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KEY DEVELOPMENTS

European developments impacting dominant, vertically integrated operators – the TeliaSonera judgment

Introduction

On 17 February 2011, the European Court of Justice (ECJ) – on a reference for a preliminary ruling by the Stockholm District Court (SDC) – clarified, and indeed expanded upon, the scope of the law in relation to pricing practices of vertically integrated companies. The ruling impacts dominant, vertically integrated companies active both within and outside of regulated markets, such as telecoms. Companies on both sides of the Atlantic are therefore called upon to once again pay heed to the EU dominance rules (Article 102 TFEU).

Background

The Swedish Competition Authority (SCA) deemed that TeliaSonera (the dominant telephone company and mobile network operator in Sweden) had abused its dominant position by applying a pricing policy pursuant to which the spread between the sale prices of ADSL products intended for wholesale users, and the sale prices of services offered to end users, was insufficient to cover the costs which TeliaSonera itself had to incur to distribute those services to end users.

The SCA therefore brought an action before the SDC requesting that the latter order TeliaSonera to pay an administrative fine for having breached domestic and EU abuse of dominance rules.

The SDC decided to stay proceedings and refer a number of questions to the ECJ for a preliminary ruling. The ECJ was asked to clarify the circumstances in which the spread between, on the one hand, the wholesale prices and, on the other hand, the retail prices for services supplied to end users, resulting from the pricing practice applied by a vertically integrated telecommunications company, may constitute an abuse of a dominant position.

Ruling of the ECJ

In line with previous reasoning, the ECJ ruled that a practice adopted by a dominant company constitutes an abuse where, given its effect of excluding competitors who are at least as efficient as itself by squeezing their margins, it is capable of rendering entry of those competitors onto the relevant market more difficult or impossible.

The ECJ held that there would be such a margin squeeze if, inter alia, the spread between the wholesale prices and the retail services for services to end users were either negative or insufficient to cover the specific costs of the wholesale services which TeliaSonera must incur to supply its own retail services to end users. The spread must not allow an equally efficient competitor to compete for the supply of those services to end users.

The ECJ laid down a number of principles underpinning unlawful margin squeeze practices, the most salient of which are identified here:

1. Margin squeeze may, in itself, constitute an independent form of abuse distinct from that of refusal to supply, so that the legal conditions for the latter do not need to be met. This stands in contrast to its categorisation and treatment in the Commission's Guidance Paper and what was opined in Advocate General Mazak's Opinion.
2. Article 102 TFEU may apply even in the absence of regulatory obligations to supply. Vertically integrated undertakings operating in unregulated industries should thus pay heed to this judgment.
3. A margin squeeze can be considered an abuse of a dominant position in the absence of losses. Even if a dominant undertaking suffers losses in order to squeeze the margins of its competitors, there is no requirement that evidence must be produced in relation to the ability to recoup such losses.
4. An infringement of Article 102 TFEU is possible when the dominant undertaking in an upstream market is not dominant in a downstream market.
5. When assessing whether a pricing practice is abusive, as a general rule account should be taken primarily of the prices and costs of the undertaking concerned. On the other hand, the costs and prices of competitors may be relevant where, for example, the cost structure of the dominant undertaking is not precisely identifiable for objective reasons.
6. In order to establish whether a given practice is abusive in this context, that practice must have an anti-competitive effect on the market. It is sufficient to demonstrate that there is an anticompetitive effect which may potentially exclude competitors who are at least as efficient as the dominant undertaking. The fact that the desired result, namely the exclusion of competitors, is not achieved does not alter its categorisation as an abuse. The ECJ also states that the functional relationship of the wholesale products to the retail products must be analysed. Accordingly, when assessing the effects of the margin squeeze, the question as to whether the wholesale product is indispensable may be relevant. The ECJ furthermore held that if the level of margin squeeze is negative, an effect which is at least potentially exclusionary is probable. If, on the other hand, such a margin remains positive, it must then be demonstrated that the application of that pricing practice was likely to make it more difficult for the operators concerned to trade on the market concerned.

Conclusion

From a practical perspective, all vertically integrated undertakings active in Europe must be sure to tailor their commercial pricing policies in such manner that they comply with the EU dominance rules. This is perhaps not such good news for vertically integrated dominant companies, but may be welcomed by their competitors.