CROSS – SUBSIDISATION IN TRANSPORT AND EC LEGISLATION

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1. Introduction

Cross – subsidisation is a difficult problem in transport in perspective of the Competition Law. Its difficulty is trifled: cross – subsidisation is not only difficult to define, but also difficult to identify and difficult to regulate. It is therefore convenient to approach this issue with prudence and modesty knowing that an "easy solution" of this problem is unlikely to appear. It is nevertheless essential to try harder as the "problem" of cross – subsidisation is real and serious one; a problem that might even jeopardise the chances of success of European liberalisation policy.

2. What is "cross – subsidisation"?

"Cross –subsidisation" means a kind of subsidisation when there is a transfer of resources within an undertaking (as opposed to external subsidies). In order to cross – subsidise an undertaking has to have monopoly power at least in one of the markets where it is active. Cross- –subsidisation is more likely (and more likely to define, to identify and to regulate) in situations where there are some common costs. It is often the case in the utility sector.

The definition (and the identification) of cross – subsidies is a difficult issue in itself. This problem is closely linked with the question whether all cross – subsidisation should be considered illegal or some forms of cross – subsidisation should be considered legal.

The traditional method of identifying "cross – subsidies" relies on cost allocation. "Cross – subsidy" is deemed to exit if the prices charged in competitive market do not cover the cost incurred in providing these services; these services are considered to be "subsidised" by services in monopoly markets where prices largely exceed their costs. Unfortunately, "common cost" is a typical feature of utility and one that terribly complicates the picture. In the presence of common costs the key question is how these costs attribute to the different activities. Different methodologies exist: fully – distributed cost, stand – alone cost, incremental cost. No clear consensus exits which methodology is the best.

Some economists support demand – based methods, in particular the so-called "Ramsey pricing", rather than cost –based methods. According to this opinion it would be optimal for the monopolist to charge higher prices to low –elasticity customers and low prices to high –elasticity customers. In this perspective the relevant element to identify cross- subsidisation would be demand, not cost. A cross –subsidy may exist between two identical services with identical costs and identical prices: these authors would consider that paying the same price the high –elasticity customer is "subsidising" the low –elasticity one.

The approach based on demand cannot be used to define cross-subsidies in the Competition Law perspective as it would lead to an absurd result. As every mullet product firm tends spontaneously towards Ramsey pricing (in order to maximize profits), cross- subsidies would only occur as a result of regulatory imposition. The underlying assumption is that a monopolist should have the freedom to charge "what the market can bear" without fearing antitrust intervention. This theory implies that (cost defined) cross –subsidies should in general be lawful.

3. Cross –subsidisation between monopoly and competitive markets

Particularly difficult kind of cross- subsidies may appear where an undertaking that benefits from a dominant position in one market is also active in competitive markets. In some cases the undertaking may cross-subsidise its monopoly activities with resources obtained in the competitive markets.

The problems arise with regard to cross- subsidisation from monopoly to competitive markets. A further distinction seems necessary whether the competitors in the competitive market have to obtain access to the monopoly segment controlled by the monopolist or not.

A "vertical" cross – subsidisation may occur in the context of access to an "essential facility". When the undertaking that controls an essential facility is also active in other competitive markets that are upstream or downstream, the monopoly power conferred by the control of the bottleneck may be exploited by charging directly to its competitors in those markets a high price for access. In that respect one could argue that the competitive activities of the vertically – integrated operator are also "cross- subsidised" by the monopoly activities. Competitors are in the same way exploited and excluded. However, this "vertical cross- subsidisation" raises very specific issues commonly discussed under the names "essential facility doctrine", "interconnection" and/ or "access pricing".

A "horizontal" cross subsidisation occurs in the absence of an "essential facility" element. This cross subsidisation occurs between two groups of customers and hurts competitors only indirectly. In horizontal cross –subsidisation customers in the monopoly markets are exploited to the benefit of customers in the competitive markets and to the detriment of competitors. Those are not directly exploited but they are excluded.

The scenario where "horizontal" cross- subsidisation might appear:

- An air carrier that benefits from exclusive rights in the domestic routes is also active and competing in international routes.

4. Transparency of cross – subsidies

Even if an agreement could be reached as regards the criteria of identifying cross- subsidisation and as regards its legal regime, another serious problem exists: that of its "transparency". It is obvious that in the absence of concrete and reliable information about prices and especially about cost, the best of the legal regimes would be useless. The requirement to keep transparent analytical accounts within an undertaking active both in monopoly and in competitive markets could also be established by a directive of the Commission based on Article 90.3 of the EC Treaty.

5. Legal regime of "cross – subsidisation" in transport

Cross- subsidisation may be treated under

National regulatory rules and under Community sectarian rules other than competition rules. The legal standards under these different legal regimes are not necessarily the same. Regulatory intervention may in some cases go further and impose stricter standards than Competition rules. Normally national regulatory intervention and sectarian Community rules coexist with Community competition rules. In most cases the former would act as a kind of "filter". Community competition rules would probably act as a kind of second resort for plaintiffs whose complaints are not satisfied by other regulatory regimes.

The legal regime of "cross – subsidisation " in EC Competition Law is unclear. On the one hand, there seems to be a consensus that in principle cross-subsidisation is a "bad thing" that should be prevented. On the other hand, it seems also clear that at least some forms of cross- subsidisation may be beneficial for the society and should therefore be allowed. Irrespective of the question of what the legal regime should be, nobody really knows what the legal regime actually is.

The ideal legal regime of cross – subsidisation should have this profile it should allow cross – subsidisation that is economically beneficial for the

Society and prohibit bad cross- subsidisation;

- It should be simple enough to provide legal certainty and to allow effective enforcement.

Both objectives cannot be totally achieved. An optimal legal regime from the point of view of economic efficiency would probably require sophisticated cost and/ or demand analysis that are not compatible with effective enforcement and with legal certainty. Compromise would be necessary.

Article 86 of the EC Treaty. Cross – subsidisation is by definition an unilateral practice. This means that in principe its regime under EC Antitrust law is defined by Article 86 of the EC Treaty which prohibits abuses of dominant position.

Cross- subsidisation requires by definition a dominant position in at least one market. In the utility sector the dominant position will often result from an exclusive right granted by the public Authorities. However dominant position and exclusive right are two different concepts. In some cases the scope of the exclusive rights would be much narrower than relevant market from an economic point of view. In these cases the protection from competition arising from this exclusive right might not be enough to create a "dominant position". Of course, a dominant position may also exist in the absence of exclusive rights.

The key question is to what extent can cross – subsidisation be considered as an "abuse" contrary to

Article 86. It is clear that some kinds of cross-subsidisation are normal business practices that may be necessary, for instance, in order to enter into a new market or in order to keep market shares. It also clear, however, that Competition rules may prevent a dominant firm from using certain strategies that are acceptable for non – dominant firms.

Cross-– subsidisation does not totally fit in any of the traditional categories of abuses. However, its profile suggests that it could more or less imply some kind of "excessive pricing" in the reserved market and/ or some kind of "perdition" in the competitive market. Cross- subsidisation could also be seen as a distinct kind of abuse.

"Excessive pricing" in captive market? A cross – subsidy may in some cases imply extra- normal profits being made in one sector that are used in order to subsidise the activities of another sector. In theory this could be contrary to Article 86, if the prices in the monopoly market are set at such a high level that they can be considered as "abusive".

However, in practice both the definition and the proof of the excessive character of the price under Article is a very difficult task. This price regulation is supposed to prevent the monopoly rent being appropriated by the monopolist. If price regulation of the monopoly activities worked properly, the problem of "cross – subsidisation" would be much more limited. In practice, however price regulation has only a limited impact on the control of monopoly profits.

Even if one assumes a correct functioning of price regulation for the monopoly activities, the presence of costs that are common to both the monopoly and the competitive activities create opportunities for cross-subsidisation.

In any event, the application of Article 86 of the EC Treaty against excessive prices in the monopoly market (and/ or the application of national price regulation against monopoly prices) is unlikely to solve the problem of cross- subsidisation.

Cross – subsidisation as a particular category of abuse? Some general statements may give the impression that "cross- subsidisation" is considered as an abuse in itself. However, Article 86 does not prevent a company, even a dominant one, from competing and from entering new markets. As some forms of "cross – subsidisation" may be indispensable to do so, it seems clear that not every form of cross- subsidisation would constitute an abuse. The mere transfer of resources in it (absent excessive or predatory prices) cannot be considered as an abuse contrary to Article 86.

"Predatory pricing" in the open market? The problem of cross – subsidisation is often considered as falling under the general category of "perdition". This is not necessarily very helpful as the "problem of perdition" is perhaps as intractable as the "problem of cross-subsidisation".

Perdition in EC Competition Law. The approach of European Competition Law as regards perdition is still mostly cost-based. The doctrine concerning perdition in EC Law was established by the Court of Justice "Kazoo".

Under the "Akzo" doctrine it would be contrary to Article 86 for an undertaking which is dominant in one market to use this market power in order to offer "predatory" prices in another market, even if the undertaking is not (or not yet) dominant in the second market. According to the "Akzo" doctrine prices are considered "predatory" and contrary to Article 86, if they are fixed at a level below average variable cost. However, prices that are fixed at a level below average total cost (but above average variable cost) are only contrary to Article 86, if one can prove an anti-competition intention. Prices above average total cost are presumed legal.

Cross – *subsidisation as a "predatory" practice* The main reason that makes "have cross – subsidisation " an almost intractable problem for competition law is the presence of common costs. The fact of having common costs to various lines of production implies that the determination of the total cost of these products is to some extent arbitrary and in any case difficult. Common costs may be either fixed or variable, but in the utility sector they tend to mainly fixed costs (infrastructures, etc.) For the sake of simplicity the variable cost is not more difficult to calculate for the utility sector than for any other industry. Fixed costs, however, would normally include common cost which allocation is problematic and to some extent arbitrary. This means that one of the main elements necessary to determine whether a price is predatory ("average total cost") is very hard to determine in situations of cross – subsidisation.

Prices in the competitive market are below average variable cost. One could in theory apply Article 86 against "predatory pricing" practices falling within the first category: prices below average variable cost. It seems clear that prices below average variable cost are in general unjustified and they can be presumed to be anti- competitive.

This may be agreed even by the supporters of demand – based (Ramsey) pricing, as a price below marginal costs is irrational for a firm, unless anticompetitive. A ban of these prices seems therefore fully justified.

To sum up, "cross – subsidisation" by a dominant operator in an utility market will be contrary to Article 86 of the EC Treaty, if it can be shown that the prices in the competitive market (where this operator is not necessarily dominant) are below their average variable cost.

Prices in the competitive market are above average variable cost. The trouble is that most of the alleged "cross- subsidisation" cases in the network industries show prices above average variable cost. We can not therefore rely on the clear standard applying to prices below that level. We have to face two cumulative difficulties:

a) The difficulty of determining the legal status of prices that are at a level between average variable cost and average total cost and

b) The difficulty of determining what is average total cost in the presence of common costs.

According to "Akzo" the rule concerning prices that are above average variable cost but below average total cost is to consider these prices lawful unless an anticompetitive intention can be proved. Prices above average total cost are generally considered lawful. As regards prices between average variable cost and average total cost, it is inappropriate to rely on an intention in order to determine whether a price is predatory or not. Firstly, the delimitation between an intention to compete vigorously and an intention to eliminate a competitor is far from easy. On the other hand, the end of any rule concerning perdition should be to prohibit the prices that have or may have anti-competitive effect rather than to punish the "bad intention".

Prices above average variable cost are not always anti-competitive. They would became anti- competitive only, if they may hurt an efficient competitor to the extent he it is obliged to leave market, to renounce to entry or to reduce the intensity of its competition.

The point of departure should rather be to determine whether an efficient competitor is being hurt as a result of the pricing strategy of the incumbent. The plaintiff should have the burden of the proof of the three following elements:

- that he can be considered an "efficient" operator;
- that the monopolist beats his prices and
- that he incurs in losses as a result of the monopolist pricing strategy.

In these circumstances the pricing strategy of the dominant firm would eliminate or neutralize an efficient competitor and would therefore be anti- competitive. The only exception is when the monopolist can prove to be "more efficient" than the competitor, i.e., when the low level of his prices can be justified on cost-efficiency grounds.

Proposed rule. Cross subsidisation in a utility industry should be considered predatory and contrary to Article 86 of the EC Treaty in the following circumstances:

1. An undertaking (the monopolist) enjoys exclusive rights in a given market (the monopoly market) and is at the same time active in a competitive market.

2. A competitor can prove

a) either that the monopolist prices are below its average variable cost.

b) or alternatively, the three following elements:

That he is an "efficient" operator in the competitive market;

That the monopolist prices in the competitive market are equal or lower than his prices; That he is suffering persistent losses as a result of the monopolist pricing strategy.

The monopolist can not prove

a) either that his prices are above an ideal

"stand-alone" cost (this is equivalent to rebating the proof that the competitor is "efficient")

b) or, that his prices are above its "average total

costs" as resulting from the objective cost –allocation criteria that he has chosen.

Article 92 of the Treaty. *A cross – subsidisation implies a transfer of resources within the undertaking from one activity to another. This transfer may be more or less easy to identify. If the costs of the different activities are separated, it is easy to prove that the losses in one activity are compensated by the profits in the other activity. In other cases the transfer may be disguised by an inappropriate allocation of common costs.*

Article 90.2 of the EC Treaty. Article 90.2 of EC Treaty contains an exception for "public service" reasons that can be invoked to Exempt State measures and/or behaviours by undertakings. In principle, this exemption could be applied as regards the prohibitions contained in Article 86 and/or 92 of the EC Treaty.

In most cases Article 90.2 would not at all be applied to cross- subsidisation such as those examined here. In fact, normally the competitive activity that receives the transfer of resources is not an activity of "general

economic interest" (contrary to the activity that originates the resources which is normally an activity of "general economic interest").

There are, however, activities of "general economic interest" that are not monopolistic but subject to competition. The question is whether a transfer of resources from the monopoly sector to a sector which is competitive but also of "general economic interest" could be justified under Article 90.2 of the EC Treaty. This possibility cannot be excluded, if different conditions of this provision are fulfilled.

Even if Articles 86,90.1+86 and /or 92 prohibit the cross-subsidy, one has to consider whether Article 90.2 can be applied to justify the cross- subsidy. In fact, if one admits that the competitive services are correctly considered as "universal services", it might be better to have an open market with very low prices than to protect totally these activities from competition.

In general, however, cross – subsidies target sectors are both non- – reserved and non- –universal services. In these cases Article 90.2 cannot be applied.

6. Conclusions

Cross – subsidisation from the monopoly to the competitive activities within one undertaking is a complex phenomenon. In theory different competition rules such as Articles 86 and 92 can be applied at the same time.

Cross- – subsidisation in a utility should be considered predatory and contrary to Article 86 of the Treaty in the following circumstances:

1. An undertaking (the monopolist) enjoys exclusive rights in a given market (the monopoly market) and is at the same time active in a competitive market.

2. A competitor can prove

a) Either that the monopolist prices are below its average variable cost.

b) Or, alternatively, the three following elements:

- That he is an "efficient" transport operator in the competitive market,

- That the monopolist prices in the competitive market are equal or lower than prices and

- That he is suffering persistent losses as a result of the monopolist pricing strategy.

1. The monopolist can prove

a) either that his prices are above an ideal "stand – alone cost" (this is equivalent to rebating the proof that the competitor is "efficient");

b) or, that his prices are above its "average total costs" as resulting from the objective cost –allocation criteria that he has chosen.

The same can be said about Articles 90.1 and 86 to the extent that cross –subsidies are imposed or encouraged by the Government.

Transfers of resources from a monopoly activity to a competitive activity within one public undertaking may under certain conditions be considered in the meaning of Article 92. An examination under Article 92 would therefore have to be done in most cross- subsidy cases. However, the utility of Article 92 as an instrument to deal with cross –subsidies would, to a large extent, depend of the interpretation of the "market investor principle" in this area. It is submitted in that respect that the appropriate question is whether a private investor – without a captive market to which to allocate all the common costs – would be prepared to finance the same losses. A different interpretation might deprive Article 92 of the most of transport utility as an instrument to deal with cross –subsidisation.

Article 92 may probably be applied to cross – subsidisation within private-owned (or privatised) undertakings benefiting from exclusive rights. This results from Article 90.1. If the application of Article 92 to private –owned (or privatised) undertakings benefiting from exclusive right is rejected, Article 86 would be the only available instrument.

The exception of Article 90.2 would normally not play role in cross –subsidies cases. The only possible exception might be the cases where the competitive activity is at the same time a "service of general economic interest".

Literature

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KRYŽMINIS SUBSIDIJAVIMAS TRANSPORTE IR EB TEISĖS AKTAI

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S a n t r a u k a

Aiškinama kryžminio subsidijavimo sąvoka transporte, kuri Lietuvoje kol kas nėra labai paplitusi. Lietuvai tapus ES nare ji plačiai bus vartojama ir geriau suvokiama. Kryžminis subsidijavimas yra labai svarbi sąvoka, kuri apima dau-

gybę įvairių situacijų. Ypač tai būdinga vienai itin svarbiai kryžminio subsidijavimo formai, kuri atliekama vienoje įmonėje, kai pelnas iš veiklos pagal teisinį monopolį subsidijų forma perkeliamas į kitą veiklą, kur nėra monopolio. Kryžminis subsidijavimas reiškia, kad pelnas, gautas iš monopolinio sektoriaus, vienu ar kitu būdu yra perkeliamas į nepelningą sektorių. Šitas pelnas gali būti arba nebūti „perteklinis“. Pelno perkėlimas konkurencinėje veikloje tada taikomas siūlant paslaugas, kurių kaina žemesnė nei išlaidos.

Teisiniu požiūriu tai gali būti suprantama:

- kaip „perteklinės“ kainos monopolinėje rinkoje;
- kaip „grobuoniškos“ kainos konkurencinėje rinkoje;
- kaip pelno perkėlimas iš monopolinės į konkurencinę rinką.

Kiekvienas požiūris gali būti svarstomas pagal atskirus Sutarties straipsnius (86, 90, 92 ir 93 straipsniai).

Kryžminis subsidijavimas suprantamas kaip viršpelnis, kuris gaunamas viename sektoriuje ir yra panaudojamas subsidijuoti veiklą kitame sektoriuje. Teoriškai tai gali prieštarauti 86 straipsniui (arba 90.1+86 straipsniams, jeigu tarifai yra reguliuojami vyriausybės), jeigu kainos yra nustatytos tokio aukšto lygio, jog gali būti suvokiamos kaip piktnaudžiavimas.

Pagal „Akzo“ doktriną, kuri prieštarauja 86 straipsniui dėl įmonių, kurios dominuoja vienoje rinkoje, reikia naudoti tą rinkos jėgą tam, kad būtų pasiūlytos „grobuoniškos“ kainos kitoje rinkoje, netgi jeigu įmonė dar nedominuoja toje rinkoje.

Pagal „Akzo“ doktriną kainos suprantamos kaip „grobuoniškos“ ir prieštaraujančios 86 straipsniui, jeigu jos yra žemesnio nei ribinės išlaidos lygio. Tačiau kainos, žemesnės už bendrų išlaidų vidurkį (bet aukštesnės nei ribinės išlaidos), tik tuomet prieštarauja 86 straipsniui, jeigu galima įrodyti antikonkurencinius tikslus.Todėl, kaip teigia analitinė išlaidų skaičiavimo sistema ir egzistuojantis teisingas išlaidų paskirstymas, 86 straipsnis (arba 90.1+86 straipsniai, jeigu kainos yra reguliuojamos vyriausybės), jos gali būti lengvai taikomos prieš „grobuoniškas“ kainas ir taikomos analitinėje išlaidų skaičiavimo sistemoje. „Akzo“ doktrina buvo sukurta Justicijų teismo turint omeny labai skirtingą išlaidų struktūrą. Kainos, aukštesnės nei ribinės išlaidos, bet žemesnės už vidutines bendrąsias išlaidas, yra suvokiamos kaip piktnaudžiavimas, kol jas nustatome pagal veiklos pobūdį. Nuostoliai, kuriuos bet kokia įmonė patirs įeidama į naują rinką, bus svarstomi kaip suderinami su 86 straipsniu teigiant, jog yra aiški perspektyva, kad veikla taps pelninga per vidutinį laikotarpį.

Tačiau, kai taikoma „Akzo“ doktrina, teisinga yra įvertinti, kad dauguma „per žemų kainų“ konkurencinėje veikloje neprieštaraus 86 straipsniui.

86 straipsnis neapsaugo kompanijos, netgi dominuojančios, nuo naujų firmų įėjimo į rinką. Tačiau aišku, kad įmonė, turinti išimtinę teisę vežti keleivius ir dirbanti stiprios konkurencijos sąlygomis, negali taikyti kelių konkurencinių strategijų, kurios yra teisėtos nedominuojančioms firmoms.

Klausimas, kas išplės 86 straipsnio prevenciją dominuojančiai firmai, vykdančiai agresyvią kainų politiką, išreikštą kryžminiu subsidijavimu?

Tai padaryti galima vadovaujantis „dominuojančios pozicijos išplėtimo teorija“. Pagal šią teoriją, įmonė, kuri yra dominuojanti vienoje rinkoje, negali grubiai nepažeisdama 86 straipsnio užimti dominuojančią poziciją gretimoje, bet skirtingoje rinkoje. Tai gali būti ribojanti situacija, kai normalus investitorius (be laisvosios rinkos, kuri paskirsto visas fiksuotas išlaidas) neinvestuoja tam tikros sumos per tokį pat laikotarpį įeidamas į naują rinką.

„Išplėstos teorijos“ taikymas kryžminiam subsidijavimui reikš, kad kai kurių išteklių perkėlimas gali prieštarauti 86 ir 90.1 straipsniams netgi, jeigu „perteklinės“ arba „grobuoniškos“ kainos griežtai ribojamos.

Sąvoka „valstybės pagalba“ pagal 92 ir 93 straipsnius normaliai liečia valstybės išteklių perkėlimą įmonei nekomerciniu požiūriu. Šie ištekliai gali būti gaunami tiesiogiai iš valstybės, kaip valstybės subsidijos arba netiesiogiai per valstybės kontroliuojamą įmonę. Naujas Justicijų teismo įstatymas aiškiai parodo, kad išteklių perkėlimas valstybinės įmonės viduje iš vienos monopolinės veiklos į konkurencines veiklas gali būti suvokiamas kaip valstybės pagalba.

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