

Unclassified

DAF/COMP/WD(2016)65

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

24-Nov-2016

English - Or. English

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

Cancels & replaces the same document of 15 November 2016

ROUNDTABLE ON "PRICE DISCRIMINATION"

--Note by Israel--

29-30 November 2016

This document reproduces a written contribution from Israel submitted for Item 7 of the 126th OECD Competition committee on 29-30 November 2016.

*More documents related to this discussion can be found at
www.oecd.org/daf/competition/price-discrimination.htm*

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JT03406168

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ISRAEL

1. In this written contribution we will focus on describing two different cases dealt with by the Israel Antitrust Authority (hereinafter: "**the IAA**"), both of which involve discounts given to certain customers which had an adverse effect on competition. These cases will demonstrate ways in which price discrimination can harm competition and solutions used by the IAA to solve those issues.

2. In the first case that will be discussed, the Director General reached an agreed structural remedy designed to prevent an adverse competitive effect of a discount policy applied by Neshet, a cement monopoly.¹ While the structural remedy does not address the discounts directly, it was intended to reach a better competitive structure that would have a positive influence on competition in both the cement and the concrete markets and hopefully improve the weak competitive situation.

3. The IAA reached an agreement with Neshet, according to which as a condition for the IAA not imposing a prohibition on the mentioned discounts, Neshet would divest its Har-Tuv cement plant (one of three) to a new competitor, thereby increasing the number of manufacturers in the Israeli cement market from one to two.

4. In the second case that will be discussed, the IAA published a draft of recommendations for amending the existing sectoral regulations in order to improve competition in the market for Liquefied Petroleum Gas (LPG) supplied to private households with a central gas system ('Tank'). Among the issues addressed in the draft, the IAA addresses the special prices offered by LPG suppliers to certain customers in order to reduce their incentive to gather their neighbours or get together and switch to a competing supplier.²

5. Both cases discussed in this paper illustrate the ongoing challenge in addressing price discrimination behaviours. The IAA focuses its efforts and resources in treatment of such behaviours which have an adverse effect on competition.

1. The cement monopoly discount case

1.1 Background

6. Neshet was designated by the IAA as a monopoly, being the only cement manufacturer in Israel.³ The alternative of import of cement to Israel has significant disadvantages,⁴ relies on a single importer and

¹ Instructions to a Monopoly: Neshet Israeli Concrete Factories Ltd., (30.10.2014) **Antitrust** 500696.

² The IAA recommendations regarding the supply of LPG to households using central gas systems (Draft published for public hearing), (2.8.2016) **Antitrust** 501022.

³ A monopoly declaration: Neshet Israeli Concrete Factories Ltd., (25.12.1988) Antitrust 390 (according to the Restrictive Trade Practices Law, 5748-1988 (hereinafter "**the Antitrust Law**"), the Director General can declare and publish the existence of a monopoly. A monopoly is defined as a person or company concentrates the supply or purchase of exceeding 50% of the goods or services in their market.").

is limited in the quantities it is able to supply;⁵ as such it is not an effective alternative. Because of the size of the local market and certain technical barriers, the probability of establishing an additional local cement competitor was also very low. The result was that competition in the cement market hardly existed. Due to these circumstances, Neshet's cement prices are regulated by a sectoral regulator. The price regulation sets a list of maximum prices per ton but permits providing reductions to customers purchasing large amounts (discounts at different levels to those who purchase over 100, 1000, 4000 or 10,000 tons).

7. Cement amounts to 50% of the cost of concrete. The leading concrete manufacturers are Ready-mix and Henson, each of which is held by a big international cement firm, Heidelberg Cement and Cemex (respectively). Other concrete suppliers are significantly smaller. The IAA found that Neshet was concerned about the possibility that Ready-mix or Henson might invest efforts in finding alternatives to purchasing from Neshet, *e.g.*, through purchasing from importers or developing a capability to import cement themselves.

8. The way Neshet had dealt with this threat was by providing the largest concrete manufacturers, particularly Ready-mix and Henson, with especially low prices (significantly lower than the regulated prices) and favourable credit terms. These prices and terms were presented and justified as objective quantity rebates as they were given to the largest purchasers according to the price level fixed for purchasers of such quantity; however the IAA found that they were aimed at Ready-mix and Henson (which were the only companies at the highest price reduction levels) having an effect of diminishing the incentive to purchase from alternative suppliers. Although Ready-mix and Henson were truly the largest cement purchasers from Neshet the IAA found that the quantities purchased by them did not justify the reductions in terms of saving on Neshet's production costs. Nevertheless, those reductions significantly reduced Ready-mix and Henson's motivation to try to import cement and thus diminished the possibility of developing a competing alternative to Neshet's cement.

9. The concrete market suffers from competition difficulties as well. Both Ready-mix and Henson affirmed that their large savings due to their special purchase prices stayed in their own pockets and were not transferred to their clients. This means they prefer keeping the difference to themselves rather than increasing their market share by offering competitive prices. The result was that the prices in the concrete market were well above competitive prices, as the two market leaders did not offer competitive prices and the smaller suppliers lacked the ability to compete, as they were not eligible for substantial discounts, if any, and purchased the cement at a significantly higher price.

10. The outcome of the provided discounts was that competition was harmed by diminishing the incentive to develop an import alternative in the cement market and also by limiting the possibility of price competition in the concrete market.

1.2 Legal background: Instructions according to article 30 to the Antitrust Law

11. Article 30 to the Antitrust Law allows the Director General to instruct monopolies as follows:

1. If the Director General believes that business competition or the public is being harmed as a result of the existence of a monopoly or the behaviour of a monopolist, he or she may give the monopolist instructions regarding the measures that it must take to prevent such harm.

⁴ As the concrete producers are extremely sensitive to the timing and continuity of their cement supply, the imported cement, for which continuity of supply and price are less stable, isn't an equal alternative.

⁵ At most, a little over 10 percent of the cement supply in Israel.

2. If the Director General believes that there is a risk of substantial harm to competition or to the public as a result of the behaviour of a monopolist, he or she may give the monopolist instructions regarding the measures it must take to prevent such harm.

12. These powers provided by the law are not limited to a fixed list of behaviours, nor do they focus only on behaviours which are a violation of the Antitrust Law. In any case where the Director General finds that the existence or behaviour of a monopoly may result in harm (or possibility of substantial harm) to competition, he or she may design the instructions appropriate for preventing that harm.

1.3 The IAA's decision

13. As the Director General found that the competitive situation met the conditions of article 30 both in the cement and the concrete markets, he decided to instruct Neshet to change its pricing policy. After discussions with Neshet, the Director General agreed with Neshet on instructions under which Neshet would divest one of its plants and transfer all of its production capacity to a purchaser which is not, and is not related to, a concrete manufacturer or a cement importer – a solution which would lead to a better competitive situation than instructions dealing only with the discounts directly.⁶

14. These agreed instructions were drawn up in the belief that the divestiture solution will allow local competition to Neshet in manufacturing, which would probably not be created without them and would allow an alternative steady and regular supply of cement.

15. While behavioural instructions on stopping the price discrimination through discounts might have supported the import of cement by the large manufacturers of concrete, it is believed that allowing for an alternative local production would have better competitive effects on the relevant markets.

2. The Liquefied Petroleum Gas (LPG) market case

16. The LPG case dealt with a suspected price discrimination used by LPG suppliers in order to prevent customers from switching gas suppliers. The IAA drafted recommendations for the responsible sector regulators to change their relevant regulations and forbid this behaviour. At present, the IAA's draft recommendations are published for a public hearing.

2.1 Background

17. LPG is a major source of energy for households in Israel, used mainly for cooking and heating. The most common way of consuming LPG by households is connecting an apartment building or several buildings to a central gas tank.

18. Weak competition in the LPG market is evident from the long-lasting similar and stable market shares of the three large suppliers and the extremely low percentage of switching between them (less than 1% of customers). Customers indicated that when they asked for a quote from a large supplier, they were not given competitive offers.

19. In the past years the relevant regulators – the Ministry of National Infrastructure, Energy and Water Resources and the Ministry of Interior – made efforts to improve the situation by various regulations, but the state of competition has not changed significantly.

⁶ The agreed solution was part of a combined agreement reached with Neshet together with the Ministry of Finance and the Ministry of Economy and Industry.

20. The IAA carried out a thorough examination of the LPG market and found various factors affecting competition. The LPG market is characterized by a shortage of input, as most of the time the LPG supply does not meet its demand. The three large LPG suppliers are less affected by the shortage, as they have access to large storage containers which allow them to store gas during periods when there is a surplus or to import gas.⁷ Unlike the larger firms, the smaller firms⁸ lack storage solutions and so are unable to store gas purchased locally or enjoy import alternatives during periods of shortage.

21. Apart from the LPG shortage, smaller suppliers have additional difficulties limiting their ability to compete, an important one of which is the switching barriers costumers face when attempting to transfer to a competing supplier. There are detailed regulations aiming to lower switching barriers, but these did not solve the switching difficulties.

22. According to the Land Law-1969 and the relevant regulations, a building may change its LPG supplier if it presents written consent of more than 50% of its apartment owners. Getting these approvals is very challenging, especially if many of the apartments are rented out. Moreover, customers have complained that the LPG suppliers do not cooperate with switching requests and will claim that the signatures collected are forged, do not belong to the apartment owners, that there are additional buildings connected to the certain tank and their consent is required too, etc. For customers or small suppliers to bring these disagreements to court is expensive and time consuming.

23. The IAA suspects that when large suppliers discover that a building is planning to switch to a competing supplier, they approach some apartment owners who have not yet given their consent and offer them special prices.⁹ By giving those clients special offers they prevent the entire building (or buildings) from switching to a competing supplier. As a result, the growth barriers for competing suppliers grow even higher. An examination of prices paid to suppliers revealed that, in fact, there were substantial differences in prices paid by clients connected to the same LPG tank.

2.2 IAA's recommendations

24. The IAA believes that in order to improve the competitive situation, the regulators involved must use a combination of regulatory tools addressing the competitive concerns in the LPG market, including with respect to the suspected use of price discrimination as a switching barrier.

25. The two first recommendations deal with the LPG shortage faced by small suppliers and are aimed to allowing small LPG suppliers to purchase from the refineries all the LPG they request and to initiate an LPG storage container which will be rented to small suppliers in order to allow them to import LPG.

26. The third recommendation focused on the difficulty in collecting signatures from the apartment owners in order to switch an LPG supplier. The IAA recommended changing regulation in a way that will lower the switching barrier and empower any building committee to decide on the issue of switching an LPG supplier. An alternative recommendation is to allow tenants (who are not apartment owners) to give their consent, instead of the owners who tend to be indifferent to the price, as it is usually paid by the tenants.

⁷ In addition, one of the large suppliers is vertically integrated with a refinery.

⁸ About 20 suppliers with aggregated supply that amounts to not more than ten percent of the market.

⁹ These suspicions are based mainly on complaints and conversations with clients.

27. The fourth recommendation is to forbid large LPG suppliers to discriminate between customers connected to the same central tank. This recommendation may prevent certain customers from getting reductions that they would be able to receive by negotiating their prices and may even raise their prices. However it will allow buildings to get together and agree on switching suppliers without intervention from large suppliers. It also gives customers interested in lowering their LPG costs an incentive to try to negotiate a better price for the entire building or to try to switch the building's LPG supplier.

28. In conclusion, the IAA suggested dealing with the market failures in the LPG household supply market, such as the shortage in input faced by small suppliers and the switching barriers, via solutions including increasing small companies' purchase allowance and prohibiting harmful price discriminations.

29. After drafting the recommendations, the document was sent to the relevant government ministries for comments. The ministries were willing to accept most of the recommendations. Consequently, the IAA published an amended draft for a public hearing which will end in the near future. After analysing and examining the comments received from the public, the IAA is intending to publish its final recommendations.

3. Conclusions

30. Analysing the above cases illustrates that there are various ways in which "price discrimination" can be used to harm competition and various tools that the Antitrust Authority can use to try to prevent these harms.

31. In the Neshet case we demonstrated how a monopoly with regulated prices can charge purchasers different prices which would result in a reduced incentive of its largest customers to develop an import alternative, and that this discrimination may lead to uncompetitive prices. We also demonstrated that the remedy to this behaviour does not necessarily have to deal directly with the discriminating prices; instead, the remedy may focus on finding a different solution that creates a better market structure.

32. In the LPG case, we demonstrated that "price discrimination" used by firms within an oligopoly can raise switching barriers and block attempts by small suppliers to compete. In this case, the IAA found that the best way to deal with the obstructive discrimination is to change the sectoral regulations and forbid the discrimination. These recommended changes should hopefully increase consumers' ability and incentive to switch to competing suppliers, and as a result lead to a better competitive situation.