Ineffective Pricing Abuses

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One of the most commonly levelled complaints about the prohibition of abuses of dominant positions provided for in Article 102 TFEU is that it lacks a unifying theory that is capable of explaining why some conduct is "abusive" and other conduct is not. While a unifying theory may continue to prove too ambitious for a body of law that covers everything from overcharging consumers to making misleading statements to regulators, recent cases offer a glimmer of hope that a unifying theory might be found for at least a subset of conduct that is covered by Article 102 TFEU: pricing abuses.

As any EU competition law textbook will tell you, pricing abuses come in many different breeds, each of which has its own jurisprudential pedigree. We have predatory pricing (Case 62/86 *Akzo*), selective discounting (Cases C-395/96 and 396/96 P *Compagnie maritime belge*), various types of rebate schemes (e.g. conditional – Case 85/76 *Hoffman-La Roche* – and retroactive – Case 322/81 *Michelin I*), and more recently we have margin squeezes (Case C-280/08 P *Deutsche Telekom*, Case C-52/09 *TeliaSonera*).

The case law has spawned an equally wide array of tests to distinguish abusive pricing from lawful "*competition on the merits.*" We have *per se* illegality for conditional rebates, *per se* legality for above-cost non-selective discounting and a cocktail of price/cost tests and qualitative "plus factors" for the rest. Slowly, however, an overarching principle seems to be emerging whereby the dividing line between lawful and unlawful conduct is determined by the capability (or lack thereof) of the conduct to foreclose equally efficient competitors.

It is difficult to pinpoint the start of this trend. The Commission's *Guidance on its enforcement priorities in applying [Article 102 TFEU] to abusive exclusionary conduct by dominant undertakings* was certainly redolent with the concept of foreclosure. But that document only set out the Commission's enforcement priorities. It did not (and could not have) change the law.

A better candidate might be the ECJ's recent judgment in Case C-209/10 *Post Danmark*. That case concerned a reference for a preliminary ruling from a Danish court. The Danish competition council argued that Post Danmark had abused its dominant position by offering selective discounts to three former customers of its competitor. The Danish court asked the ECJ what test to apply. The ECJ answered that "*it is necessary to consider whether that pricing policy … produces actual or likely exclusionary effect, to the detriment of competition and, thereby, of consumers' interests.*" The ECJ stressed (at para 21) that it is no part of the purpose of Article 102 "*to ensure that competitors less efficient than the undertaking with the dominant position should remain on the market.*"

On closer inspection of the ECJ's judgment in *Post Danmark*, however, it is apparent that the seeds of that general principle have been present for some time. The judgment drew heavily on the reasoning underlying the price/cost test established in landmark predatory pricing case of *Akzo*, in which it was held that pricing below variable cost is unlawful because an equally efficient competitor could not profitably match those prices. Similarly, the ECJ in *Post Danmark* also referred to its more recent rulings in the *Deutsche Telecom*

and *TeliaSonera* cases that established the equally efficient competitor test and the need to prove capability to foreclose in the margin squeeze context.

Nevertheless, in stating the principle in such general terms, the Court appears to have closed off the argument that targeting the customers of a competitor with special discounts might be abusive even if it passes a price/cost test (cf *Compagnie maritime belge*). While the Court left open the possibility of proving anti-competitive intent where prices are above variable costs but below total costs (paras 27-29), the strong steer that the Court gave (as demonstrated by the quotes above) was that driving out competitors is acceptable behaviour so long as the prices offered could not drive out *equally efficient* competitors.

Although the ECJ's ruling in *Post Danmark* was an encouraging step towards establishing a unifying framework for these cases, there is still considerable room for improvement. The area most desperately in need of work is rebates. From an economic perspective, there is very little difference between offering a low price and offering rebates from a high price. While rebate schemes can be considerably more complex than linear pricing, even the Commission's *Guidance* acknowledges that from a competition perspective the basic question should be the same: is the dominant firm's pricing capable of foreclosing competition. At least part of that analysis must be a comparison of prices with costs.

Notwithstanding the Commission's own analysis of the point in its *Guidance*, just one month after *Post Danmark*, the ECJ declined to apply that principle in Case C-549/10 P *Tomra*. Rather than criticise the General Court's failure to compare Tomra's post-rebate prices with its costs, the ECJ harked back to its older *Michelin* case law to justify the proposition that the capability of a rebate scheme to foreclose competition can be assessed by reference to qualitative factors rather than by reference to prices and costs (*Tomra* paras 67-82). Further guidance on the relevance or otherwise of the Commission's *Guidance* in rebate cases is likely to be provided when the General Court gives judgment in the *Intel* case that it heard in Summer 2012.

Whatever approach the Court takes in *Intel*, there is still further room for progress in the areas that are at the forefront of the equally efficient competitor approach: predatory pricing and margin squeezes. In *TeliaSonera* the ECJ ruled that the analysis of foreclosure in margin squeeze cases requires *more than* just a price/cost test (para 61). The Court acknowledged that, even if a vertically integrated dominant firm's retail prices were higher than its wholesale prices (so that equally efficient downstream competitors relying on the dominant firm for wholesale supplies could not profitably match its retail prices), those prices might not be capable of excluding competition for other reasons. The most obvious reason for that in the margin squeeze context would be that the downstream competitors might be able to obtain equally viable wholesale supplies from elsewhere.

Recent cases in the United Kingdom demonstrate, however, that the need for more than a price/cost test goes far wider than issues about indispensability of wholesale inputs. The United Kingdom's telecommunications regulator, Ofcom, recently issued a "no grounds for action" decision in *BT/Gamma* that illustrated that point. In that case, Ofcom found that BT had imposed a margin squeeze on its competitors over a nine-month period (in the sense

that its average retail prices had been too low for competitors relying on its wholesale prices to match them in that period). However, that finding was largely driven by the very low retail prices that BT accepted on one particular contract. In reaching the conclusion that BT had *not* thereby abused its dominant position, Ofcom took into account the fact that (on the particular facts of that case) offering low prices on just one contract could not have foreclosed competition in the market as a whole.

Ofcom's approach in conducting that analysis of effects is consistent with the general principle articulated in the *Post Danmark* selective pricing case discussed above. Yet it is not clear whether the same principle would be applied in a straightforward below variable cost predatory pricing case. The ECJ in *Post Danmark* seemed to endorse the strict prohibition of below-cost pricing set out in *Akzo* (para 27). Regulators in the United Kingdom still seem to be following that approach too: in the *DB Schenker* case in 2010, for example, the United Kingdom's rail regulator, the ORR, considered whether DBSR had offered below-cost prices on a single contract. The ORR concluded that DBSR had *not* done so, but its decision was a missed opportunity to consider whether in the predatory pricing context anything more than a price/cost test might be required. It is difficult to see why a different approach should be taken for predatory pricing: after all, margin squeezes are often economically indistinguishable from predatory pricing by downstream businesses, because the wholesale price charged by the vertically integrated dominant firm to downstream competitors is (often) a variable opportunity cost of making downstream sales.

No doubt it will take a few more years to see whether the Commission's *Guidance* and the ECJ's recent (if partial) enthusiasm for the equally efficient competitor foreclosure test herald a real change in approach that could bring about a unification of this part of the Article 102 TFEU field. But the potential benefits of harmonisation are great. Abuse of dominance cases are becoming more complex all the time, with increasingly sophisticated use of economics. Finding the answer in a difficult case is likely to become easier once it becomes clearer what the question is.