Comments on the European Commission's discussion paper on the application of Article 82 of the Treaty to exclusionary abuses by Celesio AG

1. Celesio AG welcomes the move towards an effect-based approach and the bringing in line of Art 81 and Art 82 in assessing competition restrictions as set out by the Commission in its discussion paper. However, although the concentration on the market foreclosure effects of a company's conduct are welcomed and thus the general economic approach, Celesio would like to draw the Commission's attention to some thoughts and additional remarks on the Commission's reasoning in the discussion paper and also to the particularities of specific markets which acquire separate guidelines or at least specific provisions in the guidelines for these sectors as the general rules cannot provide for enough flexibility to account for these particularities without broaden their application so much as to render them impracticable.

2. These main thoughts can be summarised as thus:

- Market foreclosure effects on downstream markets can be an abuse of a dominant position even if the dominant undertaking is not itself active on the downstream market.

- In regard to the finding of a dominant position in certain cases the "one product one market" approach has to be taken. This is in particular the case where there is no substitute for the product in question.

- There is a need for further sectoral guidelines / regulations on the application of European competition law to specific markets, in which no free competition exists because of state regulation.

A. General comments on the discussion paper

3. The comments concentrate on the exclusionary conduct of refusal to supply but follow the structure of the discussion paper. References in brackets are references to the numbered paragraphs in the discussion paper.

4. The Commission sets out that the objective of Article 82 with regard to exclusionary abuses is the protection of competition on the market as a means of enhancing consumer welfare and of ensuring an efficient allocation of resources (3.), therefore aimed at preventing market foreclosure and the promotion of the single market as do the basic freedoms granted by the EC Treaty.

Dominant position on relevant market

5. Art 82 prohibits the abuse of a dominant position, thus a position of economic strength on a relevant market (11.), by an undertaking. The paper refers to the Commission Notice on the definition of the relevant market (OJ C 372, 09.12.1997) for details how to assess the competitive constraints on a company and hence the relevant market but does set out additional guidance in regard to the price-setting by the alleged dominant undertaking (SSNIP-test and cellophane fallacy). However, in this additional price-related guidance the paper sets out another approach which is to examine the characteristics and intended use of the products concerned and to assess whether there are, from the view of the
consumer, sufficient substitutes for these products (18.) The same approach is described in regard to single branding obligation. "[A] dominant position usually implies that for a good part of demand on the market there are no proper substitutes to the dominant supplier's product, because for instance its brand is a "must stock item" preferred by many final consumers or because the capacity constraints on the other suppliers are such that a good part of the demand can only be provided for by the dominant supplier. For distributors it may be necessary to trade in the dominant suppliers' products in order to be able to satisfy an important part of their customers' demand and in order to reach a viable scale of business. (143.)"

6. This approach, to take into account the substitutability of a product/service in question, can be generalised for exclusionary conducts, especially in regard to refusal to supply cases, to define the relevant market. This may also lead to the "one product - one market" approach where the product in question is not substitutable with any other. In situations where the products are not sold directly to the (end-)customer by the producer but undergo different stages of supply it has to be assessed on every level whether the product in question is substitutable for the buyer on that level in relation to his customer demands.

7. Also the general approach of referring to the relevant competitive constraints which the company's conduct has as its objective or effect to reduce or to eliminate can lead to the definition of the relevant market being one single product where the conduct in question seeks to reduce or eliminate other sources of supply for that product.

Dominance
8. The paper states the settled case law's definition of dominance as "a position of economic strength enjoyed by one 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, its customers and ultimately of the consumers. (20.)" And: "Market power is the power to influence market prices, output, innovations, the variety or quality of goods and service, or other parameters of competition on the market for a significant period of time. (24.)" One of these parameters is also the supply - it is a clear indication of substantial market power when a company is able to limit the supply with significant effects on the downstream markets, e.g. shortages and consequent loss of customers.

9. Where the product in question is unsubstitutable the producer has automatically a dominant position on the downstream market. This differs from the assessment of dominance in regard to horizontal competitors, where the barriers to expansion and entry have to be examined in addition to the market shares.

(Exclusionary) Abuse
10. "Article 82 prohibits exclusionary conduct which produces actual or likely anticompetitive effects [thus market foreclosure] in the market and which can harm consumers in a direct or indirect way. (55.)" This statement by the Commission is in line with the definition of "abuse" in exclusion cases by the European Court of Justice which implies "that the conduct in question must in the first place have the capability, by its very nature to foreclose competitors from the market. (cited in 58.)" Foreclosure is defined as denying actual or potential competitors profitable access to a market and is said to be market
distorting if it likely hinders the maintenance of the degree of competition still existing in the market or the growth of that competition and thus has a likely effect that prices will increase or maintain at a supra-competitive level. (58.) "To establish such a market foreclosure effect it is in general necessary to not only consider the nature or form of the conduct, but also its incidence, i.e. the extent to which the dominant company is applying it in the market, including the market coverage of the conduct or the selective foreclosure of customers to newcomers or residual competitors... In addition the degree of dominance will be a relevant factor. (59.)"

11. It is agreed that these are main factors to determine a market foreclosure effect and thus abuse, however, in addition the fact that the dominant company deliberately forecloses the market in full awareness of the effects should play a role in assessing if the conduct is abusive, which is without prejudice to whether the abusive conduct can be justified.

12. The paper goes on differentiating between price and non-price based exclusionary conduct with the latter having foreclosure effect, but still needs assessment whether this foreclosure is anticompetitive (61.). Also it distinguishes between horizontal and vertical foreclosure, viz whether the conduct is excluding an upstream or a downstream rival (69.). In regard to vertical foreclosure the paper refers to the refusal to supply cases and states that from a competition policy point of view, this is mostly only a worry if the dominant undertaking is itself active in the downstream market (72.). In the section on refusal to supply conducts the Commission repeats this assessment: "[In vertical foreclosure cases] although the excluded buyer could be only a customer, typically competition problems arise when it is also a rival to the dominant company in the economic activity for which the input is needed. (209.)"

13. However, the refusal to supply distributors, who are dependent on the product because of no existing substitutes with which to satisfy the consumers' demands, does create a market foreclosure on the downstream market without the dominant company being necessarily active on the downstream market itself. Competition is distorted with the market shares being frozen and it being quite impossible for newcomers to enter the market. This leads to partitioning of markets, especially where the refusal to supply has as its effect the elimination of other sources of supply with these products. One can compare these cases with single branding obligations which have by their nature the capability to foreclose and are anticompetitive when at least a substantial part of the market demand is bound (148. and 149.).

14. The paper then states: "For a refusal to supply to be [exclusionary] abusive, it must, however, have a likely anticompetitive effect on the market which is detrimental to consumer welfare." (210.) And: "An abuse may only arise when the termination is likely to have a negative effect on competition in the downstream market. (222.)"

15. These negative effects for consumers are obvious in the refusal to supply cases where there are no substitutes the consumers could be supplied with, especially in regard to products of general importance. Competition is completely excluded, particularly on the downstream market, and the refusal to supply leads to shortages to the detriment of the consumers' interests. In addition a conduct has anti-competitive effect when the dominant company uses the conduct to achieve another purpose (208.). As with the conduct of exclusive dealing and tying also the refusal to supply often pursues other aims such as preventing the sourcing of products from other Member States and thus partitioning of the market.
Objective justifications and efficiencies

16. Exclusionary conduct may escape the prohibition of Art 82 in case the dominant undertaking can provide an objective justification for its behaviour (objective necessity and meeting competition defence) or it can demonstrate that its conduct produces efficiencies which outweigh the negative effect on competition, with the dominant company bearing the burden of proof (77. seq.). The conduct concerned must be necessary for reasons of objective factors applying generally and be indispensable to the production or distribution of the products in question (80.). Also the efficiency justification requires the conduct in question to be indispensable to achieve the (alleged) consumer benefiting efficiencies. Moreover, even with all other conditions fulfilled the efficiency defence will fail when in respect of a substantial part of the products concerned competition is eliminated (84. seq.).

17. In cases of non-substitutability of the products, however, a refusal to supply will always lead to complete elimination of competition. In addition, it is because of the supply restriction itself that the consumers are in a worse position which could improve with the dominant company supplying the product. That is to say the dominant company creates the shortage to the detriment of consumers itself which it then remedies.

B. Specific comments on the discussion paper in regard to the particularities of the pharmaceutical supply market

18. The pharmaceutical supply chain is not governed by normal market conditions. Instead it is a highly state-regulated market with manufacturers, wholesalers and pharmacies being (partly) under public service obligations. Thus, wholesalers and pharmacies are in some Member States legally obliged to keep minimum quantities of stock available for prompt supply. And both the market authorisation holder (manufacturer) and wholesaler of medicinal products are under an obligation to ensure the appropriate and continuous supply of these products so the need of patients in the Member States are covered (Art. 81 para 2 of 2001/83/EC as amended). The health systems in all Member States are relying on this supply chain working.

19. Restriction of supply with pharmaceuticals to wholesalers will in general lead to the one product-one market definition as the distributor himself has no influence on which pharmaceutical products he has to deliver. Not only can he not substitute the ordered medicine he is not legally allowed to - only qualified dispensers as pharmacists and physicians are allowed to decide which medicines will be dispensed to the consumer. In case of prescription only medicines in general not even the pharmacist can substitute the prescribed product. The physician will specify the pharmaceutical exactly as to the active ingredient, the form, the quantity and also the supplier, choosing (where applicable) between the original, generic, parallel- or re-imported product. Every Member State has a numbering system for medicines to that effect distinguishing every single product. The wholesaler has to deliver the specified product ordered - if it is not on stock he cannot supply and neither can the pharmacist.

20. Therefore in the pharmaceutical supply market in all Member States products are not substitutable on all supply levels. The wholesaler can never substitute, the pharmacists only limitedly and not even the manufacturer himself would be able to supply a different
from the ordered product. Thus, a refusal to supply with pharmaceutical products leads automatically to market foreclosure and supply shortages to the detriment of the consumer and constitutes an exclusionary abuse.

21. Moreover, this refusal to supply cannot be justified on the grounds of public health as the same is jeopardised by the supply restrictions. Another justification for the supply restrictions could be the R&D argument which has also been referred to by Advocate General Jacobs in the Syfait-case (C-53/03) and which is part of the economic approach: There might be a positive effect of discrimination and exclusionary conduct as the duty to supply could lead to an adverse impact on the undertakings’ incentives to invest. This argument, however, is of little validity in regard to vertical supply restrictions. Instead, the typical cases in which discriminatory and exclusive competition might be beneficial and thus justified are the refusal to licence cases. To force the (dominant) intellectual property right holder to licence this right to less successful horizontal competitors may very likely induce the dominant company not to invest himself in R&D which would have a negative effect on the market in general. However, these refusal to licence cases are materially different from refusals to supply vertically. The prices for pharmaceuticals differ greatly in the Member States. Hence a producer has an interest to prevent parallel import of his (patent protected) pharmaceutical from a low-priced to a high-priced Member State which he can achieve with supply restriction on the pharmaceuticals in the low-priced Member States. But parallel trade has no (or only to a limited extent) impact on a manufacturer’s decision to invest in R&D, unlike a coercion to share its expensive developments.

22. This notwithstanding the pharmaceutical supply market is unique in its importance and amount of State regulation. The participants have all justifiable commercial interests which need reconciliation for the benefit of the secure and continuous supply of every patient in the Member States with medicines. In addition the governments in the Member States have to limit public spending to allow for financially feasible health systems. In other sectors the need for separate guidelines was recognised (e.g. the motor vehicle sector) to take account of market particularities. It is suggested that also the even more special pharmaceutical supply market requires separate rules to provide for the different interests of market players and State governments as well as for the general interest to secure public health.

23. Extra provisions and exemption as part of the general guidelines on the application of the European competition rules could allow for these particularities, considered the high regulation and the extreme differences to other markets it is suggested, however, that separate sectoral regulations or guidelines would be preferable.

24. Celesio would like to offer its support in the further discussions or next steps the Commission might embark on.