = €2.50.*

NB: can be some complications in assigning fixed costs to different products – but EU case law says this must be resolved in the company's favour.

PREDATORY PRICING: SAFEGUARDS (ECONOMICS)

AEC test



Recoupment test:

- How did/will the firm recoup its losses?

No economic sense test:

- Is there a commercial rationale for below cost pricing?
- Absent the entrant / competitor, would the firm have priced in this manner?

Evidence of intent?

Internal documents are key

- Another way to cut prices: targeted price cutting
- Many legitimate pro-competitive reasons
- All forms of rebate OK for non-dominant firm
- BUT – dominant firms have a special responsibility to ensure that rebates do not prevent, restrict or distort competition
- The form of the rebate matters:
 - Tied to exclusion of rival?
 - Tied to market share target?
 - Tied to volume target?
 - Retrospective on ALL units sold or only partial?

REBATES WITH DIRECT EXCLUSIONARY EFFECT

- Rebates tied to direct exclusion of competitor or customer share target – see CCM Case 001 IBL Kraft Cheese



- Retrospective rebates tied to volumes could have anticompetitive effect: do they foreclose rivals from the market? E.g.
 - Customer buys 50,000 units per year at Rs 1, = Rs 50,000
 - Supplier offers rebate of 10% on ALL units if buys 60,000
 - What is the price of the 'extra' 10,000? Customer pays Rs 60,000 – 10% - Rs 54,000. So price = Rs 0.4. Hard for rivals for compete against that.
- Hard or effectively impossible? Key questions:
 - Is the remaining demand from that customer enough to sustain rival?
 - Is the remaining demand from other customers enough to sustain rival?
 - Can other suppliers offer equivalent discounts?
- No simple rules of thumb: but dangerous if rebates are **retrospective**, have **volume targets > current sales** and if **affected market share is high**.

- Different prices to different customers for the same thing
- What is ‘the same thing’? Lots of perfectly legitimate reasons for customers to get different prices:
 - Different timing or terms of supply
 - Different costs
 - Clearing stock
 - Efficient pricing to cover fixed costs
 - Volume discounts/rebates + loyalty – maybe a problem, as discussed
- Most competition authorities would only be concerned if there is effect on competition (exception: price differences between member states of European Union).
- Usually, this concerns supply of an input to a rival

PRICE DISCRIMINATION AGAINST DOWNSTREAM RIVALS

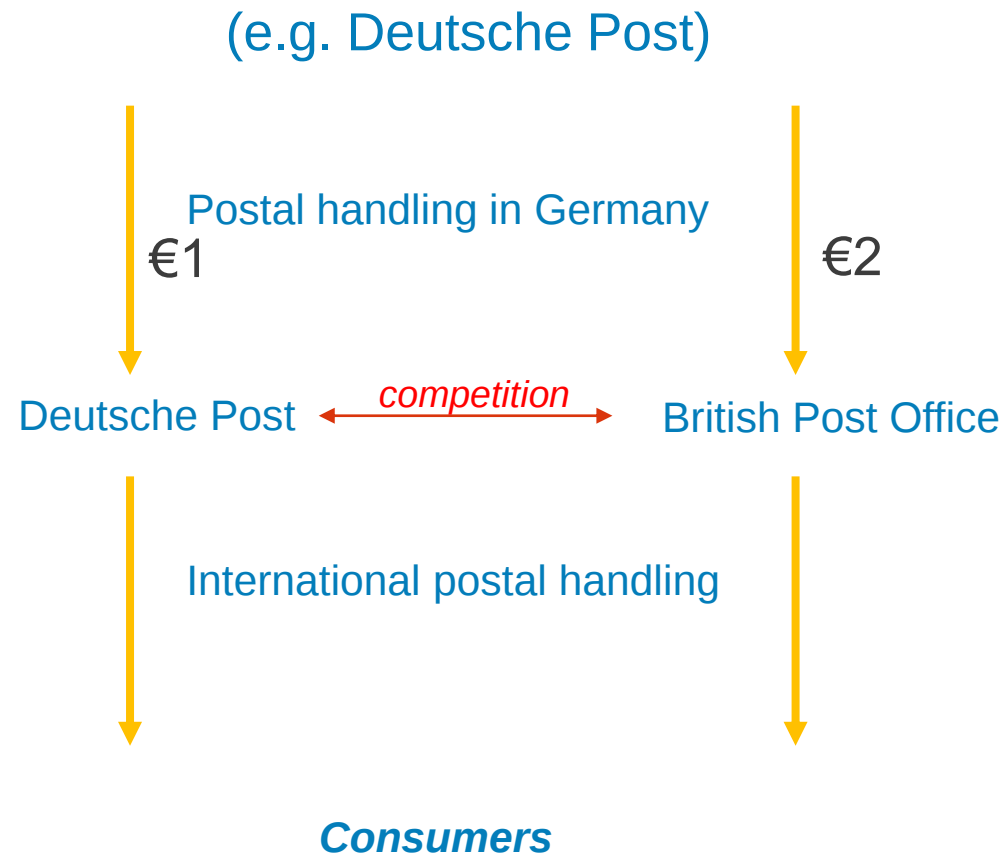
- A vertically integrated dominant firm needs to be careful if charging downstream rivals a higher price for an input than it charges 'itself':

Dominant upstream supplier...

...charges for an input over which it has market power...

...to downstream suppliers...

...who compete for consumers



MARGIN SQUEEZE AGAINST DOWNSTREAM RIVALS

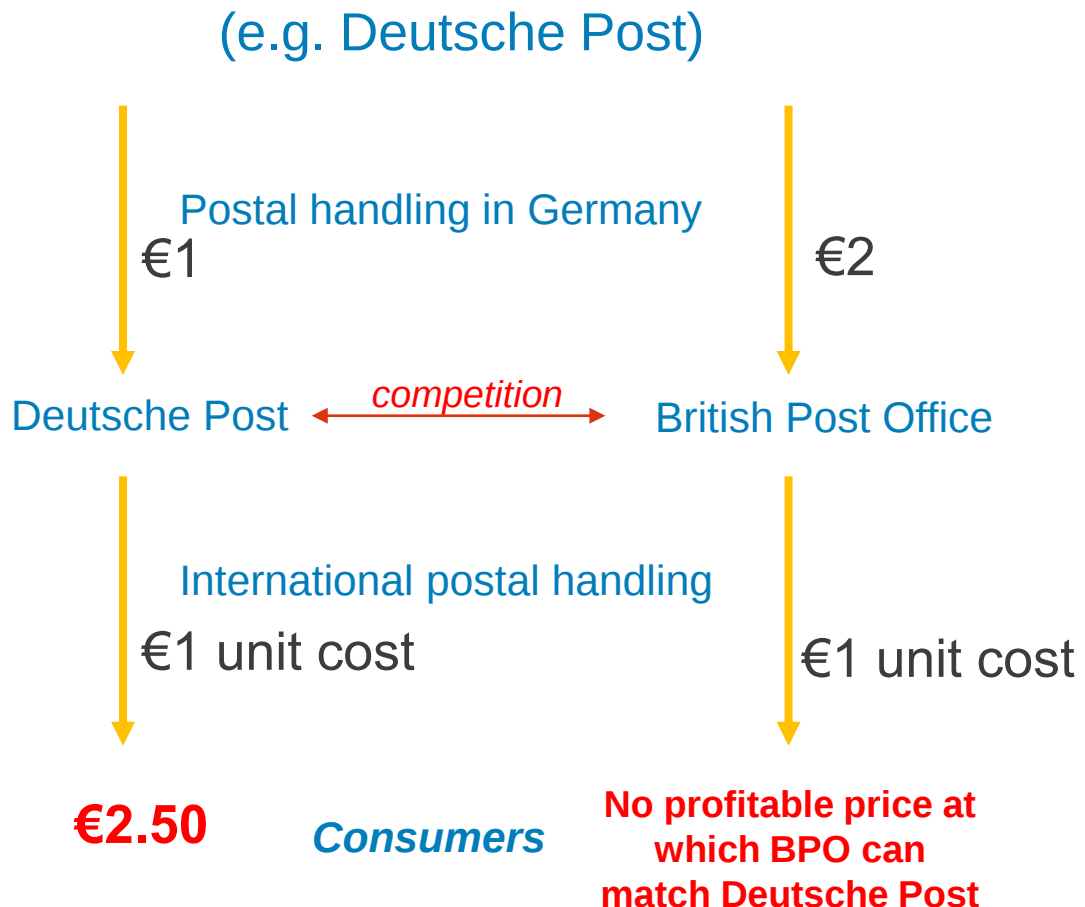
- If the dominant vertically integrated firm also sets a downstream price that the rival cannot match at the inflated upstream price, that is a margin squeeze

Dominant upstream supplier...

...charges for an input over which it has market power...

...to downstream suppliers...

...who compete for consumers



Summary



SUMMARY: DOES MY PRICING BREACH COMPETITION LAW (1) ?



- Have I come to an understanding with a competitor fixing prices or sharing markets?
 - If 'yes' >> collusive price fixing, very illegal!
- Have I agreed with a downstream reseller the price at which my product can be sold?
 - If you have set a floor price, yes >> resale price maintenance, also illegal

SUMMARY: DOES MY PRICING BREACH COMPETITION LAW (2) ?



- What about prices too low and rebates? Not necessarily a breach. Mostly OK.
 - Monopoly situation: do you meet the 30% test, do the top 3 meet the 70% test, are you dominant? If 'no' then you can price how you like.
 - If you are in a monopoly situation, that is not necessarily a problem but:
 - Prices below your average variable costs, or prices below average total cost with evidence of intent to exclude could be a breach of the law
 - Certain types of rebates could be a breach of the law: if they foreclose rivals, making it impossible for them to compete
- What about price discrimination and margin squeeze?
 - Again, first assess monopoly situation and dominance
 - Then probably only a concern for vertically integrated business supplying downstream businesses – especially if your business competes downstream
 - Are you setting prices for an input that your rival needs to compete against you? If so, be careful that any price differential the rival pays is justified.

Thank you

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