

Excessive pricing enforcement action on the rise: a new enforcement trend?

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Summary

Although enshrined in the EU treaties since inception, 'unfair pricing' as an abuse of market power was a little-used tool in enforcers' armoury. Antitrust authorities are not set up to be price regulators presiding over precisely when a high price becomes a "price which bears no relationship to economic value". Sound economic principles dictate that one company's excessive price is another's incentive to enter the market and scoop up that margin. So, excessive pricing should be self policing. The few cases that were brought tended to be based on exceptional circumstances, and many failed on the facts.

A May 2017 EU probe has brought the abuse back to the enforcement agenda. However, this is unlikely to denote a new trend; it is too early to say that this is the new normal. The European Commission has been cautious in its statements on excessive pricing – EU Competition Commissioner Vestager underlined the need for caution: "when we do take action against excessive prices, we need to make sure we're not taking away the rewards that encourage businesses to innovate." European Court of Justice (ECJ) Advocate General Wahl also confirmed that the bar for regulator intervention in relation to alleged excessive pricing is high.

Legal test for excessive pricing under EU competition law

Article 102(a) of the Treaty on the Functioning of the European Union lists the imposition of "unfair selling prices" as a specific example of abuse of dominance. A high price charged by a dominant company will not be considered excessive (and hence not abusive and problematic under EU competition law) provided that the price has a "reasonable relation to the economic value of the product". Competition authorities are unwilling to be the judges of reasonableness in this context for as long as there is no 'plus factor' of conduct that does not qualify as "competition on the merits".

The leading ECJ judgment in *United Brands* holds that a price is unlawfully excessive where "it has no reasonable relation to the economic value of the product supplied". The legal analysis involves:

- determining whether the difference between costs actually incurred and the price actually charged is excessive (cost-price analysis); and
- if so, determining whether the price is unfair in itself (intrinsic economic value analysis) or when compared to competing products (benchmark comparison).

Cost-price analysis

Calculating what is a reasonable profit can be a complex exercise. Generating a high margin over costs alone is not conclusive of abuse in this context. Cost plus a reasonable profit margin may represent a baseline below which a price could not be considered excessive, but a price above that baseline may not necessarily be abusive.

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Intrinsic economic value analysis

The law recognises the validity of consumers' perception of the value of a product as an important aspect of this analysis. In *Port of Helsingborg* the European Commission stated in this regard that:

"[t]he demand-side is relevant mainly because customers are notably willing to pay more for something specific attached to the product/service that they consider valuable. This specific feature does not necessarily imply higher production costs for the provider. However, it is valuable for the customer and also for the provider, and thereby increases the economic value of the product/service."

In that case the excellent location of the port of Helsingborg, which allows ferries to cross the Oresund in an expeditious way, was taken into account. As such, a proper assessment of the economic value of a product should take into account factors such as cost savings resulting from superior efficacy, for example.

Benchmark comparisons

To determine whether a high profit margin results from the exercise of market power or from superior efficiencies in terms of costs or innovation, a number of comparisons may be relevant:

- a comparison of the prices charged by the dominant company with prices it charges in other (geographic) markets;
- a comparison of the prices charged by the dominant company with prices other companies charge in other (geographic) markets for the same product; and
- a comparison of the prices charged by the dominant company over time.

One of the challenges is that there is a lack of guidance from the European Commission and the European courts as to when the difference between a price charged and the economic value of the product is so big as to be considered excessive, and hence abusive. The European Commission is wary of effectively acting as a price regulator, so there is unlikely to be more clarity on this point in the near future.

Recent enforcement

Latvian collecting societies

In 2008 the Latvian Competition Council fined the national copyright collecting society for allegedly abusing a dominant position by charging excessively high copyright levies. On appeal, the Latvian Supreme Court requested clarification from the ECJ on how to assess excessive pricing allegations under EU competition law. Wahl delivered his opinion on April 6 2017, which was broadly in line with the *United Brands* framework.

He confirmed that there is "no single method, test or set of criteria" generally accepted in legal and economic thinking to assess excessive prices. None of the existing methods can be used in all circumstances since their suitability (and, at times, the very possibility of applying them) will depend on the specific features of each case. For example, a cost-price analysis would not be suitable in relation to the supply of certain intangible goods such as copyrighted musical works.

Given these limitations, Wahl proposed that competition authorities should examine cases "by combining several methods among those which are accepted by standard economic thinking and which appear suitable and available in the specific situation". Any convergence of results could be taken as an indicator of the possible benchmark price in a given case.

Wahl noted that the intrinsic economic value analysis is meant to identify those instances in which the unfairness of a price can be determined without the need to make any comparison with similar or competing products. This could be the case where, for example, legislation enables a dominant company to demand payment for services not requested or where excessive pricing is employed as a means to pursue a separate anti-competitive aim (eg, curbing parallel trade).

Checking whether the price imposed was unfair when compared to competing products can be a "sanity-check". Similarly, in principle a comparison with prices applied in other markets is

appropriate. However, Wahl stressed that not only do significant differences in price levels exist within the European Union, but the purchasing power of consumers may also vary across jurisdictions, underlining that using a purchase price index "can be a useful instrument to ensure that a comparison of the rates applied... in different countries is made on a homogenous basis".

While, in theory, any deviation from the benchmark competitive price may warrant intervention, this would "neither be realistic nor advisable". A price should be deemed excessive only when it is both "significantly and persistently above the benchmark price". This requires a case-specific analysis and an authority should intervene "only when it feels sure" that "almost no doubt remains" as to the abusive nature of pricing.

Wahl goes on to state that "it is only when no rational economic explanation – other than the mere capacity and willingness to use market power even when abusive – can be found for the high price applied by a dominant undertaking that that price may be qualified as abusive". Once an authority has "recorded an excess between the actual price and the benchmark price", it falls on the dominant undertaking to provide the authority with possible justifications for the (real or apparent) higher price. In the absence of clear guidance from the European Commission or the European courts on what constitutes an excessive price (and, conversely, a price that would not be considered excessive), this leaves dominant undertakings accused of charging excessive prices facing a Herculean task.

Wahl also made a number of quite sweeping statements in his opinion. For example, he stated that: "there is simply no need to apply [Article 102] in a free and competitive market: with no barriers to entry, high prices should normally attract new entrants. The market would accordingly self-correct." However, the situation may be different "in markets with legal barriers to entry or expansion and, in particular, in those in which there is a legal monopoly". In fact, Wahl goes as far as stating that "unfair prices under Article 102 [of the Treaty on the Functioning of the European Union] can only exist in regulated markets, where the public authorities exert some form of control over the forces of supply and, consequently, the scope for free and open competition is reduced". While potentially good news for dominant players outside of regulated markets, it is unlikely that the ECJ will endorse this line of thinking without reservation.

Wahl's opinion sets the bar for intervention at a high level. It remains to be seen to what extent the ECJ will embrace Wahl's approach when it rules on the questions from the Latvian Supreme Court.

Aspen

In May 2017 the European Commission opened an investigation into Aspen concerning pricing practices for niche off-patent cancer medicines containing five active pharmaceutical ingredients sold in different formulations and under multiple brand names. The investigation covers all of the European Union, with the exception of Italy.⁽¹⁾

In October 2016 the Italian Competition Authority fined Aspen more than €5 million for abusing its dominant position by increasing the prices of the same medicines from 250% to 1,500%. This appears to be a clear-cut case of abuse given the scale of the increase without any ostensible cost justification. But, in addition, Aspen was condemned for seeking to increase prices in Italy up to the levels in "the main European Union countries" in order to limit the parallel trade of the products out of Italy. The authority also alleged that Aspen threatened to withdraw the marketing authorisation of the products if AIFA (the Italian medicines agency) did not agree to the price increases. Threats of product withdrawal were viewed as an aggravating factor in the Italian case, and will almost certainly weigh equally heavily with the European Commission.

In addition to enforcement activity at EU level, there has also been a spate of enforcement activity at national level.⁽²⁾

Comment

Companies with strong market positions are understandably worried as to whether recent enforcement action at EU level (and at member state level) in relation to excessive pricing signals the start of a new enforcement trend. However, this is unlikely. To date, excessive pricing cases have been rare – the European Commission is wary of acting as price regulator and Vestager has urged the

need for caution in this area. This is not expected to change. However, further clarity in this area is needed, in particular on the question of when the difference between a price charged and the economic value of the product is so big as to be considered excessive, and hence abusive. While companies should not get their hopes up too much, there may be some further clarity on this question when the ECJ rules on the questions from the Latvian Supreme Court or as a result of the European Commission's investigation into Aspen.

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Endnotes

(1) Non-EU regulators are examining this case with interest, as seen in the recent South African investigation into Aspen, Pfizer and Roche in relation to alleged excessive pricing for certain cancer medicines which – for the first time – examines excessive pricing for an on-patent drug.

(2) In December 2016 the UK Competition and Markets Authority (CMA) fined Pfizer £84.2 million and Flynn Pharma £5.2 million after concluding that they had engaged in excessive pricing for phenytoin sodium capsules, an anti-epilepsy medicine, raising costs by as much as 2,600%. The CMA also ordered the companies to reduce their prices. Both companies have appealed the CMA's decision. In July 2017 the French Competition Authority announced the launch of a sector inquiry in the healthcare sector. The inquiry will cover all aspects of the French drugs market, but it looks like pricing by pharmaceutical companies active in France will be one of the focus areas of the inquiry.

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