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New Guidelines from the Israeli Competition Authority Concerning the Analysis of Significant Market Power

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On January 2019, the Economic Competition Law (formerly the Restrictive Trade Practices Law) was amended, broadening the definition of the term "monopoly": According to the amendment, in addition to an entity whose market share exceeds 50%, an entity holding significant market power with respect to the supply or purchase of certain assets or services, will also be considered a monopoly, even if its market share is less than 50%.

On July 21, 2019, the Israeli Competition Authority (the "**ICA**") published guidelines aimed at clarifying to the public the ICA's interpretation of the term "significant market power" (the "**Guidelines**").

The publication of the Guidelines paves the way for the Competition Authority to begin enforcing the provisions in the Competition Law applying to monopolies, in the context of companies with a market share of less than 50%, as long as the ICA is able to prove that such companies have significant market power according to the characteristics set out in the Guidelines.

It is important to emphasize that a monopolistic position, including one deriving from market power, is not prohibited in itself and does not constitute a violation of the law. However, a monopolist is subject to strict duties of fairness and proper conduct. Therefore, entities that may have market power should be aware of this and act accordingly, taking into consideration the restrictions set forth in the Economic Competition Law with regard to monopolies (such as the prohibition of improper discrimination among customers, the prohibition of unfair pricing, the prohibition of unreasonable refusal to supply goods or services, etc.).

According to the Guidelines, significant market power is the ability and economic profitability to determine significantly inferior conditions of supply (or purchase) for a given product compared to those that would have existed in a competitive market, in a non-temporary manner, for all customers or for a certain group of customers. Market power can be activated in relation to different supply conditions: price, quantity, quality, variety, availability and more. According to the Guidelines, in order to determine the existence of significant market power, it is necessary to examine whether it is possible to operate in a manner that is free of competitive restraints of two types: demand-side restraint and supply-side restraint.

<u>Demand-Side Restraint</u>

As a rule, an entity holds significant market power insofar as it does not have a competitive restraint on the demand side, i.e., as long as its customers continue to purchase the product even if it determines supply conditions that are inferior to the competitive conditions.

The larger the **market share** of the entity being examined, the more it will serve as an indication of the existence of significant market power. In this context, the gap between the market share of the entity in question and the market shares of the other players in the market will also be examined. In general, it is rare for an entity with a low market share to hold significant market power. However, the ICA refused to offer a safe harbor or set a minimum market share requirement under which it will not claim that a firm might have market power.

Additional characteristics that are examined on the demand side and can provide an indication of the existence of significant market power are:

- The existence of a **strong brand**, which, from the consumers' point of view has a unique demand, while similar products that are not of the same brand are not considered a substitute by the consumers. The similarity of each branded product to all the products that may be a substitutes from the consumers' point of view should be examined, as well as the extent to which these products limit the branded product.
- The existence of **transition or switching barriers** between different suppliers, in a manner creating significant market power for the suppliers, even if each of them supplies products or services to a relatively low percentage of customers.

<u>Supply-Side Restraint</u>

In this context, the ICA will examine the question of how other suppliers in the market will react to a price increase / output decrease or other worsening of conditions on the part of the company with the apparent market power. In cases in which a reaction by other suppliers is **likely, timely and sufficient** – that is, a reaction is worthwhile from the perspective of the other suppliers, is expected to occur within an immediate time range and at a sufficiently rapid pace to create deterrence and to an extent enabling acceptance of customers at a scope that is sufficiently large – it can be stated that there is a competitive restraint that prevents the use of market power.

Where there are high barriers to entry and expansion, for example, economies of scale or scope, production capacity constraints, regulatory regime making it difficult to operate, etc., these will be an indication of lack of supply-side restraint and thus will support the conclusion that market power exists.

Additional Indicators of Market Power

The Guidelines also mention a number of specific situations in which market-specific characteristics may indicate the presence of significant market power. One such case relates to the field of "**social networks**" in which the **network effect**, i.e., the fact that the benefit the participants derive from the network increases when the number of members in the network increases – constitutes an entry barrier limiting restraint by new and small players. Additional cases that may create market power are **aftermarkets** in which the supplier of an initial product has market power towards the purchaser of the product, in the purchase of follow-on products such as spare parts, consumables required to operate the initial product or services regarding the initial product. The existence of market power in an aftermarket also depends on the level of competition in the primary market. In markets where there is **vertical integration**, that is, the activity of the entity in question is carried out in two adjacent markets (such as an input and a final product) – the vertically integrated entity might have market power. In such cases, an entity wishing to compete may be required to compete simultaneously in both upstream and downstream markets, including coping with the costs involved and any entry barriers, and therefore might not be able to restrain the market power of the existing integrated firm.

Finally, the Guidelines also refer to the existence of **collective market power**, stemming from coordinated activity of several players, which consistently refrain from offering competitive offers to customers, but without explicit or implied coordination. In the absence of other significant competitive restraints, market players can worsen the supply conditions of customers without fear of competitive restraint, and therefore each is considered to have significant market power. In this context, it is important to note that the foregoing constitutes grounds for intervention and enforcement by the ICA in oligopolistic markets, which may also lead to private enforcement in this respect.

To read the Guidelines (in Hebrew),
click here

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