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The dominance concept: new wine in old bottles

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*The views expressed are those of the author and do not necessarily reflect those of DG COMP or the European Commission

Dominance as a necessary condition

- The EU treaty prohibits single-firm conduct that harms consumers only when undertaken by dominant companies (Article 82).
- Possible reasons:
  - Provide legal certainty
  - Impose discipline on the EU Commission
- It didn’t fully worked because:
  1. The concept of dominance is somewhat elusive
  2. It became increasingly difficult to define dominance
  3. Ultimately proof of dominance was almost sufficient to establish an abuse (the special responsibility doctrine)

1. Dominance ≡ Substantial Market power

- All firms have some market power, though most have very little.
- Accordingly, the relevant question in antitrust cases is not whether market power is present, but whether it is important (i.e. substantial).
- European Court of Justice (1978) defines dominance as the:

  "…power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers."

  - That is, a firm is dominant if its decisions are fairly insensitive to reactions of competitors and customers
  - Elasticities are a measure of this (in)sensitivity and of market power

behave independently to an appreciable extent

≡

ability to significantly and profitably and durably increase prices

2. Factors that determine if a firm has substantial market power

- Significant[2] market shares
- Barriers to entry and expansion (in the absence of the conduct)
- No technological leapfrogging
- Lack of countervailing buyer power.

The acid test:

is the firm the <u>most efficient</u> in the market?

3. Dominance is only a screen

- If a practice is shown to be anti-competitive the firm must be dominant
- But proving that a practice is anti-competitive is hard and takes time. This requires scarce resources and reduces legal certainty
- Further, large players may not be dominant
    1. innovation is taking place at a rapid pace
    2. there is fierce competition between large players
    3. strong disciplining by potential entrants or customers
- A dominant firm (if merger control is effective) normally has lower costs or sells superior products.

Non-hypothetical example

- The EU Commission recently reviewed a complain where:
  - defendant had high market shares in a homogenous good market (above 60%)
  - Important barriers to entry could be identified: large overcapacity, declining demand, high fixed costs to establish new facilities, strong learning effects
  - Extensive use of long term contracts and thus limited customer switching
  - Defendant had the broadest product and technological range and the largest financial resources.

- The EU Commission concluded the defendant was <u>not dominant</u> because:
  - Buyer concentration (top 3 customers take 70%)
  - Product homogeneity allows to switch supplier without incurring significant switching costs
  - Buyers have dual sourcing strategy and shift volumes between suppliers
  - Rival suppliers have overcapacity
  - Competition mechanism: bidding for large occasional contracts

Careful use of market shares

- The use of market shares is often advocated:
  - To set up a bright line safe harbour
  - To allow for an implicit safe harbour for non-leaders
- Bright-line safe-harbours make sense but the threshold should not be placed too high. The "non-leader" safe harbour makes no economic sense. Examples:
  - Rivals are constrained (e.g. electricity industry)
  - Strong multi-market presence (e.g. airline industry)
  - Market leader are more constrained by regulation than non-leaders (e.g. telecoms)
  - Leader may be more constrained by close substitutes or by new entry (e.g. pharma)
- Policy justifications:
  - Consistency with unilateral effects in merger control
  - Leave open the door to "attempted monopolisation"

A remark on market delineation

- The EU Notice explicitly adopts the Hypothetical Monopoly Test (HMT) to delineate market boundaries for mergers, agreements and single-firm conduct
- The HMT is a useful conceptual tool to identify competitors constraining the defendant
- The assessment of dominance serves the same purpose but takes it one step further: how much is the defendant constrained?
- Often, market definition will be a by-product of the dominance assessment.
- This reflects that market definition is only a means to an end. The real issue of interest is market power.