GUERNSEY COMPETITION & REGULATORY AUTHORITY

Guernsey Competition Law

GCRA Guideline 5 – Abuse of a Dominant Position

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What this Guideline is about

This Guideline is one in a series of publications designed to inform businesses and consumers about how we, the Guernsey Competition and Regulatory Authority (**GCRA**), apply competition law in Guernsey.

The purpose of this Guideline is to explain to consumers, businesses and their advisers the provisions in the Guernsey competition law in respect of abuse of a dominant position in a market: how to identify that a business is in a dominant position and the conduct that may be regarded as abusive. Specifically, this guideline has been prepared to explain section 1 of the Competition (Guernsey) Ordinance, 2012 (the **2012 Ordinance**).

This Guideline should not be relied on as a substitute for the law. If you have any doubts about your position under the law, you should seek legal advice.

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1 Introduction

Why is competition important?

Open and vigorous competition is good for consumers because it can result in lower prices, new products of a better quality and more choice. It is also good for fair-dealing businesses, which flourish when markets are competitive.

Competition law in Guernsey

In Guernsey, the 2012 Ordinance prohibits anti-competitive behaviour, including anti-competitive agreements between businesses and the abuse of a dominant position in a market. It also requires certain mergers and acquisitions to be notified to the GCRA for approval.

What powers does the GCRA have?

The GCRA has a wide range of powers to investigate businesses suspected of breaching the law. We can order that offending agreements or conduct be stopped and levy financial penalties on businesses and individuals for the breach.

What types of organisation are considered a 'business'?

Throughout this Guideline, we refer to a 'business'. This term (also referred to as an 'undertaking' in Guernsey competition law) means any entity engaged in economic activity, irrespective of its legal status, including companies, partners, cooperatives, States' departments and individuals operating as sole traders.

A Note on European Union (EU) Competition Law

Guernsey competition law is modelled on the competition provisions in the Treaty on the Functioning of the EU (**TFEU**). Section 54 of the 2012 Ordinance provides that the GCRA and the Royal Court may take into account the principles laid down by, and any relevant decisions of, the European courts in respect of corresponding questions arising under EU competition law[1].

Relevant sources of EU competition law include judgments of the European Court of Justice or General Court, decisions taken and guidance published by the European Commission, and interpretations of EU competition law by courts and competition authorities in the EU Member States. Section 54, however, does not prevent us from departing from EU precedents where this is appropriate in light of the particular circumstances of Guernsey.

[1] The provisions of section 54 were amended with effect from 23 February 2021 by the European Union (Competition) (Brexit) (Guernsey) Regulations, 2021, regulation 1, which replaced the word "must" with the word "may".

2 Abuse of a Dominant Position

Any conduct in a market by one or more businesses that amounts to the abuse of a dominant position in any market in Guernsey for goods and services, is prohibited and may give rise to the imposition of financial penalties.

The GCRA conducts a two-stage test when analysing these cases:

- whether a business is dominant in a relevant market; and
- if so, whether it is abusing that dominant position.

The prohibition relates to the abuse of the dominant position, not the holding of the position.

We would find conduct to constitute an abuse only after an examination of the market concerned and the effects of the conduct. Third parties adversely affected by the conduct of a dominant business may, in addition to making a written complaint to us, take action in the Royal Court to stop the behaviour and seek damages.

The 2012 Ordinance provides that an abuse of a dominant position may, in particular, consist of:

a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
b) limiting production, markets or technical developments to the prejudice of consumers;
c) applying dissimilar conditions to equivalent transactions with other trading parties and thereby placing them at a competitive disadvantage; and
d) making the conclusion of contracts subject to acceptance by other parties of supplementary obligations that by their nature or according to commercial usage have no connection with the subject of the contracts.

The examples listed above are illustrative only and should not be construed as definitive of exhaustive. The important issue is whether the dominant business is using its position in an abusive way. This may occur if it uses practices that restrict the degree of competition that it faces or it otherwise unjustifiably exploits its market position.

In conducting investigations of allegations of abuse of a dominant position, the GCRA will have regard to principles of EU competition law, including, in particular, the European Commission's Guidance on its enforcement priorities in investigating abusive exclusionary conduct by dominant businesses[2].

[2] OJ C 45/02, 24.2.2009

3 Exemptions

The GCRA has no power to grant exemptions from the prohibition of abuse of a dominant position. Section 3 of the 2012 Ordinance provides for exemptions by the Committee *for* Economic Development, on grounds of public policy, where there are exceptional and compelling reasons of public policy to do so.

4 Assessing Dominance

Having defined the relevant market or markets, it is necessary to determine whether the business has a market position amounting to dominance. A business may be dominant if it possesses a substantial level of market power. The essence of dominance is the power to behave independently of competitive pressures. This can allow a dominant businesses to charge higher prices profitably (or, if it is a dominant buyer, to extract lower prices) than if it is faced with effective competition. This means that a feature of a business with a dominant position is that it can successfully increase prices above a competitive level, or decrease quality, without losing enough business to make the move unprofitable. It can also use its market power to engage in anti-competitive conduct and exclude or deter competitors from the market.

The European Court of Justice has defined a dominant market position 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, customers and ultimately consumers."[3]

In assessing whether there is dominance, the GCRA will consider whether and to what extent a business faces constraints on its ability to behave independently. Those constraints might come from:

- **existing competitors**, according to their strength in the market: this may be shown by market share;
- **potential competitors**: this may be shown by a lack of significant entry barriers and evidence of the existence of other businesses which might enter the market in a manner that is likely, timely and sufficient; and
- **other constraints** such as strong buyer power from the businesses' customers (which may include distributors, processors and commercial users).

[3] Case 27/76 *United Brands v Commission* [1978] ECR 207, [1978] 1 CMLR 429

5 Market Shares

The 2012 Ordinance does not provide market share thresholds for defining dominance. Market shares can be an important factor in assessing dominance but do not, on their own, determine whether a business is dominant. It is also necessary to consider the position of other businesses operating in the same market and how market shares have changed over time. The weaker the position of its competitors and the higher and more stable the level of market share held by a business, the greater the degree of market power it is likely to have in the market.

The European Court of Justice has stated that dominance can be presumed, in the absence of evidence to the contrary, if a business has a market share persistently above 50 per cent.[4] The GCRA considers it unlikely that an individual business will be dominant if its market share is below 40 per cent, although dominance could be established below that figure if other relevant factors (such as the weak position of competitors in that market) provided strong evidence of dominance.

[3] Case C62/86 *AKZO Chemie BV v Commission* [1993] 5 CMLR 215.

6 Potential Competition

Another major factor in establishing dominance is whether the business faces, or is likely to face, competition from new entrants. An attempt to raise prices may prompt entry into the market and force prices down to their original level. If that is the case, a finding of dominance is less likely. The GCRA will therefore examine whether businesses would be able to enter the market and thereafter expand if they are given an inducement to do so, and whether there are any barriers which would prevent entry into the market. Market entry must be likely in commercial terms, of a scale that is likely to be sufficient to prevent a business from becoming dominant, and likely within a reasonably short timeframe.

There are many ways in which different types of entry barriers can be classified, but it is useful to distinguish between the sources:

- **Absolute advantage** – businesses may not have equal access to important assets or rights. For example, there may be regulations that restrict new entry, such as requirements to possess licences or permits. Copyright, patents and other intellectual property rights can be examples of these regulatory barriers, although such rights do not automatically imply that a business is dominant: it may be possible to innovate around these rights or there may be competition between holders of rival rights within the same market. Alternatively, businesses may have preferential access to important inputs, such as raw materials. For example, exclusive access, whether by law or in practice, to a port might be an absolute barrier to entry if other ports could not serve the same market;

- **Strategic advantages** – these are advantages which a business enjoys from being already active in a market (first-mover advantages). They can arise when new entrants would face sunk costs – those which must be incurred when entering a market but which cannot be recovered on exit. The importance of sunk costs in deterring new entry depends on whether new entrants expect to recover them from the revenue that they will earn operating in the market. If new entrants expect to face vigorous competition from existing businesses in the market, sunk costs are more likely to deter new entry. The importance of sunk costs, therefore, will depend at least to some extent on the conduct (or expected conduct) of the allegedly dominant business; if the incumbent itself has incurred sunk costs, that may make it more likely to respond vigorously to new entry. A strategic advantage might also arise if new entrants find it more difficult to fund the necessary investments than incumbents; and

- **Exclusionary behaviour** – a business may build up a reputation for unfair behaviour that deters new entrants. Businesses can also conclude contracts which tie up distribution: a manufacturer might tie up all retailers within a market exclusively to its products, for example. Such behaviour can increase the impact of an absolute or strategic advantage.

It is also important to take into account the rate of innovation within the market. In markets where high rates of innovation occur, or are expected, barriers to entry may be eroded quickly. It is important that competition policy does not undermine the incentives for such innovation.

7 Other Constraints

Lastly, consideration is given to whether there are other factors, apart from existing or potential competition, that will constrain the business's behaviour. The principal example is strong buyer power that might arise if customers are large relative to the business, well-informed about alternative sources of supply, readily able to switch from one supplier to another, or able to foster new supply (including own-supply). For example, a large retail chain may be able to resist attempts by a supplier with a high market share to take advantage of its position on the market. The key issue is the buyer's bargaining position relative to the seller. (On the other hand, a business with strong buyer power may itself be dominant. If it exploits its sellers, this could itself be an abuse, particularly if the business also enjoys market power in downstream markets.)

Businesses may also be constrained by Government regulations. In this situation the business may still be considered to be dominant although regulation may prevent it abusing that dominant position.

8 Collective Dominance

The laws prohibit abuse of a dominant position by *'one or more undertakings'*. This language mirrors that contained in Article 102 of the Treaty on the Functioning of the European Union (EU), and means that a dominant position may be held by two or more independent businesses, provided that from an economic point of view they present themselves or act together in a particular market as a collective entity. Businesses must therefore be sufficiently linked to each other to adopt the same conduct. The GCRA intends to follow, as far as possible, guidance under EU competition law concerning questions of collective dominance. While this guideline refers to a position of dominance in the singular, in all cases this should be read as including a position of dominance held collectively by two or more businesses[5].

[5] See for example, Cases T-68, 77 and 78/89, *Societa Italiana Vietro* ("Flat Glass") [1992] ECR II-1403

9 Abuse

If a business can be regarded as having a dominant position in a market, analysis of particular conduct then shifts to whether a business's behaviour might be regarded as crossing the line from normal competitive behaviour to an abuse of a dominant position.

The laws list broad categories of business behaviour within which particular examples of abusive conduct are most likely to be found, rather than specifically prohibiting business practices. Conduct may be abusive when it adversely affects consumers directly (through the prices charged, for example) or indirectly through the effects of conduct on the competitive process (for example, conduct which raises or enhances entry barriers or increases competitors' costs).

Conduct for which there is an objective justification, ie, a legitimate reason, is not regarded as an abuse even when it might restrict competition. An example is a refusal to supply that is due to the poor creditworthiness of the customer. Refusals to supply based on health and safety factors may also be objectively justified. However, it will still be necessary for a dominant business to show that such behaviour is proportionate to the objective justification, ie, does not go further than is necessary to achieve a legitimate aim.

Conduct that stems from the superior efficiency of a business is not an abuse – the purpose of competition policy is to encourage, not penalise, efficiency.

Abusive conduct generally falls into one of the following categories:

- Conduct that exploits customers (or suppliers) through, for example:
  - excessively high (or low) prices; or
  - discriminatory prices, or other terms or conditions; or
- Conduct that is anti-competitive (sometimes called ‘exclusionary behaviour’), because it removes or limits competition from existing or new competitors; for example, predatory behaviour. Vertical restraints (such as exclusive purchasing arrangements) and refusals to supply existing or potential competitors may also be abusive in some cases, but this will depend on the facts in each case.

The following examples do not constitute an exhaustive list of behaviour that the GCRA might regard as an abuse of a dominant position. They are likely to cover many potential cases, but each case will be considered on its own merits.

10 Excessively High Prices

An abuse of a dominant position may arise from directly or indirectly imposing an unfair purchase or selling price. A price charged by a dominant business may be unfairly excessive if "it has no reasonable relation to the economic value of the product supplied".[6] Note that there are several variables of competition and price is only one of those. The question is whether the difference between the costs actually incurred and the price actually charged is excessive and, if so, whether a price has been imposed that is either unfair in itself or when compared to other competing products.

Experience in the EU has shown that excessive pricing cases are very rare. Moreover, enforcement action against high prices and profits carries the danger of distorting the competitive process. This is because the ability to earn high profits in the short run has been recognised as a factor that can promote competition and innovation. High prices earned by a dominant firm should, in absence of barriers to entry, attract new entry or innovation, which should in turn bring prices down to competitive levels. A large disproportion between prices and costs may also be a result of efficiency – the dominant firm is more efficient than its rivals – and not abuse. Price controls feature more commonly in the regulation of previously monopolised sectors, such as telecommunications, where consumers need to be protected from excessive prices until competition becomes established, than in competition law.

[6] Case 27/76 *United Brands v Commission* [1978] ECR 207, [1978] 1 CMLR 429. See also Case 26/75 *General Motors Continental NV v Commission* [1975] ECR 1376.

In applying the laws to claims of excessive pricing, the GCRA therefore will be mindful of the need not to interfere in natural market mechanisms where high prices will encourage new entry or innovation and thereby serve to increase competition. Excessive prices are likely to be regarded as an abuse only in markets where a business is so dominant and new entry so unlikely that high profits are likely to persist without correction for a substantial period.

11 Price discrimination

Price discrimination involves applying different conditions (normally different prices) to equivalent transactions. It can take two main forms:

- the charging of different prices to different customers, or categories of customer, for the same product – where the differences in price do not reflect the quantity, quality or any other characteristics of the items supplied. The pricing structure would not be considered discriminatory, however, where there were objective and proportionate reasons for a business charging different prices to different customers – for instance, where there were different transport costs; or
- the charging of the same price to different customers, or categories of customers, even though the costs of supplying the product were different.

Price discrimination raises complex economic issues and is not automatically an abuse. Moreover, as with all alleged abuses of dominance, the GCRA may consider objective justifications for the conduct. For example, price discrimination might be objectively justified in industries where there are high fixed costs and low marginal costs (the cost of supplying each additional unit of output is very small compared to the initial investment to set up the business). It may therefore be more efficient to set higher prices to customers with a higher willingness to pay to recover the investment in fixed costs. In general, price discrimination will not be an abuse in such industries if it leads to higher levels of output than a business could achieve by charging every customer the same price.

We would consider price discrimination to be an abuse only if there was evidence that prices were excessive (as discussed above) or that it was used to exclude competitors, for example, because it was predatory or because it involved discounts designed to foreclose markets, these issues are explained in the sections on predatory pricing and vertical restraints, below. It would be unlikely to be an abuse if it resulted from a pricing obligation imposed by a regulator.

12 Discounts

The offering of discounts to certain customers is a form of price competition and generally is a positive benefit to consumers. As with price discrimination, discounts will infringe the competition laws only if they are anti-competitive: if prices are set at predatory levels or if they are used to foreclose a market.

Foreclosure can occur, for example, when discounts are conditional on customers buying all or a large proportion of their purchases from the dominant business (fidelity discounts), or where they are conditional on the purchase of a range of products. Fidelity discounts are not an uncommon practice. Businesses may offer such rebates in order to attract more demand, and as such they may stimulate demand and benefit consumers. However, such discounts — when granted by a dominant business — can also have actual or potential foreclosure effects similar to exclusive purchasing obligations. Rebates paid to customers that meet certain targets may be seen to be anti-competitive in some circumstances.

13 Predatory Behaviour

Predatory behavior, in particular through pricing, is a practice where prices are set so low as to eliminate one or more competitors and threaten the competitive process itself. In these circumstances, consumers may benefit in the short run from lower prices, but, in the long term, weakened competition will lead to higher prices, reduced quality and less choice. Distinguishing predatory behaviour from legitimate competition is difficult. Since the main objective of competition policy is to create conditions where consumers benefit from effective competition, the distinction must be drawn between low prices that result from predatory behaviour, and low prices that result from legitimate competitive behaviour. This is not an easy distinction to make and there have been relatively few EU cases where predation has been proven. The European Court of Justice has stated that where prices are below the average variable cost of production (variable costs are costs which vary with the amount of output produced), predation can be presumed.[7] In the normal course of business, selling at below average variable cost is unlikely to be rational and could be taken as conclusive proof of predation. A business failing to cover its variable costs (or pricing below its average variable cost) is, on average, making losses on each unit of output it supplies.

Selectivity in applying discounts or other forms of targeted behavior by dominant firms constitute forms of behavior relevant to considerations in this area of competition law. Intent of a party in setting prices as well as use of other variables of competition to achieve similar ends can also be relevant to assessments in this area which the GCRA may take into account when assessing concerns around predatory behaviour.

[7] Case C 62/86 AKZO Chemie BV v Commission [1993] and Tetra Pak II [1997] 4 CMLR 662.

14 Intentions

Where prices fall between average variable costs and average total costs, the GCRA would need to consider evidence on the dominant business's intentions before establishing whether its behaviour is predatory. Pricing in this range for short-run periods will often be a rational strategy for a business and represent legitimate competition. In that case, it would not be an abuse. If, however, prices were set at this level as part of a strategy to eliminate a competitor, this conduct would be considered an abuse. In addition to the evidence on costs explained above, the following areas of evidence on the business's intentions may be relevant:

- **Whether there is evidence of incremental losses** – predation is strategic behaviour whereby a business accepts short run losses in order to eliminate a competitor so as to charge higher prices in the future. The alleged predatory strategy therefore should lead to incremental losses for the business in the short run. In *Compagnie Maritime Belge*, the European Court of First Instance cited the fact that the parties 'admit having reduced their earnings' as evidence of an abuse**.** If, however, the alleged behaviour results in the business making higher profits (or lower losses) than it otherwise would, then that behaviour would be legitimate competition and would not be an abuse. Thus, where a business could demonstrate that its behaviour was increasing its profits (or reducing its losses), that particular behaviour would not be predatory.[8] The assessment of whether an action has resulted in higher or lower profits can be very complicated. Difficulties can arise in determining the appropriate comparison. Where the action is a straightforward price cut,

[8] *Compagnie Maritime Belge Transports SA and Others v Commission* [1997] 4 CMLR 273.

the best comparison is between the business's profits before and after the price cut. Where the price cut occurs at the same time as a new entrant enters the market, however, the incumbent business's profitability prior to the price cut is less useful, as its profitability would have been reduced by the new entrant in any case.

- **Other evidence on the behaviour of the business** – in some cases the behaviour of the business will indicate whether there is intent to behave predatorily against a rival. The actions of a business that targeted its price cuts against a new entrant, while maintaining its prices elsewhere, would be consistent with predation. Conversely, price-cutting across the board, not just in the areas where it competes with the new entrant, is not evidence of intent. Other evidence might include the timing of the action, whether the action follows a pattern of aggressive pricing or is a one-off or any other relevant evidence.

- **Documentary evidence** – in some instances, documentary evidence may determine whether a business intended to behave predatorily.

15 Feasibility of recouping losses

Predation involves businesses incurring short-run losses so that they can increase profits in the long run. In the short run, the business incurs losses in order to eliminate competitors. In the long run, it will expect to recoup the losses by charging higher prices (or offering less favourable terms). Predation works only if the business will be able to recoup its short run losses by charging higher prices in the future – which will be possible only if the business will not face significant competition in the future, for example from new entrants.

A dominant business can be expected to recoup losses in a market where it is already dominant. Consequently, the question of feasibility is likely to arise only where a dominant business is alleged to be engaging in predation in a related market where it is not currently dominant. In *AKZO* and *Tetra-Pak II*[9] the European Court of Justice found the businesses' conduct to be an abuse without explicitly considering whether recouping losses would be feasible. The GCRA therefore does not consider that it necessarily would be required to establish that recoupment was feasible.

[9] Case T-83/91 *Tetra Pak v Commission* (Tetra Pak II) [1993] ECR II-755

16 Vertical Restraints

Vertical restraints are arrangements between suppliers and purchasers that restrict the commercial freedom of one or more parties. They differ from horizontal agreements because they are arrangements between businesses at different stages in the supply chain, including between manufacturers and retailers. The same principles apply in the supply of services or property rights.

Vertical restraints can produce anti-competitive effects but they may also produce benefits which can outweigh any anti-competitive effects they produce. Any assessment of the effects of a vertical restraint needs to take account of both its potential anti-competitive effects and any countervailing benefits. While not all vertical arrangements are anti-competitive, the risk of anti-competitive effects is much higher when an arrangement includes a dominant business. European case law suggests that when a dominant business signs up customers to exclusive contracts, this is very likely to constitute abusive conduct.

Vertical arrangements are discussed in more detail in GCRA Guideline 11 – Vertical Arrangements.

17 Refusal to Supply

In general, businesses should be free to contract with who they choose and obligations to do so need to be justified. The European Court of Justice established in *Commercial Solvents* that refusal to supply an existing customer by a dominant business can be an abuse if no objective justification for the behaviour can be provided.[10]

Obvious justification for a refusal to supply might be that the customer had poor creditworthiness, or that supplies were cut for a temporary period due to capacity constraints. Another example of justification for a refusal to supply may be where it is based on genuine health or safety considerations. A key question in each case is whether the issue cannot be dealt with by less restrictive means.

A refusal to supply might also be used to impose a vertical restraint: a manufacturer imposing a selective distribution system is, by definition, refusing to supply outlets outside the system, in which case the principles explained above would apply. In other cases, refusal to supply may be used to exclude certain competitors, particularly in up-stream or down-stream markets.

[10] Cases 6 and 7/73 *Commercial Solvents v Commission* [1974] ECR 223, [1974] 1 CMLR 309.

More recent cases of this type have raised the question of whether the dominant business is abusing ownership of an essential facility. A facility can be viewed as essential if access to it is indispensable in order to compete in a market and duplication is impossible or extremely difficult owing to physical, geographic or legal constraints (or is highly undesirable for reasons of public policy).[11] Potential examples include ports, bus stations, utility distribution networks and some telecommunications networks. In general, ownership of an essential facility confers a dominant position. The refusal of access may then constitute an abuse. Essential facility questions have arisen in small islands such as Guernsey, where there may be only room for one facility.

[11] Judgment of the ECJ in Case C-7/79 *Oscar Bronner v Mediaprint and Others*, in particular the opinion of AG Jacobs, paragraphs 47 & 65.

18 Abuse in related markets

As explained at section 2 above, the test for abuse of a dominant position under the 2012 Ordinance: whether a business is dominant, and whether the business is abusing that dominant position. It is not necessary to show that the abuse was committed in the market which the business has a dominant position. In certain circumstances, the abuse of dominance prohibition may apply where a business that is dominant in one market commits an abuse in a different, but closely associated, market. This principle was laid down by the European Court of Justice in the case of *Tetra Pak II*[12].

19 Conclusion

The examples described above illustrate dominant company practices that may amount to abuse, but they do not constitute an exhaustive list. It is intended that this guideline assists in better informing businesses as to the nature of assessments under the relevant provision in the laws through a discussion of how similar provisions are interpreted and applied in other jurisdictions. The main question will be whether the conduct either exploits the business's customers, or reduces existing or potential competition without any objective justification, thereby maintaining or expanding the business's dominance.

[12] Case T-83/91 *Tetra Pak v Commission* (Tetra Pak II) [1993] ECR II-755

20 How can I find out more?

Please contact us if you have a question about the competition law or if you suspect that a business is breaching the laws and wish to complain or discuss your concerns.

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