EXPERT REPORT SF

FOCUSING ON EXCLUSIONARY PRACTICES

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This note proposes justifications for focusing competition authority resources on exclusionary conduct claims over, but without condoning, excessive pricing claims when both issues are raised in the same case.

A. EXCLUSIONARY VS. EXPLOITIVE CONDUCT

It is common to distinguish between exploitive and exclusionary forms of abuse of dominance. Professor Eleanor Fox describes the distinction this way:

> One is the microeconomic model popularly used in the United States today, which counsels no antitrust intervention unless the transaction is likely to diminish aggregate consumer or total wealth (thus, the critical importance of the welfare triangle to show output limitation). According to this methodology, there is no "exclusionary" violation; the violation is exploitation. The second methodology begins on a larger canvas. The analyst looks at the market structure and dynamics, and asks whether the practice interferes with and degrades the market mechanism. Freedom of trade (and competition and innovation) without artificial market obstruction is presumed to be in the public interest, especially the public's economic interest. Barriers must be justified. By this metric, significant unjustified exclusionary practices are anticompetitive and should be prohibited.[2]

Bellamy and Child's treatise describes exploitive conduct as that which is unfair or unreasonable towards those who depend on the dominant firm for goods or services; exclusionary conduct extends or preserves market power by excluding actual or potential competitors.[3]

Refusal to deal and essential facility theories primarily target exclusionary conduct. Excessive pricing theories generally target exploitive conduct.

Many cases will involve both exclusionary and exploitive conduct. A dominant firm may achieve the market power necessary to price its product excessively through conduct that excludes competitors. Thus it will nearly always be possible to allege excessive pricing to the detriment of consumers in any case involving exclusionary conduct – excessive pricing is normally the harm that consumers bear from the exclusionary conduct. Eleanor Fox explains:

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[2] Eleanor M. Fox, *What Is Harm To Competition? Exclusionary Practices And Anticompetitive Effect*, 70 Antitrust Law Journal 371, 372 (2002).

[3] PM Roth (ed) *Bellamy and Child European Community Law of Competition* (Sweet & Maxwell London 2001) par 9-072.

> It is accepted wisdom that the greatest economic evil of monopoly (or dominance) is the condition of market power because market power — especially monopoly power — leads to elevated prices and deflated output. The monopolist gets higher profits even while selling fewer goods; thus by definition the monopolist fails to satisfy demand at cost including a reasonable return on investment. Excessive pricing is theoretically the paradigmatic offense.[4]

While cases involving exclusionary conduct will nearly always accommodate excessive pricing claims, there may be cases of excessive pricing that do not involve exclusionary conduct. This may be true where there is a natural monopoly – a monopoly for which exclusionary conduct is not necessary to maintain market power. In such cases, competition authorities may be forced to evaluate exploitive practices such as excessive pricing because there are no other avenues to ensure that consumer interests are protected.

B. ADDRESSING CASES INVOLVING BOTH EXCLUSIONARY AND EXPLOITIVE CONDUCT

The question arises as to how to approach complaints that raise both exclusionary and exploitive conduct. One option is to focus analysis on the claim of exclusionary conduct, without condoning the excessive pricing. This option may be supported by several justifications.

1. **Focusing on exclusionary conduct as cause of the harm.**

Focusing prosecutorial resources on exclusionary conduct will in many cases target the cause of the harm to consumers – the limitation of competition – rather than the effect – excessive pricing. By focusing on the cause of the harm, the logical remedy – promoting competition – will in most cases remedy the excessive pricing as well. In the case at hand, for example, a compulsory licence will address both the exclusionary conduct and, by allowing lower cost suppliers to enter the market, the excessive pricing as well. Pursuing the excessive pricing claim will add little or nothing to the remedial outcome of the case.

2. **Conserving administrative and judicial resources.**

The consequence of focusing on the root cause of the harm may be a conservation of judicial and administrative resources. As mentioned above, it will nearly always be possible to bring an excessive pricing claim in conjunction with an exclusionary conduct claim and therefore a practice of analysing both claims wherever possible will likely consume significant resources. Because focusing on the exclusionary conduct is liable to remedy both alleged violations, the allocation of resources to the exclusionary conduct is more efficient.

3. **Focussing on institutional competence of authorities.**

Focusing on exclusionary conduct is also more in line with the institutional competence of competition authorities. It is not thought that courts or competition authorities have the expertise necessary to determine the right price for a particular good or service, and therefore

[4] Eleanor Fox Expert Report.

determining when a price is excessive – and what price should be demanded as a remedy – may be seen as problematic.[5] Eleanor Fox explains:

> [E]nforcement of an excessive pricing law entails difficulties. First, one might fear that depriving a firm of the fruits of its success (monopoly prices) may undercut its incentives to become successful in the first place. Second, determining when a price is sufficiently excessive and at what level the price is not exploitative are difficult tasks. Thus, there are problems of incentives if "excessiveness" is found too freely, and there are problems of administrability.[6]

Identifying exclusionary acts are the routine tasks of competition authorities and constructing remedies for violations found are far less problematic from an institutional competence perspective.

4. Adhering to common practice in other contexts.

For all the above reasons, it is rare for courts to intervene on excessive pricing bases when exclusionary acts have also been found. Competition authorities generally prefer to address exclusionary conduct rather than exploitative conduct, even where authorization to bring charges based on excessive pricing are present in authorizing legislation.

In the U.S. a focus on exploitive conduct is institutionally imbedded in legislation. There is no legislative prohibition of excessive pricing as such. This is true despite the fact that "[e]xcessive prices, maintained through the exercise of a monopolist's control of the market, constituted one of the primary evils that the Sherman Act was intended to correct."[7] Under U.S. law,

> unless the monopoly has bolstered its power by wrongful actions, it will not be required to pay damages merely because its prices may later be found excessive. Setting a high price may be a use of monopoly power, but it is not itself anticompetitive.[8]

It is widely recognized that there may be circumstances when prohibitions of exclusionary conduct alone will not address exploitive pricing of a dominant firm. Accordingly, "in this regard the United States is not the model for the world."[9]

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[5] *See* R Whish *Competition Law* (Butterworths London 2001 4th ed) 634-635 (arguing that government intervention based on price (1) might obstruct the self-correcting operation of normal market forces; (2) prevent expensive and risky research and development should a monopolist not be able to charge what the market will bear; (3) is confronted with formidable difficulties in determining whether a price is indeed exploitative; and (4) may find it difficult to translate a policy of price control into a sufficiently realistic legal test); Manuel Martinez, European Commission Administrator at the Directorate General for Competition, *Some Views on Pricing and EC Competition Policy* (explaining that a reason for the paucity of pricing-related abuse cases in Europe "can be found in the practical difficulties in establishing price abuses. I am not sure that every European company active in manufacturing would be able to state precisely what their real production costs are.").

[6] Eleanor Fox Expert Report.

[7] *Berkey Photo, Inc. v. Eastman Kodak Co*, 603 F.2d 263 (2nd Cir. 1979).

[8] *Id.*

[9] Eleanor Fox Expert Report.

The European Union provides the leading model for prohibitions of excessive pricing. But even there, competition authorities habitually focus their resources on exclusionary acts. In its 1994 Competition Report the E.C. Commission stated:

> [T]he Commission in its decision-making practice does not normally control or condemn the high level of prices as such. Rather it examines the behaviour of the dominant company designed to preserve its dominance, usually directed against competitors or new entrants who would normally bring about effective competition and the price level associated with it.[10]

There are many examples in the E.C. of competition authorities focusing their analytical resources on exclusionary practice rather than or prior to excessive pricing claims. In *United Brands*,[11] one of the first and most influential excessive pricing cases, the European Court of Justice was faced with allegations both that the respondent was excessively pricing its bananas in Denmark relative to other brands and that it was excluding competitors by refusing to deal with distributors that also distributed rival brands. Without stating a definite rule that pricing and exclusionary conduct claims would not be entertained in the same case, the Court remanded the excessive pricing complaint (based on the failure of the Commission to investigate the cost structure of the dominant firm) and decided the exclusionary conduct claim against the respondent. There is no record of further proceedings on the excessive pricing claim, perhaps because remedying the exclusionary conduct addressed the pricing behaviour as well.

The lead of *United Brands* has been followed in other cases. In *Decision of the Director General of Fair Trading, Exclusionary Behaviour by Genzyme Limited*, CA No. 93/3/03 (27 March 2003) the UK competition authority focused on Genzyme's tying practices (requiring the National Health Service to pay a price which included home delivery of Cerezyme) and the impact of the tying practice on blocking competitors from entering the market for supply of drugs to treat Gaucher's disease rather than focus on the extraordinary price of the drug Cerezyme, used to treat the rare Gaucher's disease. And in *Decision of the Director General of Fair Trading, Napp Pharmaceutical Holdings Limited and Subsidiaries* (Napp), No. CA CA98/2/2001 (30 March 2001), the UK competition authorities did reach a finding of excessive pricing for Napp's sustained release morphine, but only after initially finding Napp to have engaged in predatory pricing in the public sector segment of the market, with the predatory pricing behaviour positioning the firm to excessively price in the private sector.

In other contexts, courts frequently focus their analysis on alleged violations of the law that are most specifically responsible for the harm alleged. This is the approach of the South African Constitutional Court as explained in *Dawood v. Minister of Home Affairs* (7 June 2000). In that case, the Court stated that although any alleged violation of a right in the constitution may have an "incidental and limiting effect" on many other rights, it is the "primary right implicated . . . upon which we should focus."[12] Thus, although human dignity is itself protected in the Constitution and is offended in nearly every case involving a violation of another right, "the primary constitutional breach occasioned may be of a more

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[10] XXIVth Report on Competition Policy (Commission 1994) par 207, quoted in A Jones & B Sufrin *EC Competition Law: Text, Cases, and Materials* (Oxford University Press Oxford 2001) 328.

[11] *United Brands Company and United Brands Continental BV v. Commission of the European Communities*, Case No. 27/76 (14 February 1978).

[12] Para 36.

specific right such as the right to bodily integrity, the right to equality or the right not to be subjected to slavery, servitude or forced labour."[13]

CONCLUSION

In this case, the alleged transgressions of the Act most responsible for the high prices consumers are forced to pay involve excluding competition by refusing to licence competitors. Prohibiting the exclusionary acts under sections 8(b) and (c) will likely remedy the excessive pricing complaint by allowing consumers to access lower priced products in a competitive market. Accordingly, the submissions by the Competition Commission to the Competition Tribunal may request that the excessive pricing claims in this case be addressed only if it is found that there is no a sufficient basis for an open licensing order under sections 8(b) or (c).

[13] *Dawood* at para 35.