Bocconi

NOTE ON THE ENFORCEMENT OF ARTICLE 102

Chiara Fumagalli and Massimo Motta

26 October 2023

Università Bocconi
ETTORE BOCCONI
DEPARTMENT
OF ECONOMICS

Index

1. GENERAL DEFINITION OF EXCLUSIONARY ABUSES

Università Bocconi
ETTORE BOCCONI
DEPARTMENT
OF ECONOMICS

1.a Objective of enforcement

— In line with EU competition law, it should be consumer welfare.
  - Interpreted broadly
  - Forward-looking perspective
  - Balance of harm approach

— Other objectives mentioned in the jurisprudence of EU Courts may be misleading
  - Protection of competitive structure/competitive process: what does it mean exactly?
  - A given conduct of the dominant firm can make the market less constestable/more concentrated and be beneficial for consumers.

1.b Definition of abuse

— For an exclusionary abuse to be established it is necessary to show that the conduct produces anti-competitive effects by harming consumers.*

→ As shown by a large body of academic work, the anti-competitive effect can derive from practices that **aim at excluding rivals** but also from practices whose primary goal is not exclusion and **foreclosure is a side-effect.**

→ A conduct should not be considered automatically abusive because of «**its shape**».

→ Effects should be **appreciable**.

→ Effects should be assessed on consumer welfare, **not on rivals**.

* Our understanding is that this interpretation is in line with the view expressed in the Competition Policy Brief No 1/2023 (Section III.A)

1.b Definition of abuse

— Other concepts are difficult to reconcile with an economic notion:

- «Lack of competition on the merits»: what does it mean?
  - **A conduct that does not make sense taking as given the existence of competitors?**

    Economic theory has rationalised the use of practices that are detrimental to consumers without aiming at excluding rivals (foreclosure being a side-product).

  - **A conduct that involves sacrifice of profits?**

    Economic theory has shown that there are anti-competitive practices that do not involve profit sacrifice

  - **Absence of a «level playing field» ?**

    AA cannot intervene whenever there exist asymmetries.

  - **A conduct that «automatically» exclude rivals?**

    They may generate efficiency gains and benefit consumers.

1.b Definition of abuse

— Other concepts are difficult to reconcile with an economic notion:

- « Making it harder for rivals to compete»: but also pro-competitive conduct does that!

1.c Form versus effects of conduct

— The economic literature shows that contracts and rebates conditional on buyers purchasing a large proportion (**contracts that reference rivals**) of their needs from the dominant firm have a stronger anti-competitive potential than other practices.

- Exclusive dealing contracts and market share contracts allow a dominant firm to exploit a first-mover advantage and deter entry.

- Practices that reference rivals can manipulate the buyer-rival relationship so as to allow the dominant firm to extract rents from rivals → (total or partial) foreclosure due to uncertainty.

- Practices that reference rivals can be used by a dominant firm to generate a demand-boosting effect and raise its prices → (total or partial) foreclosure is a side-effect.

1.c Form versus effects of conduct

— The economic literature also shows that such practices might also exert beneficial effects on consumers

- promotion of relation-specific investments; by making competition more intense.

→ We favor establishing a rebuttable presumption: they are abusive unless the dominant firm is able to prove otherwise.

— The standard of proof for rebuttal should be higher the stronger the extent of dominance.

1.c Form versus effects of conduct

- A growing literature points to the anti-competitive effects of tying:
  - To **exclude** (partially or totally) rivals from the tied markets
    - Imperfect rents extraction
    - Scale economies in the tied market
    - Commitment to aggressive behavior in case of entry
  - To **increase prices** in the tied market (softening of competition)
- However tying is also a way through which firms continuously innovate and produce significant improvements for consumers.
- Rebuttabal presumption also in this case?

1.d Partial foreclosure

— An exclusionary abuse may also consist of partial rather than full exclusion.

- However, not any shift in market share from the rival to the dominant firm should be interpreted as partial foreclosure.

— Effects should be appreciable (in terms of coverage and being non-occasional).

- Absence of a *de minimis* rule in Article 102 should not be interpreted to mean that all conduct which seems to exert some exclusionary effects is necessarily abusive.

2. THE AS-EFFICIENT-COMPETITOR TEST

Università
Bocconi
ETTORE BOCCONI
DEPARTMENT
OF ECONOMICS

2.a The role of the AEC test

— **Price-cost** tests can be informative evidence for predation and rebate schemes that do not reference rivals (selective price cuts, quantity rebates, etc.).

— The test should be complementary to a convincing theory of harm: well-specified mechanism that rationalises the incentive to exclude consistent with the facts of the case.

— In line with the current case-law approach,

- prices > LRAIC: strong presumption of legality
- prices< AAC: strong presumption of abuse
- Inbetween: abuse established if available evidence (including documentary evidence on intent). supports a clearly defined theory of harm

2.a The role of the AEC test

— We agree with this approach even though economic theory does not suggest that a price-cost test is the criterion to distinguish prices that are predatory from those that are not.

- A safe harbour for prices above costs avoids the risk of chilling legitimate competition.
- Prices below costs are an administrable proxy of **profit sacrifice** (not as replicability test).

— This interpretation of the price-cost test:

- Guarantees legal certainty (based on information available to the dominant firm).
- Efficiency of the rival is irrelevant (as well as quality, product differentiation, innovation).

2.a The role of the AEC test

— Economic theory shows that selective price cuts and quantity rebates may allow the dominant firm to target aggressive price offers to specific customers or specific portion of the demand of customers facilitate exclusion

- Evidence that the price averaged across **all** customers or **all** units purchased by a given customer is above costs should not be enough to conclude lack of abuse.
- When rebates are retroactive, the discounted price to compare with costs requires an **estimation of the contestable part of the demand**.

— Formulation of a solid theory of harm indispensible:

- To guide the application of the test
- Because the price-cost test involves inevitably elements of complexity (on the determination of the cost thresholds, on the estimation of the contestable part of the demand, etc.)

2.a The role of the AEC test

— Similar approach applies to bundled rebates (unless full-line forcing) and margin squeeze.

2.a The role of the AEC test

— For the practices for which we favor a rebuttal presumption, such as exclusive dealing and discounts conditional on buyers purchasing a large proportion of their needs from the dominant firm, evidence of prices above costs should not be treated as discharging the burden of proof of the dominant firm.

- Economic theory has demonstrated that their anti-competitive potential is stronger.
- Profit sacrifice is not be necessary to exclude.
- The price-cost test may be misleading when the goal of the practice is to sustain (immediately) high prices.

— Key role of the theory of harm (and all quantitative and qualitative evidence available) when it is not clear whether a given practice triggers the presumption.

2.b «Not-yet-as efficient competitor» test

— When it makes sense to run a price-cost test, prices and costs to compare are the ones of the dominant firm (because proxy of profit sacrifice).

— The efficiency level of the rival should not be informative → we do not favor a «not-yet-as-efficient competitor» test.

— We acknowledge that:

- Also less efficient rivals can exert significant competitive pressure.
- In dynamic markets the rival may be less efficient at present, but may turn into a disruptive competitor in the future, conditional on achieving sufficient foothold in the market.

— But such a test would undermine legal certainty of the dominant firm and might be distortionary.

3. VERTICAL FORECLOSURE

Università Bocconi
ETTORE BOCCONI
DEPARTMENT
OF ECONOMICS

3.a Indispensability

— The economic literature does not show that indispensability of the input is a necessary condition for a dominant firm to engage in vertical foreclosure (which includes outright refusal to supply, margin squeeze, self-preferencing).

— Therefore,

- For a vertical foreclosure action, the input at issue should be a crucial asset but not an indispensible one (within the *Bronner* meaning)
- All vertical foreclosure cases should be subject to this principle → Ourtright and constructive refusal to supply* should not be subject to different standards, such as requiring indispensability for the former but not for the latter.

*input supplied at an arbitrarily high price, access delayed continuosly, interoperability degraded.

3.a Indispensability

— To preserve incentives to innovate and invest, we would find it justified to limit vertical foreclosure actions to dominant firms that:

- Have not committed considerable resources, effort, creativity or acumen to develop the input;

or

- Have already abundantly gained from their input.

or

- Are already subject to regulatory obligations to share their input with others.

3.b Self-preferencing

— Situations where an integrated firm discriminates in favor of its (first party) services or products to the detriment of those of a rival (third party) → self-preferencing as a form of vertical foreclosure.

- same considerations about indispensability apply.
- price-based self-preferencing should be assessed under the usual margin squeeze approach.

— Limiting principles:

- As for other forms of vertical foreclosure, self-preferencing might have objective justifications (that should be supported by unambiguous and objective evidence).
- In some situation self-preferencing might not have appreciable effects.
- In some situations what appears as self-preferencing is an efficiency.

→For self-preferencing to constitute an abuse, detrimental effects on consumers should be shown.

THANKS.

Università Bocconi
ETTORE BOCCONI
DEPARTMENT
OF ECONOMICS

Università Commerciale Luigi Bocconi
Via Sarfatti 25 | 20136 Milano – Italia | Tel +39 02 5836.1