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ECONOMIC ANALYSIS AND EVIDENCE IN ABUSE CASES – Contribution from Ukraine

- Session II -

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More documentation related to this discussion can be found at: oe.cd/eac.

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Economic analysis and evidence in abuse cases

- Contribution from Ukraine –

1. The Law of Ukraine “On Protection of Economic Competition”¹ (hereinafter - the Law) stipulates that the abuse of a monopoly (dominant) position in the market is the actions or inactivity of an economic entity occupying a monopoly (dominant) position on the market that resulted or can result in the prevention, elimination or restriction of competition, in particular the restriction of the competitiveness of other economic entities, or in the infringement of the interests of other economic entities or consumers, which would be impossible in case of the existence of substantial competition on the market. In particular, the Law also provides seven examples of such actions and types of behavior. Five of these are inherently exploitative behaviors that directly harm the interests of trading partners and consumers, and the last two examples relate to behaviors that affect the structure of markets by reducing existing competition:

1. Unfair prices and contractual terms;
2. Discriminatory prices and conditions (terms);
3. Tying of goods (the conclusion of agreements with additional obligations that have nothing in common with the subject of the contract);
4. Limitation of production, markets or technical development;
5. Partial or complete refusal to purchase or sell a product if there are no alternative sources of sale or purchase;
6. Substantial restriction of the competitiveness of other economic entities;
7. Creation of entry (exit) market barriers or the removal of sellers, buyers, other economic entities from the market.

2. Most frequently in its practice the Antimonopoly Committee of Ukraine (hereinafter – the AMCU) faces the following theories of harm: exploitative abuse, exclusive dealing, refusal to deal. In 2019, as a result of decision-making or provision of recommendations, bodies of the AMCU ceased 268 violations and actions that contain signs of violation in the form of abuse of monopoly (dominant) position, as well as 227 violations in 2020. In 2019, 46% of ceased violations were in the form of unfair pricing or contractual terms setting, and 57% of such violations were also ceased in 2020.

3. In investigations related to the abuse of monopoly (dominant) position, the AMCU is guided by the Methodology on definition of the monopoly (dominant) position of economic entities in the market as of 05.03.2002 № 49-r (hereinafter - the Methodology). In general, the analytical process for determining whether an economic entity occupies a monopoly (dominant) position and measuring market power is as follows:

¹ [Law of Ukraine “On Protection of Economic Competition”](#)

1. *“Analysis of signs related to possible abuse of monopoly (dominant) position”*

The AMCU may initiate research on its own initiative or on the basis of applications received from economic entities, consumers or submissions from public authorities.

2. *“Market definition which is defined through evaluation of the product and geographic dimensions and temporality”*

In determining the market, the AMCU can assess the demand-and-supply-side substitutability, the impact of price change on the interchangeability of goods (SSNIP-test), analyze the stages of products’ life cycle and the degree of import penetration, as well as the impact of anti-dumping measures or other trade restrictions, therefore economists are already involved at this stage.

3. *“Evaluation of market shares and degree of market concentration”*

At this stage, the calculation and comparison of the shares of major economic entities, the assessment of the stability of the market shares, the possible calculation of the Herfindahl-Hirschman Index (HHI) or concentration ratios (CR3-CR5) takes place. An analysis of the spare capacities of an economic entity which determines the existence of a monopoly (dominant) position and other market participants may also be performed. An economic entity with a high market share and reserve of spare capacities has a significant advantage over competitors who make full use of their capacities. On the contrary, the capacity reserves of competitors with smaller market shares may constrain the non-market behavior of the economic entity which is the market leader.

The analysis of market power takes into account the stage of market development. In dynamic markets, actual market shares do not necessarily reflect the level of market power. Innovation can quickly change the situation and balance of power in a market, especially when an economic entity has exclusive access to advanced technologies. If the market is stagnant or in recession, where new entrants are unlikely to emerge, the economic entity’s large market share is an important preliminary indication of its significant market power.

4. *“Analysis of barriers to entry into the market”*

The economists can analyze structural barriers, for example: the impact of factors such as fixed costs and economies of scale on the ability of new entrants to set prices at a competitive level, to conduct price-cost analysis, to measure profitability on the market.

5. *“Comparison of market participants and definition of signs of the market power”*

The assessment of the level of market power is carried out by comparing the economic entity in respect of which the existence of a monopoly (dominant) position and other market participants is defined, to determine whether the economic entity is subject to significant competition or not.

4. Basing on the above-mentioned analysis, if the monopoly (dominant) position of the economic entity is defined, the abuse of market power by that entity is investigated. In particular, in the framework of the investigation economists are involved in:

- Determination of a competitive price that might exist in a highly competitive environment, as well as an analysis of “predatory” pricing by the dominant firm;
- Conduction of cost-benefit analysis;

- Evaluation of the discriminatory effect of applying different prices or different acquisition conditions to an equivalent good;
- Analysis of the nature of the discounts granted, whether or not they are economically justified, or just intended only to discourage customers from purchasing the relevant goods from other suppliers;
- Evaluation of the damage to economic entities or consumers from exploitative actions such as limitation of production or technological development;
- Analysis of the exclusive contract conditions in terms of economic pressure or financial incentives, which lead trading partners or consumers to refuse from dealing with third parties, in particular actual or potential competitors of the dominant firm etc.

1. Case study (Decision of the AMCU as of September 05, 2019, No. 598-r²).

5. Based on the results of a study of the state of competition in the mineral nitrogen fertilizers market, the following barriers to competition were defined:

- *for producers and wholesalers*: economic constraints associated with the need to organize the industrial production of fertilizers and to build the appropriate infrastructure, which requires significant investment and time.
- *for wholesalers and retailers*: lack of sufficient working capital that would allow to carry out economic activities in the planned amount (to buy, to store, to transport products) and to maintain their own solvency during the periods of seasonal price lowering.
- *for the importers*: anti-dumping measures imposed on imports of ammonium nitrate, urea and urea-ammonium mixture originating in the Russian Federation were introduced during 2014-2017.

6. The regional features of the market for the sale of mineral nitrogen fertilizers were also studied:

- An economic entity - the supplier to a large extent purchased fertilizers not directly from producers, but from wholesale suppliers at the national and interregional levels. At the same time, the majority of fertilizers were also purchased by agricultural producers from wholesale suppliers at the national and interregional levels.
- The volume of purchases of mineral nitrogen fertilizers depended on the receipt of orders. Such orders are formed on the basis of needs, analysis of sown areas and technological maps of sowing, which, in particular, contain information on the rate of fertilizer application.
- The main factor influencing the level of sales prices of fertilizers by regional suppliers and their dynamics was the level of purchase prices of fertilizers from wholesale suppliers at the national and interregional level.

² [Decision of the AMCU as of September 05, 2019, No. 598-r \(In Ukrainian\).](#)

7. According to the results of collection and analysis of case materials, it is established that the Ostchem Group held a dominant position in this market with a following share: 61.01% in 2014, 52.40% in 2015, 55.56% in 2016, 35.45% in 2017. The decrease in the share of the Ostchem Group in 2017 is resulting from the unauthorized shutdown of plants for the period of spring field works (from March to June).

8. In the course of consideration of the case the modeling of the cost of mineral nitrogen fertilizers without intragroup manipulations was carried out. The actual price of fertilizers exceeded the simulated one by 13-60% in different periods. In less than six months, the relevant manipulations led to an overestimation of the cost of ammonium nitrate by \$ 30 million. Measurement of the level of profitability in the market and analysis of behavior showed that the Ostchem Group's policy is to maintain the loss of plants and make a profit at those plants of the Ostchem Group that sell mineral nitrogen fertilizers outside the Ostchem Group and change over time.

9. Having a dominant position in the market of mineral nitrogen fertilizers, the Ostchem Group abused its position and committed violations that are prohibited and consisted of the following:

- During 2014-2015, by manipulating the purchase prices of natural gas for fertilizer production by reselling natural gas at inflated prices within the Ostchem Group, thereby artificially inflating the cost, it set prices for the sale of nitrogen fertilizers on the market that would be impossible if significant competition existed in the market (violation of Part 1 of Article 13 of the Law of Ukraine "On Protection of Economic Competition").
- In March 2017, having an advanced payment for fertilizers received by the Group through NF Trading Ukraine LLC from 170 economic entities on the basis of concluded sales agreements, all plants of the Ostchem Group almost simultaneously stopped production of nitrogen fertilizers during the spring season field works and for 4 months did not take any measures to resume gas supply and to resume production, thereby limiting the production of fertilizers that caused (or could cause) harm to other economic entities - buyers (violation of Clause 4 of Part 2 of Article 13 of the Law Of Ukraine "On protection of economic competition").

10. The decision of the AMCU provides for the imposition of a fine on a profitable member of the Ostchem Group and the implementation of the compulsory split-up of plants. At the moment the decision is in the process of judicial appeal.