MyCC

GUIDELINES ON

CHAPTER 2 PROHIBITION

Abuse of Dominant Position

Malaysia Competition Commission

CONTENTS

These Guidelines are not a substitute for the Act or any Regulations that are made pursuant to the Act. These Guidelines may be revised should the need arises. The examples given in these Guidelines are for illustrative purposes only and are not exhaustive. They do not set a limit on the investigation and enforcement activities of the Malaysia Competition Commission ("MyCC"). In applying these Guidelines, the facts and circumstances of each case will be considered in totality. Persons in doubt about how they and their commercial activities may be affected by the Act may wish to seek legal advice.

The MyCC would advise enterprises to conduct self-assessment of their businesses in respect to their conduct, procedures, management and control. They should also have competition compliance procedures in place for all their employees at all levels, including the Board of Directors.

1. INTRODUCTION

1.1. Chapter 2 of the Act prohibits an enterprise from engaging (whether independently or collectively with other enterprises) in any conduct which amounts to an abuse of a dominant position in any market for goods or services in Malaysia.

1.2. In assessing whether there has been a breach of Chapter 2, the MyCC will proceed in two stages:

- firstly, the MyCC will ask whether the enterprise being complained about is dominant in a relevant market in Malaysia; and
- if the enterprise is dominant, then the MyCC will assess whether the enterprise is abusing that dominant position.

1.3. A dominant enterprise may abuse its position by:

- directly or indirectly imposing an **unfair purchase or selling price or other unfair trading condition** onto a supplier or customer;

- **limiting or controlling**: production; market outlets or market access; technical or technological development; or investment, **to the prejudice of consumers**;

- **refusing to supply** to particular enterprises or group or category of enterprises;

- **discriminating** by applying different conditions to equivalent transactions that: discourages new market entry or market expansion or investment by an existing competitor; seriously damages or forces a competitor that is just as efficient from the market; or harms competition in the market in which the dominant enterprise operates or in any upstream or downstream market;

- **forcing conditions** in a contract which have no connection with the subject matter of the contract (e.g. making the contract conditional on buying an unrelated product);

- **any predatory behaviour** towards competitors; or

- **buying up scarce supply** of inputs (either goods or services) where there is no reasonable commercial justification.

1.4. While the Act prohibits a dominant enterprise from engaging in certain conduct that its non-dominant competitors can do, the Act does not prohibit a dominant enterprise from engaging in conduct that has a reasonable commercial justification or is a reasonable commercial response to market entry or conduct by a competitor.

1.5. Market share shall not by itself be regarded as conclusive of dominance. Dominance shall be assessed in terms of the enterprises ability to act without concern about competitor's responses or ability to dictate the terms of competition in a market in Malaysia. Other factors such as barriers to entry, countervailing buyer power, etc. may also be used in the assessment of dominance.

2.
HOW WILL THE MYCC DETERMINE DOMINANCE?

2.1. An enterprise shall be dominant (whether as a supplier or a buyer) if it has significant market power in a relevant market in Malaysia. To assess whether an enterprise is dominant, first the relevant market must be defined in accordance with the MyCC's Guidelines on Market Definition. This involves determining both:

- the relevant product market; and
- the relevant geographic market.

2.2. In general, the MyCC will consider a market share above 60% to be indicative that an enterprise is dominant. (Please refer to para 2.9 to para 2.13 in the next few pages.)

2.3. Once the relevant market has been defined, the MyCC will determine whether an enterprise has a dominant position. Section 2 of the Act defines "Dominant Position" as follows:

> "Dominant Position" means a situation in which one or more enterprises possess such significant power in a market to adjust prices or outputs or trading terms, without effective constraint from competitors or potential competitors."

2.4. From an economic perspective, abuse of significant market power has two different categories of conducts for competition law purposes:

- firstly, "exploitative conduct" which is the ability of an enterprise to maintain price above the competitive level for some time without worrying about whether consumers will switch to other products or worrying that new competitors will enter the market.

- secondly, "exclusionary conduct" which is the ability of an enterprise to dictate the level of competition in a market by preventing efficient new competitors from entering or significantly harming existing equally efficient competitors – either by driving them out of the market or preventing them from effectively competing.

2.5. The ability of an enterprise to price well above the competitive level for a sustained period or the ability to actually drive an equally efficient competitor out of business provides evidence that the enterprise has considerable market power i.e. is dominant. Dominance is usually determined indirectly by using a range of criteria which is discussed below.

2.6. As explained in the Guidelines on Market Definition, the relevant market determines which enterprises compete in the market for the goods or services under investigation. Even if there is only one enterprise in a market – a monopolist – that by definition has no competitors, this situation would be considered as dominant position for competition law purposes.

2.7. So how much market power does the MyCC consider necessary to determine whether an enterprise is dominant? i.e. How significant is the market power of the enterprise? An enterprise with 100% market share is likely to be dominant because there is no competition. Even in markets where there are many competitors, where enterprises compete on product features as well as price, an enterprise may still have some limited market power – for example, local shops may be able to price higher than a supermarket in a shopping mall 10 kilometres away because consumers are prepared to pay a little extra rather then travel to the mall. The MyCC is not concerned with such cases of limited market power. Any possible benefit from increased competition would outweigh the costs of intervening. But, if in the preceding situation, the supermarket in a shopping mall had no competitors for 100 kilometres, then there could be some concern of abuse of dominant position.

2.8. So, whether an enterprise is dominant depends on a range of competitive conditions in the relevant market. Enterprises that are potentially dominant should carry out a self-assessment exercise to determine whether they could be dominant for competition law purposes in Malaysia and adapt their competitive conduct and ensure that they do not abuse their dominant position.

2.9. Whether an enterprise is dominant also depends on the constraints faced by the enterprise. These constraints include:

- existing competitors – here market shares of competitors provide a starting point for assessing the constraints competitors impose on the alleged dominant enterprise.

- potential competitors – the possibility that new entrants will come into the market if prices are set high by the alleged dominant enterprise. The possibility of new entrants depends on the barriers to entering the market. For example, a significant barrier is licensing requirements on entry.

- other constraints imposed by buyers with significant power or economic regulation imposed by government, such as price regulation.

Constraints Imposed by Existing Competitors: Market Shares

2.10. Market shares indicate the outcomes from *existing* competition. An enterprise that has a large market share could have obtained that position by either being more successful than competitors in meeting consumer needs or by anti-competitive conduct. The MyCC will assess the way enterprises compete in the market under investigation and determine whether existing market shares are the result of vigorous competition or anti-competitive conduct.

2.11. However, even if an enterprise has achieved its dominance by being efficient in the past, it still may be able to act anti-competitively either now or in the future. So, while understanding how dominance was achieved can be important, the main task is to determine whether an enterprise that is subject to investigation for abuse of a dominant position has significant market power now and so has the ability to adversely affect competition.

2.12. Section 10(4) of the Act makes it clear that market share is "not conclusive as to whether that enterprise occupies, or does not occupy, a dominant position." For example, even if an enterprise has high market share, it would not be considered dominant if it is not in a position to increase price above the current level due to the possibility of new entrants or imports.

2.13. Therefore, market shares should be seen as the starting point in assessing dominance. The calculation of market shares depends on the actual relevant market definition. Enterprises should be aware that the way they define their market and calculate their market share for internal reporting and marketing purposes may not be the relevant market defined by the MyCC. Enterprises may refer to the Guidelines on Market Definition issued by the MyCC for this purpose.

2.14. In general, the MyCC will consider a market share above 60% would be indicative that an enterprise is dominant. However, other factors will be taken into account in assessing dominance, such as whether there is easy entry into the market, etc.

2.15. For example, an enterprise with new product and with new features protected by patents could be considered dominant, even though it currently only has 20% to 30% of the market but its market share is rapidly growing as consumers switch to the new technology.

2.16. Evidence on market shares may come from a number of sources including:

- data provided by enterprises in the relevant market – enterprises will be asked for their sales data and their estimates of the market shares of their competitors;
- trade associations;
- market research reports; and
- internal market review.

2.17. Market shares can be calculated in several ways and often the MyCC will ask for information based on different methods of calculating market shares. For example, market share could be calculated on the basis of value (e.g. sales) or volume (the number of units) or even production capacity (the available number of units that could be produced) – which provides an indicator of how quickly sales could be increased in response to any abuse of a dominant position.

Other Competitive Factors That Would Be Considered by the MyCC:

2.18. Apart from market shares, the MyCC will also consider the following possible factors in assessing dominance:

Degree of product differentiation

- When there is product differentiation, market share figures may not provide a good guide to market power. For example, high-powered sports cars are unlikely to compete in the same market as budget cars. So, they would be defined as separate relevant markets for competition law purposes. But are luxury sedans in the same relevant market as similarly priced high-powered sports cars? Possibly. If the MyCC considered them part of the same relevant market for competition law purposes, then market shares may not provide a good indicator of the amount of competition in the market. The fact that they are differentiated to some degree by function and that the kinds of buyer are different would have to be taken into account in assessing whether there is dominance.

Likely response by buyers to price increases

- Some products have "must-have" status by some consumers – where this occurs then certain enterprises may be able to raise price more easily than others as their consumers will not switch due to perceived status or are locked-in technically to their products.

The degree to which innovation drives competition

- Some markets have continual product improvements and innovation. The extent to which competition is driven by product features rather than price would be taken into account. For example, a high current market share may indicate that an enterprise was successful in the past. But this product could be about to be replaced by a new product with a patented technology to which other enterprises do not have access. The enterprise with the new product may have considerable market power now and into the future even though it currently has a low market share.

Constraints Imposed by Potential Competitors: Are There Barriers to New Entry?

2.19. If new enterprises can easily enter a market where enterprise A has a 100% market share, then A may not be dominant. A must have obtained its current market share by being more efficient and charging less. That is, despite having a 100% market share, the threat of new entry means A cannot charge a high price or drive an equally efficient competitor out of the market. The threat of new entry stops A from doing so and so A is not dominant.

2.20. The MyCC may also consider any barriers to entry when assessing dominance. The MyCC may consider a potential barrier to entry into a relevant market by a new entrant. Barriers to entry include, but are not limited to:

Economies of scale or size:

- This occurs where the average costs of production fall as output increases. For example, where there are high fixed costs – as the number of units produced is increased, the high fixed costs are written off against more units of output therefore reducing the average total cost per unit of output. A new entrant also has high fixed costs but may require some time to achieve a sufficient output to be cost competitive with an incumbent.

Economies of scope:

- This occurs where fixed costs can be shared over a greater range of products – similarly to economies of scope, a new entrant may face higher costs until it can provide a similar range of products as an incumbent. If it takes too long to successfully offer a range of products, then a potential new entrant may decide not to enter at all.

Regulated entry:

- Licensing requirements may limit the number of new entrants or make it difficult for new entrants to satisfy entry criteria. If so, then an incumbent may be able to act without constraint.

- Any activities governed by the Second Schedule of the Act are excluded.

Limited access to necessary inputs or distribution outlets:

- Existing exclusive distribution arrangements may make it impossible to buy crucial inputs, such as materials or to lease space to sell competing products. In the extreme, an incumbent may have access to a facility that is necessary to produce a product – if it is not economically or technically feasible to reproduce the facility, then a new entrant that must have access to the facility cannot enter.

Network effects:

- In certain industries, consumers may value a product more highly because the product is widely used by other consumers. For example, a word processing programme that initially becomes popular because of its features is likely to attract new buyers. The popular software is more valuable to new buyers because they can share documents with more users and the skills gained by learning the popular programme will make them valuable to more employers. Furthermore, developers are likely to develop more add-on applications for the popular software – thereby increasing the value of the popular word-processing software even more. A new entrant faces considerable problems in persuading customers to switch to their product.

High sunk costs:

- Sunk costs are *irrecoverable costs*. For example, advertising costs cannot be recovered if a marketing campaign is unsuccessful. In consumer product markets, a new entrant may face high advertising costs to attract consumers away from existing products. If sunk costs are high, then entry may not occur at all and so an incumbent dominant enterprise can act without constraint.

Conduct by incumbents:

- This could include a threat to potential new entrants that it will behave predatorily if new entry occurs – for example, a dominant incumbent could threaten to set price below cost or prevent a new entrant from gaining access to a necessary technology.

Other Constraints

Imposed by powerful buyers

2.21. Some markets have only a few buyers, which gives buyer market power that offsets any seller power. For example, supermarket chains or media outlets exercise considerable buyer power over grocery suppliers and programme suppliers. Buyer power can offset or considerably diminish the ability of sellers to charge high prices or set trading terms.

Economic regulation imposed by government – such as price regulation

2.22. Where the final consumer prices are regulated, then the MyCC may consider whether the enterprise under investigation still has any market power over other dimensions of competition. For example, a dominant enterprise subject to price-regulation may still be able to exclude competitors by controlling downstream retail outlets.

Collective dominance

2.23. Chapter 2 makes it clear that dominance is not simply a conduct by a single enterprise but can also include conduct of enterprises exercising significant market power together.

2.24. Collective dominance cases are likely to be rare (collusion between independent enterprises is also caught by the Chapter 1 prohibition – which covers exclusionary conduct, such as collective boycotts). The MyCC will look at each case on its merits but in general, there may be a breach of the Chapter 2 prohibition if two or more separate enterprises, which have significant market power, act similarly in a market and that conduct excludes equally efficient competitors.

3.
WHAT IS ABUSE OF DOMINANCE?

3.1. Chapter 2 deals with two kinds of abuse:

- *Exploitative abuse* i.e. mainly setting high prices; and
- *Exclusionary abuse* i.e. predatory conduct that stops competitors from competing which leads, indirectly, to higher prices, lower quality products, less innovation, etc.

Exploitative Conduct

3.2. Exploitative conduct, such as excessive pricing may result from structural conditions in the market. For example, if a dominant enterprise believes there are likely no new entrants, then it will set a high price to exploit consumers. The resulting excessive profits are not a reward for innovation.

3.3. The MyCC may only be concerned with excessive pricing where there is no likelihood that market forces will reduce dominance in a market. This situation is not likely to be common and there are some sectors which are covered by price control legislation.

3.4. In determining whether prices are excessive, the MyCC will use several criteria, the details of which may differ from market to market. In principle, the MyCC may consider the actual price set in relation to the costs of supply and other factors, such as the dominant enterprises profitability.

Exclusionary Conduct

3.5. Exclusionary conduct is conduct that prevents equally efficient competitors from competing.

3.6. Exclusionary conduct shall be assessed in terms of its *effects* on competition – which means its impact on the competitive process and not its effects on competitors. Effective competition drives inefficient enterprises out of the market. So, even if an enterprise is dominant, it should not be stopped from engaging in competitive conduct that benefits consumers even if inefficient competitors are harmed.

3.7. The MyCC will use an *effects-based* approach as used elsewhere in assessing a potential abuse of a dominant position. By adopting this approach, the MyCC shall ensure that conduct which benefits consumers will not be prohibited and therefore ensure that enterprises have the incentives to compete on merits.

3.8. Adopting an *effects-based* approach ensures good economic outcome consistent with the aims of the Act. In any event, it is very unlikely that dominant enterprises would not know the likely impact on competition from their actions.

3.9. In general, in assessing whether the effect of exclusionary conduct is an abuse or not, the MyCC will use two main tests for assessing anti-competitive effects:

- firstly, does the conduct adversely affect consumers?
- secondly, does the conduct exclude a competitor that is just as efficient as the dominant enterprise?

3.10. Some examples of exclusionary conduct by dominant enterprises that could be "abuse" are provided below. These are not exhaustive and are given to provide general guidance. Whether "abuse" will be found in a particular situation depends on the particular facts of each case. It should be noted that while certain kinds of conduct are described as constituting "abuse" in Chapter 2, there are also general catch-all provisions prohibiting conduct that constitutes "any predatory behaviour towards competitors."

Predatory Pricing

3.11. While consumers benefit from enterprises setting low prices, a dominant enterprise may set prices below its costs to drive other competitors out of business. Consumers benefit in the short term but they may lose out in the longer term as once the competitors are driven out of business, the dominant enterprise can raise price above the original level.

3.12. Enterprises may price below cost for many reasons. For example, a new entrant into the market may price below cost to gain initial market share or an existing enterprise may price a new product below cost initially to attract consumers. The issue is how to distinguish between pricing that is predatory and low pricing under Section 10(3) of the Act.

3.13. When considering whether a dominant enterprise is charging below costs, a number of different costs may be used. For example, for theoretical purposes, economists usually define predatory pricing in relation to marginal cost i.e. the cost of producing the last unit of output. However, from a competition law perspective, the concern is whether a dominant enterprise's price is reasonable across the whole relevant output and not just the last unit of output.

3.14. Several cost concepts are potentially relevant in the investigation of a predatory pricing claim. Different situations may dictate the use of different cost measures. The particular method used by the MyCC shall depend on the circumstances and particular conditions in the industry under investigation. The different methods include (but are not limited to):

- Average Variable Cost ("AVC") – this is a short-term cost concept, which is defined as the sum of all the costs that change as output changes, divided by the total quantity. All fixed costs are excluded.

- Average Avoidable Cost ("AAC") – this covers all the costs (i.e. both variable costs and the fixed costs directly related to the product under investigation) that could have been avoided if the dominant enterprise had not engaged in the predatory strategy. If an enterprise does not cover AAC, then it is giving up profits (i.e. *sacrificing* profits).

- Long-run Incremental Cost ("LRIC") – this is the change in total costs from the production of an increase in output (which can be either the total output or simply the increase in output due to the predatory conduct). So LRIC includes all the costs associated with the product under investigation even if those costs were sunk (i.e. non-recoverable) before the alleged predatory pricing conduct was engaged in.

- Average Total Cost ("ATC") – this is the sum of fixed and variable costs divided by total output.

3.15. In assessing predatory pricing, the MyCC may consider whether the price is below the cost and whether it is relevant to the particular fact of the case being investigated with a view of determining whether an *as-efficient* competitor is excluded.

3.16. Evidence of intent to drive a competitor out of business is not by itself indicative of predatory conduct. However, intention could be evidence of effect, i.e. that a predatory strategy is likely to succeed.

Price Discrimination

3.17. Price discrimination occurs where the same product is sold at different prices – the difference in price being unrelated to any differences in the cost of supplying the products. This includes both selling the same product to:

- different customers at a different price; and

- the same customer at different prices (e.g. off- and on-peak electricity charges).

3.18. An enterprise must have some control over price to be able to price-discriminate (i.e. has some market power). In order to price discriminate, an enterprise must be able to segregate customers into different groups and have the ability to stop arbitrage between the groups.

3.19. Price discrimination can be beneficial. Without it, everyone must pay the same price for the same product or service. By charging more to groups who can better afford it, price discrimination can lead to higher output by charging less to lower income groups, which can be welfare enhancing. For example, if patented drugs were sold at the same price around the world, many low-income countries could not afford to buy them. By charging a high price in developed countries and a lower price in less-developed countries (in the absence of arbitrage), more drugs are sold worldwide.

3.20. Price discrimination can also adversely affect consumers. For example, a dominant enterprise could charge low prices in geographic areas where there is more competition and cover losses by charging more in other areas that lack competition. This could force local competitors out of the market in the more competitive areas. Charging one buyer more than the other buyer may impact on competition in the downstream market. In particular, if the dominant enterprise has a subsidiary downstream, then charging a lower price for an important input to the subsidiary will mean other competitors downstream cannot compete. The MyCC may examine price (and other forms of discrimination on terms and conditions of supply) on a case-by-case basis.

Exclusive Dealing

3.21. An exclusive dealing arrangement between a dominant seller and a buyer can foreclose the market. For example, suppose a dominant supplier X has 80% of the wholesale market and establishes an exclusive dealing arrangement with buyer Y, a retail chain (now Y gains 80% of the downstream market). This means other buyers now cannot buy the product from X. Competitors of X are prevented from supplying to Y (i.e. the market supplied through Y is now foreclosed to them). The MyCC may assess whether exclusive dealing arrangements foreclose a significant part of the market, which limits the ability of competitors to compete on a case-by-case basis.

Loyalty Rebates and Discounts

3.22. Generally, loyalty rebates and discounts are pro-competitive.

3.23. However, a dominant enterprise may be able to use loyalty rebates and discounts to foreclose a market to competitors. An example would be preventing rivals from entering a market by using selective discounts or rebates.

3.24. Another example would be a loyalty rebate involving a supplier offering a discount for loyalty. Retail stores often depend on rebates for their profitability. Loyalty rebates are offered based on a buyer's past buying and rebates often increase as more is bought. For example, a supplier might give a 20% discount if a buyer buys at least 50% of their requirements from the supplier, 30% discount if at least 70% of the buyer's requirements are bought from the supplier, etc. If discounts are related to costs, they may be justifiable. However, non-costs related discounts may be structured in a way that these customers are not available to other competitors (i.e. some competitors are *foreclosed* from part of the market). How much of the market is foreclosed is the relevant issue. If the supplier offering the loyalty rebates is dominant, this means a significant number of buyers are foreclosed to the supplier's competitors.

Refusal to Supply and Sharing of Essential Facilities

3.25. Generally, enterprises are free to deal with whoever they choose. However, in some circumstances, a refusal to supply by a dominant enterprise may amount to an abuse.

3.26. Refusal to supply can cover a number of different kinds of refusal such as:

- a refusal to supply products to buyer – for example, X refuses to supply an input to a downstream buyer, Y, that Y needs – and X also competes in the downstream market with Y;

- a refusal to licence intellectual property rights;

- a refusal to grant access to infrastructure that is necessary (an *essential facility*) to supply certain products (e.g. telecommunications services, which need access to a telecoms network that cannot be economically duplicated).

3.27. The remedy for a refusal to supply is to force the supplier to supply at a reasonable consideration. However, forcing supply may reduce the incentive to invest in the product, intellectual property rights or essential facility. The MyCC will take account of the difficult trade-off involved in forcing supply, which leads to a short-term increase in competition but which may harm longer term incentives for innovation and investment.

Buying Up Scarce Intermediate Goods or Resources

3.28. Abuse also includes a dominant competitor in a downstream market buying all the supplies of scarce inputs needed by the dominant enterprise's competitors. This has the effect of increasing the cost of production to the dominant enterprise's competitors or preventing them from producing at all.

Bundling and Tying

3.29. Products are bundled if they are sold together at a lower price than separately. Tying occurs where a seller refuses to sell a product X unless the buyer also takes Y. For example, a car manufacturer might refuse to sell a car without an engine. Obviously, a buyer wants an engine so this would not normally be a competition problem. However, if a car manufacturer told a buyer that they must also take a mobile phone contract then it would essentially be forcing a product that the buyer would not want. It also means that other mobile phone companies would have a part of the market foreclosed to them (i.e. the buyers who buy the car). If the car manufacturer is dominant in the car market, then a significant number of customers will be foreclosed from a significant part of the market for mobile phones.

3.30. In general, the main issue from the MyCC's perspective with tying or bundling is the possibility that an enterprise that is dominant in one market is trying to obtain market power in another market (i.e. *leverage* its dominance).

3.31. Bundling can also be used as a way of predatory pricing – for example, the price of one of the products, D, in the bundle may be set below AVC or LRIC and so make it difficult for other producers of product D to compete.

4. DOMINANCE AND ABUSE IN SEPARATE MARKETS

4.1. An enterprise that is dominant in one market in Malaysia can abuse that dominance in a separate market. For example, a dominant enterprise in one market could use the profits in that market to price below cost in a separate market (either product or geographic) to drive competitors out of business.

4.2. One example is where a dominant enterprise, X, who sells an essential input to downstream enterprises, sets up a subsidiary, Y, in the downstream market and then refuses to sell the input to other buyers in the downstream market. As a result, competitors are excluded in a market separate to the market in which X is dominant.

5. CAN CONDUCT THAT WOULD OTHERWISE BE AN ABUSE BE JUSTIFIED?

5.1. Dominant enterprises are not prevented from "taking any step which has reasonable commercial justification or represents a reasonable commercial response to the market entry or market conduct of a competitor."

5.2. The onus of proof justifying conduct that would otherwise be found to be an abuse rests with the enterprise claiming it. Some (non-exhaustive) examples could include a dominant enterprise:

- refusing to sell to a buyer who has not paid for past purchases.
- refusing to grant access to a dominant enterprise's infrastructure that is already being used to capacity.
- offering a loyalty rebate that is related to the reduced costs of supplying a particular customer.
- meeting a competitor's price even though the price may be below cost (in the short term).

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