

COMPETITION LAW AND POLICY IN SMALL STATES

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1. INTRODUCTION

Introduction

The paper attempts to show that there are many factors associated with a small domestic market that have a bearing on competition law and policy, and therefore competition regime of a small state should take these factors into account. Special reference is made to Malta, where competition legislation is modelled on EU competition law.

The thrust of the arguments put forward in this paper is not that competition rules should be discarded in small states or that abuse should be tolerated. The basic contention is that exceptions, normally based on considerations such as improved efficiency, distribution,

Characteristics of Small States

- **The meaning of small state** – population size often used to measure the size of countries.
- **Small Domestic Market** – limitations on competition possibilities, characterised by natural monopolies, barriers to entry, often there is parallel behaviour between firms due to family ties, difficulties with enforcement, high cost of public administration, high reliance on the export market.
- **Limited natural resources endowments** – high reliance on imports
- **Market failures and externalities**, so market forces do not always work.
- **High cost per capita** due to the problem of

Implications for Competition Law and Policy

The characteristics of small states just described have implications associated with competition law and policy, notably

- abuse of a dominant position;
- Agreements;
- State aid; and
- Mergers;
- Enforcement of the law.

2. ABUSE OF DOMINANCE

Abuse of a Dominant Position...1

Generally speaking, competition legislation does not take account of economic benefits when considering abuse of a dominant position, although dominance per se is not prohibited.

In competition regimes modelled on Article 102 of the Treaty on the Functioning of the European Union (TFEU) abuse arising from dominance, such as limiting production, applying dissimilar conditions, (including price discrimination to equivalent transactions), charging unfair prices and refusing to supply goods or services in order to eliminate a trading party from the relevant market, are generally prohibited, and once detected the undertakings responsible are sanctioned.

Abuse of a Dominant Position ...2

Dominance and discriminatory conditions

Due to the small size of the domestic market, oligopolies are common in small states. In some cases letting dominant oligopolies indulge in discriminatory practices may be to the advantage of the consumer.

In oligopolistic markets, discriminatory pricing may work against rigid oligopolistic price structures and could result in lowering prices to the benefit of the consumers. To forbid discrimination could reduce efficiency and slow reactions to changed market conduct.

Abuse of a Dominant Position ...3

Dominance and excessive pricing

Similarly, a seemingly excessive price, when compared to the price of similar products in larger countries, may be justified in a small economy, since this may be one way in which a firm could cover costs associated with importing the product, particularly in the case of islands where transport costs tend to be relatively high, or to cover the relatively high overhead expenses associated with importing or producing small quantities.

The issue of transport costs is very important in this regard. One implication relating to competition law is that a straightforward comparison with analogous goods in

Abuse of a Dominant Position ...4

Dominance and foreclosure of the market

In a small state the chances of destabilization effects of new entrants into its small domestic market is relatively high, when compared to a large state. In a small domestic market, a relatively large new entrant firm may find itself controlling a large share of the market, and this may seriously destabilize same market. If this same firm decides to exit at short notice, possibly leaving many business creditors at a disadvantage, the business environment would be further destabilized to the detriment of consumers. It is to be expected, in such circumstances, that existing firms may tend to forestall new entrants, not only because they fear that they will

Abuse of a Dominant Position ...5

Dominance and refusal to supply

Due to the constraints of replicating infrastructural facilities, there is more scope for the application of the essential facilities doctrine in small states. In a small state, a dominant firm may try to deny entry of new competitors into the market by refusing to share facilities. Competition law generally compels a dominant firm which owns a facility essential to other competitors, generally one that involves high overhead cost, to provide reasonable use of that facility. In a small state, where infrastructural facilities are costly and difficult to replicate, refusal to grant third party access to essential facilities owned and controlled by a dominant firm should be more

3. AGREEMENTS

Agreements ...1

Competition legislation modelled on Article 101 of the TFEU, relating to agreements between undertakings, often permit restrictions in this regard, if the agreement contributes towards the objective of improving production or distribution of goods or services or promoting technical or economic progress. This is the case in Maltese Competition law. In other words agreements containing what may appear to be anti-competitive may be exempt if, on balance, they have an overall positive impact on the consumers.

Agreements ...2

It may be argued that in a small state collaborative arrangements (horizontal as well as vertical ones) may have positive effects on the consumers, due to the advantages of business consolidation, given the very high incidence of micro-enterprise in such states.

This is subject to the so-called 'pass-on requirement,' meaning that consumers should ultimately get a fair share of the benefits, that the restrictions to competition are indispensable to achieve the benefits and that competition is not substantially curtailed as a result of the agreement. See European Commission (2010).

Agreements ...3

For example, within the EU, the Commission recognises that joint purchasing arrangements can often be pro-competitive because they allow smaller rivals to achieve similar purchasing economies to larger competitors, which can lead to enhanced competition, for example, in the form of lower prices and/or better quality products or services. In general, there are two main benefits that may be considered in permitting certain types of agreements between undertakings namely (a) substantial efficiency gains (e.g. through economies of scale and scope) that are passed on to the consumer, and (b) intensification of supply competition through a better bargaining position of the firms forming the agreement.

4. STATE AID

State Aid ...1

As is well known, in general state aid is considered as a competition distortion. However the EU makes several exceptions to this principle. Competition regimes based on EU General Block Exemption Regulation (GBER), permit public bodies in Europe to grant state aid for a broad range of activities for relatively high outlays without these being subject to prior European Commission scrutiny, in areas of research, development and innovation (RDI), regional urban development funds, culture and heritage conservation and infrastructures for broadband, energy and sports and recreational projects.

State Aid ...2

The GBER covers various categories of aid measures, including Regional aid, Aid for SMEs, Aid for environmental protection, aid research & development and innovation, aid for disadvantaged workers and for workers with disabilities, social aid for transport for residents of remote regions [the outermost regions plus Cyprus and Malta), Aid for sport and multifunctional recreational infrastructure. Generally speaking such aid must have an incentive effect and not be granted after a project starts.

State Aid ...3

In the case of small states, especially insular ones, the case of support of these types may be stronger than in larger territories, given the high degree of market failure in small economies and the social dimension of transport in the small states that are also islands. There may therefore be a case for considering state aid as permitting some form of level playing field in cases where the small size and insularity have an important bearing on the cost of production.

5. MERGERS

Mergers...1

Mergers regulations generally allow mergers that bring about or are likely to bring about gains in efficiency that will be greater than and will offset the effects of any prevention or lessening of competition resulting from or likely to result from the concentration, provided that the undertakings concerned prove that such efficiency gains cannot otherwise be attained, are verifiable and likely to be passed on to consumers in the form of lower prices, or greater innovation, choice or quality of products or services.

Mergers...2

The type of efficiencies that are more likely to be cognizable and substantial than others, are efficiencies resulting from shifting production among facilities formerly owned separately, which enable the undertakings concerned to reduce the marginal cost of production as these are more likely to be susceptible to verification, concentration-specific, and substantial, and are less likely to result from anti-competitive reductions in output.

Such justifications to anti-competitive behaviour are found in competition regimes in certain countries, such as the US, Canada and Australia, where the efficiencies defence is expressly mentioned in the law.

Mergers...3

One factor that should be considered when discussing mergers in small states relates to the notification thresholds, in that the turnover upper limit which applies to merging undertakings when they notify their merger. It makes sense that such a threshold is determined in relation to the size of the economy, as otherwise if set too high, all mergers will not need notification.

In a small economy, where market dominance and natural barriers to entry are common, and sometimes cannot be easily dismantled, efficiency clauses are likely to have major significance. In such cases, merger control that does not sufficiently acknowledge efficiencies may

Mergers...4

Another important issue in this regard relates to the benefits of networks. Such benefits acquire greater relevance in the case of sectors relating to communications and information technology.

In such sectors, concentration could enhance consumer welfare, as otherwise consumers would lose the benefit that a more extensive network could generate in such sectors, including wider choice of complementary products and enhanced quality and service that this brings about. In the transport sector, more integrated transport services can lead to network benefits that would improve service quality through strengthened hubs.

Mergers...6

The relevance of all this to small states is that the positive impact on the economy arising from mergers are likely to be more pronounced than in larger states, due to the fact that in a small market it may be desirable to avoid excessive fragmentation and encourage consolidation.

6. COMPETITION CULTURE & ENFORCEMENT

Competition Culture and Enforcement...1

In small states, the culture of competition may not easily take root due to the fear that intense competition may destabilise a small fragile and thin market.

Another reason is that, as already noted, government involvement in such states tends to loom large over the market, and public undertakings often clamour for exclusion from competition law provisions claiming that they have a social role to play.

In addition, the advantages of business consolidation and the disadvantages associated with business fragmentation often lead authorities of small states to

Competition Culture and Enforcement...2

Furthermore even where, in small states, competition legislation is in place, its enforcement may be more difficult than in larger countries due to the fact that everybody knows each other, and social and inter-family links predominate.

Thus, in small states, methods other than enforcement may sometimes bring better results as far as implementing competition policy is concerned. Competition advocacy among citizens, to render them aware of the benefits of competition policy are of relevance in this regard.

Competition Culture and Enforcement...3

The issue of enforcement vs advocacy is a very important consideration for small states. It is not being suggested here that advocacy and enforcement contradict each other or are mutually exclusive, as in many ways they are interdependent, principally because advocacy can favourably affect enforcement by fostering a competition culture, based on awareness that abuses of dominance and collusion are undesirable.

Difficult as it may be in a small state, enforcement will remain important as there are always vested interests that gain from weak legal control. The argument proposed here is that advocacy, aimed principally to

7. CONCLUSION

Competition Culture and Enforcement...3

This paper has highlighted a number of areas which are associated with small states and which are likely to have a bearing on competition law and policy. The main argument put forward in the paper is not that competition rules should be discarded, or that abuse should be tolerated in small states.

The basic contention is that exceptions, normally based on considerations such as improved efficiency, distribution, and overall consumer benefit, are more likely to be relevant in small states in certain circumstances.

End of Presentation

**THANK YOU
FOR YOUR ATTENTION**