

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

Competition Issues in Aftermarkets - Note from Sweden

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

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1. Introduction

1. An aftermarket can be defined as a market for the provision of products and/or services for use with a previously purchased durable good. The latter is referred to as primary product. The market for the primary product is called the primary market.
2. Aftermarkets typically involve follow-on sales of spare parts, repair and maintenance services, and complementary consumables. Examples of primary products and aftermarkets include razors and replacement blades, coffee machines and capsules, printers and cartridges, cars and spare parts, computer software and updates, etc.
3. This submission begins by summarizing the theoretical framework within which aftermarkets can be assessed, considering market definition and then potential anticompetitive motives and effects of unilateral conduct in aftermarkets. The submission then turns to the legal framework in Sweden for assessing aftermarkets, describing the circumstances in which aftermarket cases would be likely to be prioritised for enforcement by the Swedish Competition Authority (SCA). Finally, Swedish cases involving aftermarkets are presented.

2. Theoretical framework for aftermarket cases

2.1. Market definition

4. As noted by the Secretariat's call for contributions¹, there are theoretically three ways to define a relevant market in aftermarket cases. First, one can define a so called "systems market", which is a single market for both primary products (e.g. aeroplanes) and secondary products (e.g. maintenance and spare parts). This could be the case when the buyers (e.g. airlines) are "sophisticated" and take into account lifecycle costs when they make a decision to choose a particular brand of a primary product.
5. The second possibility is to define a "dual market", that is to say a single market for the primary products and a single aftermarket for all manufacturers' secondary products. Such market definition arises when all primary products are compatible with all manufacturers' secondary products. This may, for example, be the result of standardisation.
6. The third option is to define "multiple markets", consisting of a single market for the primary products and a separate aftermarket for each manufacturer's secondary products. This is the case when the primary products of each manufacturer are not compatible with the secondary products of other manufacturers.

¹ COMP 2017.78

2.2. Exploitative motives and effects in aftermarket cases

7. In some cases, a manufacturer of the primary good may have an incentive to exploit its market power in the aftermarket by charging prices above competitive level. However, the welfare effects of an exploitative conduct in aftermarkets are ambiguous.

8. There is a literature² which argues that a manufacturer can profitably exercise its market power in the aftermarket by increasing prices above the competitive level even though it costs the manufacturer some sales in the primary market. Even if the consumers are perfectly informed about the lifecycle costs, the manufacturer has an incentive to lower the prices in the primary market and charge higher prices in the aftermarket. This way the manufacturer breaks even on the new customers while earning profits on the locked-in customers. This reduces total welfare.

9. There is also a literature³ which argues that aftermarket monopolisation can reduce inefficiencies and thus increase total welfare. In a setting in which it is efficient to replace some of the durable goods while maintaining the others, the consumers choose to maintain their used durable goods inefficiently too often if the aftermarket is competitive and the consumers face a switching cost. If, on the other hand, the aftermarket is monopolised, the manufacturer can apply optimal pricing which reduces the inefficiency and increases the total welfare.

2.3. Exclusionary conduct in aftermarket cases

10. In some cases, a manufacturer of the primary good may have an incentive to engage in an exclusionary conduct. Exclusionary conduct in aftermarket cases can take the form of illegal tying of supply of secondary products to the primary product or refusal to supply secondary products to competing manufacturers. Most exclusionary practices in aftermarkets involve tying. For example, a manufacturer of a primary good can tie the sale of spare parts to aftermarket services provided by the manufacturer itself.

11. The likelihood that the monopolisation of the aftermarket has a significant anticompetitive effect depends on many factors⁴. One such factor is switching costs: the higher the switching costs are, the more locked-in the customers are. Another factor is a possibility to contractually negotiate the price for aftermarket products at the time of purchase of the primary good. Available information also affects the potential anticompetitive effects in aftermarket cases. The better informed the consumers are, and the better quality information there is, the less likely the manufacturers are to be able to harm consumers. The size of the aftermarket as well as the proportion of locked-in customers relative to new customers also affect the manufacturer's incentives to engage in anticompetitive behaviour in the aftermarket. Competition in the primary market can also be named as an important factor that affects competition in the aftermarket⁵.

² See e.g. Borestein S. et al. (1995), "Antitrust Policy in Aftermarkets", *Antitrust Law Journal*, Vol. 63, pp. 455-482

³ See e.g. Carlton D.W. and Waldman M. (2009), "Competition, Monopoly, and Aftermarkets", *Journal of Law, Economics & Organization*, Vol. 26, No. 1, pp. 54-91

⁴ See Coppi L. (2007), "Aftermarket monopolization: the emerging consensus in economics", *The Antitrust Bulletin*, Vol. 52, No. 1, pp. 69-70.

⁵ *Ibid*

3. The legal framework in Sweden

12. In this submission, the term “aftermarket conduct” is used to describe cases where the conduct is undertaken on a market for products or services in the downstream market in relation to the primary market. The term used in the present submission is used as a collective term to define situations where unilateral and multilateral conduct involve, or occur on, aftermarkets and is not intended to be interpreted as a legal definition *stricto sensu*.

13. An aftermarket conduct can arise through the actions of one undertaking, and thus be unilateral, but it can also be multilateral and consist of the cooperation between two or more undertakings.

14. Unilateral conduct can be challenged as abuse of a dominant position pursuant to Chapter 2 Article 7 of the Swedish Competition Act and the corresponding prohibition in Article 102 of the Treaty on the Functioning of the European Union (TFEU). The prohibition applies both to exclusive and exploitative conduct. The most typical types of aftermarket conduct that may constitute abuse involve refusal to supply and different forms of tying and/or bundling.⁶ In these cases, the question of whether the primary and the secondary products belong to the same or separate markets has a very large significance both in the assessment of dominance and on the potential effects of the conduct.

15. Multilateral aftermarket conduct can be challenged as an anticompetitive practice according to Chapter 2 Article 1 and the corresponding prohibition in Article 101 of the TFEU. Even though there is no requirement of dominance, the market definition also plays a central role in these cases, since it is of relevance in determining the application of certain block exemptions.

16. If the market share of each of the parties to the agreement falls below 30 per cent, the aftermarket conduct may be exempted according to the Block Exemption Regulation.⁷ There is an additional block exemption available in the motor vehicle sector⁸. Here, the Commission distinguishes between a primary market for the sale of new motor vehicles and a secondary market for spare parts and repair services for motor vehicles due to the fact that the market conditions for these products differ.⁹ This block exemption is explored more in the context of the discussion of the Kia Motors case below.

⁶ See Guidance on the Commission’s enforcement priorities in applying Article 102 to abusive exclusionary conduct by dominant undertakings (OJ C 45, 24 February 2009, p. 7), paras. 47 -62.

⁷ Commission Regulation 330/2010, 20 April 2010 on the application of Article 101(3) of the Treaty of the Functioning of the European Union to categories of vertical agreements and concerted practices. See Guidelines on Vertical Restraints, para. 91.

⁸ Commission Regulation 461/2010, 27 May 2010 on the application of Article 101(3) of the Treaty on the functioning of the European Union to categories of vertical agreements and concerted practices in the motor vehicle sector.

⁹ Supplementary guidelines on vertical restraints in agreements for the sale and repair of motor vehicles and for the distribution of spare parts for motor vehicles, OJ C 138, 28 May 2010, p. 16, para. 11.

17. Guidance in the assessment of the relevant market definition in such cases can be sought in the Commission's Notice on the definition of the relevant market.¹⁰ When carrying out an assessment of the relevant market involving a primary and a secondary market, the method to be followed is the same as when dealing with one market, meaning that demand side substitution in response to relative price changes should be considered. In addition to this, when assessing conduct pursuant to abuse of dominance rules, the constraints on substitution caused by the conditions in the markets (primary and secondary) must also be taken into account and can impact how narrowly the secondary market can be defined.¹¹ An example of how a Swedish court has defined a relevant market in an aftermarket case is presented below¹².

4. The SCA's prioritisation of cases for enforcement

18. The Swedish Competition Authority's Prioritisation Policy for Enforcement (hereafter "Prioritisation Policy") describes the factors that are taken into consideration when prioritising competition concerns for enforcement.¹³ The most important basis for prioritisation is whether a conduct is able to harm competition and consumers. The SCA gives particular consideration to the share of the market that is affected by the conduct and, in cases where the foreclosure concerns an input, to what extent the input is essential to enable effective competition in the market. In assessing price-based conduct, the SCA also considers whether the pricing is capable of foreclosing a competitor which is hypothetically as efficient as the dominant firm.

19. As regards unilateral conduct, the SCA prioritises investigating conduct by dominant firms that is capable of excluding or foreclosing firms which are able to exercise effective competitive pressure on some level of the market.

20. As mentioned above, aftermarket conduct may lead to exploitative effects, making the producer of the primary good able to charge prices above competitive level for the secondary goods, but there may also be exclusionary motives and effects to such conduct.

21. An aftermarket conduct which is capable of leading to exclusionary effects would have a higher likelihood of being prioritised. The focus of the SCA's investigation would thus likely not be on the exploitative effects of the aftermarket conduct but rather on the exclusionary effects.

22. If an aftermarket conduct is prioritised for further investigation, the SCA investigates and gives careful weight to the possible efficiencies and objective justifications to the conduct.

23. The SCA's decision not to prioritise a case cannot be appealed. If the SCA decides in a particular case not to intervene against an alleged infringement of the prohibitions laid down in Chapter 2 Article 1 or 7 of the Swedish Competition Act or

¹⁰ Commission Notice on the definition of relevant market for the purposes of Community competition law ("Relevant Market Notice"), OJ C 372, 9.12.1997, paras. 5 – 13.

¹¹ See Relevant Market Notice, para. 56.

¹² Kia Motors, MD 2012:13

¹³ Available in English at http://www.konkurrensverket.se/globalassets/english/about-us/english_prioritisation_policy_for_enforcement.pdf

Articles 101 or 102 TFEU, an undertaking affected by the alleged infringement has the right to pursue legal action in the Patent and Market Court.

5. Recent Swedish cases concerning aftermarkets

24. The number of cases in which the SCA has dealt with or pursued cases concerning aftermarkets in the recent years is limited.

5.1. Kia Motors, MD 2012:13

25. A notable case regarding the assessment of aftermarkets is the judgment of the Swedish Market Court in the *Kia Motors case*¹⁴.

26. In this case, Sveriges Bildelsgrossisters Förening (SBF), a trade association for Swedish suppliers of spare parts for cars, raised an action against the car manufacturer KIA Motors Sweden AB (KIA) in the Market Court. The contested practice was KIA's use of a term in the warranty for new KIA cars according to which regular service had to be conducted by an authorised KIA repair shop during the validity period of the new car warranty. The validity period of the warranty was seven years.

27. SBF had previously submitted a complaint against KIA to the SCA, which decided not to prioritise the case. SBF therefore pursued legal action in the Market Court against KIA in accordance with Chapter 3 Article 2 of the Swedish Competition Act.

28. In its action, SBF requested that the Court order KIA to cease to apply the contested practice under penalty of a fine of 500,000 SEK or any other amount the Market Court deemed appropriate. KIA contested the claim. SBF claimed that the practice at hand was an anticompetitive agreement pursuant to Chapter 2 Article 1 of the Swedish Competition Act and Article 101 TFEU as well as an abuse of dominance pursuant to Chapter 2 Article 7 of the Swedish Competition Act and Article 102 TFEU.

29. The Court held that the application of the warranty term by KIA and its authorised repair shops constituted an infringement of Chapter 2 Article 1 of the Swedish Competition Act and Article 101 TFEU and ordered KIA to cease with the application of the contested warranty term under penalty of a fine of 5,000,000 SEK.

30. The main issue considered by the Court was whether the term included in KIA's warranty for new cars, requiring that all regular repairs during the warranty period be carried out by authorised KIA repair shops in order for the warranty to be valid, was an anticompetitive agreement pursuant to Chapter 2 Article 1 of the Swedish Competition Act. The court did not assess the question of abuse of dominant position.

5.2. Definition of the relevant market

31. The Market Court defined the relevant market as the market for service and repairs of KIA cars in Sweden.

32. The Court first considered whether the market could be defined as a systems market. It found that this was not the case and concluded that the market should be defined as an aftermarket, separate from the market for the sale of new cars.

¹⁴ *Svenska Bildelsgrossisters förening v. Kia Motors Sverige AB*, MD 2012:13.

33. According to the Court, in order to reach a finding that the market was to be defined as a systems market, it had to be shown that the circumstances were such that consumers actually perceived the purchase of a car and the subsequent service and repair costs as parts of system. Thus, in order to define a systems market it had to be shown that the behaviour of consumers was such that they were able to calculate costs for future repairs and services and they considered the costs for future services for repairs when buying a car in such a way that they impacted their choice of car.

34. According to the Court, KIA had not put forth an investigation of the considerations and the assessments consumers actually undertake when purchasing a car. Furthermore, the Court considered that it had not been shown that there was any other investigation showing that a sufficiently large share of consumers considered and took into account of a car's lifecycle costs such that they actually influence their choice when purchasing a car.

35. Since the Court concluded that the aftermarket was separate from the primary market, it went on to assess whether the relevant market would be defined as a brand-specific market for KIA or if it would be defined as the market for repair services for cars irrespective of the brand. It concluded that the market was brand-specific.

36. In its assessment, the Court considered that there was no demand substitution for KIA owners regarding substitution of KIA service to the service of other car brands. Therefore, a KIA-owner did not switch to BMW or Volvo repair shops for repair services even if the price of KIA service would rise by 5 – 10 %. The Court examined whether supply-side substitution would lead to a different definition but concluded that there were no conditions at hand in order to consider substitution patterns in the supply side, and referred to Article 23 in the Commission's Notice on the definition of the relevant market.¹⁵

5.3. Assessment of the conduct

37. In its assessment, the Court examined whether the criteria for finding an anticompetitive agreement were fulfilled. Both KIA and the authorised repair shops were found to have a joint will to act in accordance with the term set out in the contested warranty terms towards customers. Amongst other circumstances in this assessment, the Court took into account that the contested term was also reflected in the standard agreements which the authorised repair shops had undertaken to comply with in order to be authorised by KIA. Authorised repair shops had an obligation to fulfil the guarantees set out by KIA in connection with the sale of new cars. The conduct at hand was therefore considered to fulfil the agreement criteria set out in Chapter 2 Article 1 of the Swedish Competition Act.

38. The Court found that the application of the warranty term had as its object the restriction of competition as regards the regular service of KIA cars. Through the application of this term, non-authorised repair shops undertaking to service KIA cars were hindered from offering regular service for such cars in accordance with the seven-year warranty.

¹⁵ See Commission Notice on the definition of the relevant market for the purposes of Community competition law (OJ C 372, 9 December 1997, p. 5).

39. The Court considered whether the conduct could be exempted from the application of competition law due to a block exemption in the area of motor vehicles¹⁶. Given the market share of KIA and the authorized repair shops the agreement could not fall under this exemption.

40. Furthermore, the Court considered whether the conduct fulfilled the conditions for an individual exemption from the prohibition in anti-competitive cooperation in accordance with Chapter 2 Article 2 of the Swedish Competition Act and came to the conclusion that the use of the warranty terms was too far-reaching and thus did not deem the use of such terms as indispensable. The Market Court's decision could not be appealed.

5.4. Sodastream International, case number 632/2009

41. The *Sodastream case*¹⁷ is an example of an aftermarket conduct that was investigated by the SCA.

42. Further to a complaint lodged by Sodastream's competitor Vikingsoda AB, the SCA carried out an investigation into the allegedly abusive conduct by Soda-Club (CO₂) Ltd. and Sodastream International B.V., both of which are wholly owned subsidiaries of the Sodastream International Ltd. group ("Sodastream").

43. The Sodastream case involved the alleged abuse of a dominant position by Sodastream in violation of Article 102 TFEU and Chapter 2 Article 7 of the Swedish Competition Act. The relevant market was defined as the Swedish market for the refilling and distribution of gas intended for home beverage carbonation systems in Sweden. The SCA found that Sodastream held a dominant position in the relevant market. The SCA looked at different types of conduct as part of its investigation into the alleged abuse of a dominant position.

5.4.1. Distribution agreement

44. The SCA investigated whether Sodastream had sought to foreclose the market by imposing an exclusivity obligation on its customers, retailers of Sodastream products, which prohibited the customers from letting Sodastream's competitors refill gas cylinders marked with the Sodastream label. Customers were thus obliged to purchase all their gas refills of Sodastream-marked gas cylinders from Sodastream.

45. However, the investigation indicated that the majority of retailers and consumers had no knowledge of the said requirements found in their agreements with Sodastream. The investigation indicated that Sodastream had in practice not monitored whether the requirements were being implemented.

¹⁶ Vertical agreements regarding the conditions for the purchase, sale and reselling of spare parts for motor vehicles or repair services for motor vehicles, can be exempted from the application of Article 101(1) in accordance with Regulation 330/2010, provided that the threshold requirements are met and that the vertical agreement does not contain so-called "hardcore" restraints. The hardcore restraints included regard competitive restraints that rise from vertical restraints on aftermarkets for motor vehicles and aim to address those concerns.

¹⁷ The decision is available here (in Swedish): <http://www.konkurrensverket.se/beslut/09-0632.pdf>

5.4.2. User licence certificate

46. In addition to this, the SCA investigated Sodastream's inclusion of a "user license certificate" in connection with the sale of gas cylinders to consumers whereby no-one other than Sodastream was allowed to refill the gas cylinders.

47. However, the SCA's investigation found that consumers could not be considered legally bound by the "user licence certificate", and that Sodastream did not monitor whether consumers had breached the certificate.

5.4.3. Exercise of trademark rights

48. Finally, the SCA investigated Sodastream's exercise of its trademark rights against refillers which had re-labelled Sodastream-labelled gas cylinders in order to fulfil certain regulatory requirements.

49. In parallel to the SCA's investigation, legal proceedings were ongoing in the Stockholm District Court in a case regarding whether an independent gas cylinder refilling company had infringed Sodastream's trademark. The SCA noted that the District Court would be required to consider competition law interests as part of its assessment. Under these circumstances, the SCA concluded that there were insufficient grounds to continue its investigation.

50. Sodastream won the case in Stockholm District Court. The case was appealed to the higher court, which upheld the district court's ruling.