contrast

In the Picture

How free are you, as a dominant undertaking, to determine your prices?

October 2018

Imagine...

You work for a company that is the undisputed market leader in its sector.

In an attempt to optimally exploit this market position, you propose to the Board of Directors to raise prices substantially for those products where your company has the largest market share. You did the necessary number-crunching and expect significant financial revenues from such an increase, since the competition is incapable of delivering products of equal quality, so that customers will buy your more expensive products instead of going elsewhere.

The Board of Directors lauds your work and approves your plan. If everything goes as anticipated, you will probably even get a promotion … Given that you want to move forward quickly on this, you decide not to consult with the legal department: they always make everything unnecessarily complicated.

A few months later, however, the legal department contacts you to relay the message that the National

Competition Authority has initiated an investigation against your company for applying excessively high prices. There goes your promotion!

During the investigation you propose to the Authority that it should not impose a fine on your company because you are prepared to cut the prices of the products far *below* the original prices.

The National Competition Authority is not at all amused by your proposal and lets you know that it sees this as a strategy to drive your competitors out of the market by offering products at excessively *low* prices.

You stand there transfixed, stupefied even. Excessive prices? Unreasonably low prices? Illegal? Fines? What is going on here? Is a company not free to set its own prices any longer?

A brief clarification.

Companies that hold a dominant position have a special responsibility not to impair effective competition. They may not abuse their dominant position by means of exclusionary or exploitative practices.

One of these special responsibilities entails that a company in a dominant position may not charge excessive prices to its customers. This is a prohibited exploitative practice.

An excessive price is one that is not reasonably related to the economic value of the delivered good or service. Whether a price is excessive or not is difficult to determine. There are several methods that are applied, including comparing the prices with the production costs, comparing the prices with prices in other countries and comparing sale prices with previously-charged prices. There is no excessive price-setting if there is an objective economic justification for the price increase, such as e.g. the evolution of raw material prices or increased costs for research and development.

Despite the problems of proof, several companies have recently been found guilty of charging excessive prices, including in Belgium, the United Kingdom, France and Latvia.

At the same time, a company holding a dominant position is *also* prohibited from going in the other direction and charging prices that are too *low*, especially when these prices are predatory prices. This too is a prohibited exclusionary practice.

Prices that are *below* the average variable costs are assumed to be predatory prices, while prices that are *above* the average variable costs but below the average total costs are predatory prices if these prices constitute part of a plan to squeeze a competitor out of the market.

In general, a dominant company has significant financial reserves and can thus afford to suffer losses

during a certain period of time. As a result, it can force its remaining competitors – who themselves may have lower reserves – out of the market. Once this has happened, it can recoup its losses by going back to charging higher prices.

Concretely:

When setting its prices, a dominant company must comply with competition law. More specifically, it must observe the following rules of thumb:

- Avoid price-setting that is intended to exploit customers or exclude competitors.
- Make sure that there is an objective justification for any sudden and substantial price increase, such as the evolution of raw material prices, increased costs for research and development or new legal obligations.
- The same applies for the sale of goods below their cost price: there must be a clear justification for this as well. Such justification could be the launch of a new product, clearing outdated stocks or the fact that the goods simply are not selling at a "normal" price.

Want to know more?

- Guidelines on the Commission's enforcement priorities, nos. 63-74.
- Opinion of Advocate General Wahl of 6 April 2017, no. C-177/16, EU:C:2017:286, AKKA / LAA.
- Judgment of the Court of Justice of 14 September 2017, no. C-177/16, EU:C:2017:689, AKKA / LAA.