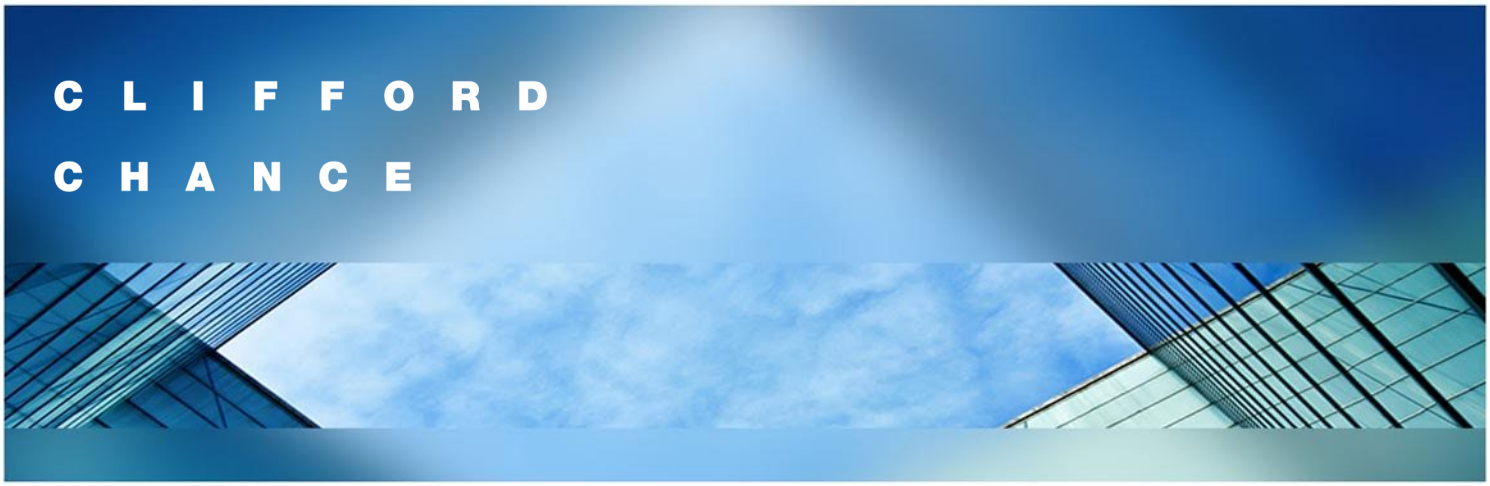

CMA LOSES IN THE COURT OF APPEAL IN LANDMARK CASE ON UNFAIR PRICING

On 10 March 2020, the Court of Appeal dismissed the Competition and Markets Authority's ("**CMA**") appeal against a previous decision of the Competition Appeal Tribunal on unfair pricing. The CMA's key ground before the Court of Appeal, that it had an unfettered discretion to choose between analysing whether a product was unfair "in itself" or "compared to competing products" was rejected. The Court found that these were not true alternatives and, importantly, if a defendant raises other methods or types of evidence then the authority must fairly evaluate them. Two further CMA grounds were rejected, in effect, on the basis that the CMA had attempted to appeal factual findings. While the CMA did succeed on one ground, that there was no requirement in every case to create a hypothetical benchmark price, the Court of Appeal upheld the Tribunal's judgment overall. The CMA has decided not to appeal and the matter will now be remitted to the CMA to reconsider the questions of abuse and penalties in light of both judgments.

Background

Pfizer's phenytoin capsules (marketed as Epanutin, a branded off-patent medicine) had been loss-making for a number of years. An identical tablet product was marketed at a price at least 30 times higher than the capsule price. Pfizer concluded a deal with Flynn under which it continued to manufacture the product while Flynn marketed the capsule. Flynn launched the capsules as a generic medicine at an increased price in September 2012, although at a lower price than the tablet. As a result, the price of capsules increased by up to 2,600%. After a long investigation, the CMA issued a decision against Pfizer and Flynn finding that they had each abused a dominant position in the manufacture and supply of "Pfizer-manufactured capsules" by charging excessive and unfair prices. The CMA imposed a record £84.2m fine on Pfizer and a £5.2m fine on Flynn (the statutory maximum) and directed both companies to lower their prices.

Following an appeal by Pfizer and Flynn, in June 2018, the Tribunal set aside the CMA's decision. It found that the CMA did not correctly apply the legal test for finding that the prices were unfair; it did not appropriately consider what was the right economic value for the product at issue; and it did not take sufficient account of the situation of other, comparable, products, in particular the phenytoin sodium tablet. The Tribunal also set aside the penalties imposed, including the £84.2m fine against Pfizer. The CMA appealed the Tribunal's judgment and Flynn appealed on a narrow issue.

Key issues in unfair pricing

- There is no single method to establish an abuse and authorities have a margin of manoeuvre in deciding which methodology to use and which evidence to rely upon.
- However, an authority does not have an unfettered discretion to choose between whether a product's price is unfair "in itself" or when "compared to competing products".
- If a defendant raises other methods or types of evidence then the authority must fairly evaluate them.
- If an authority rejects comparators wrongly or without giving appropriate reasons, its infringement decision will be more vulnerable on appeal.
- Companies should take particular care in setting prices of products which may face limited competition.
- Careful consideration should be given to any substantial increase in the price of such a product including: how far above cost the new price will be; how it compares to rival products; and how it compares to products in other markets.
- Clifford Chance acted for Pfizer during the investigation; in its successful appeal to the Tribunal; and in its success before the Court of Appeal.

The unfair limbs in *United Brands* are not true alternatives

The CMA's position before the Court of Appeal was that the two tests for whether a price was unfair in *United Brands* (unfair "in itself" or when compared to "competing products") were true alternatives. Having found that the phenytoin price was unfair in itself (because it had exceeded a return on sales of cost plus 6%), the CMA's view was that there was no need for it to consider the price of competing products, including the identical tablet. The Court of Appeal found that the CMA's reading of the test in *United Brands* was unduly rigid and literal and invested far too much significance in the word "or" at paragraph 252. If the CMA relies on the "in itself" alternative to find abuse, then it may still have an obligation in law fairly to evaluate *prima facie* comparator evidence that the prices are fair, adduced by a defendant undertaking. It therefore found that the CMA's appeal on this ground had failed.

The Court of Appeal considered all the major authorities in the area of unfair pricing and summarised the key principles arising from them. It found that the basic test for abuse is whether the price is unfair. There is no single method to establish an abuse and authorities have a margin of manoeuvre in deciding which methodology to use and which evidence to rely upon. Depending on the facts and circumstances of the case an authority might therefore use one or more of the alternative economic tests which are available. There is however no rule of law requiring authorities to use more than one test or method in all cases. In analysing whether the end price is unfair, a competition authority may look at a range of factors including, but not limited to, evidence and data relating to the defendant itself and/or evidence of comparables drawn from competing products and/or any other relevant comparable, or all of these. There is no fixed list of categories of evidence relating to unfairness.

The evidential burden in cases of unfair pricing

The judgment also clarified the burden of proof on authorities and defendants in cases of unfair pricing. If an authority chooses one method (e.g. cost plus) and one body of evidence and the defendant does not adduce other methods or evidence, the authority may proceed to a conclusion on the basis of that method/evidence alone. However, finding against the CMA, the Court of Appeal found that if a defendant relies on other methods or types of evidence then the authority must fairly evaluate it. The extent of the duty will be affected by the nature, extent and quality of the evidence adduced by the defendant which has an evidential burden. The authority will always need, at least as part of its duty of good administration, to give some consideration to *prima facie* valid comparators advanced evidentially by defendants. Contrary to the CMA's position before the Court, the fact that an appeal tribunal might review the evaluation is not a factor which affects the duty imposed on the authority.

An authority does not have to establish a hypothetical benchmark price

The Court also considered whether a competition authority is required to use a "hypothetical benchmark price" or range of prices as part of its evaluation of whether an actual price is excessive. In particular, whether non-price benchmarks such as cost or other related benchmarks (e.g. return on sales or return on capital employed) can be sufficient. To the extent that the Tribunal compelled the use of a particular test, the Court of Appeal found that it had misconstrued the case law because an authority has a margin of manoeuvre or discretion as to how it goes about proving its case. The Court of Appeal

“The authority will always need, at least as part of its duty of good administration, to give some consideration to *prima facie* valid comparators advanced evidentially by defendants."

found that all that is required is "a" benchmark or standard against which to measure excess or fairness.

An authority cannot ignore comparator evidence on the basis that it has conducted a sufficient analysis

The CMA argued, in essence, that it had conducted a detailed and sufficient analysis of the evidence that the Tribunal was unable to find serious fault with, and that the only flaw identified by the Tribunal was one of degree. The Court of Appeal found that on the facts of this case there was an obligation upon the CMA to properly and fairly evaluate the comparator evidence because it was adduced by the undertakings as part of their defences. It was not therefore open to the CMA to ignore the evidence simply because it had, in its judgment, conducted a sufficient analysis. Furthermore, while it accepted that the CMA had a margin of manoeuvre, this was quite different to whether the Tribunal, as a supervisory judicial body, must pay deference to the exercise of that judgment. Overall, the Court of Appeal could detect no error in the approach and found that at base the CMA objected to a finding of fact, which was not the proper basis for an appeal.

“It was not therefore open to the CMA to ignore the evidence simply because it had, in its judgment, conducted a sufficient analysis. "

Vos LJ added that the CAT was wrong in law to hold that the CMA had in every case to investigate comparators raised by the undertakings, which could be said to support a *prima facie* case that prices were fair. However, he added that if the CMA rejects the comparators wrongly or without giving appropriate reasons, its infringement decision will be more vulnerable, if and when the matter comes before the CAT on appeal. If the CMA wrongly ignores evidence of comparators, and those comparators turn out to be relevant or important, their analysis will fail at the CAT. Notwithstanding this, Vos LJ found that the CAT was entitled to draw the factual conclusions that it did.

The CMA had failed to take account of economic value

The CMA argued that the Tribunal had erred in finding that the CMA had attributed a nil value to patient benefit. The Court did not accept this ground of appeal. Green LJ found that on a fair reading of the judgment, the Tribunal found that the CMA had failed adequately to take account of evidence that there might be "some" (albeit unspecified) value to be attributed to patient benefit, and that the reasons given by the CMA for rejecting patient benefit as relevant (namely dependency) was itself an issue of fact and degree and did not mean that the CMA could ignore relevant evidence. The CMA had also wrongly concluded that there was nil value to such patient benefit upon an erroneous assessment (based upon an overly rigid construction of case law) that in a case of dependency no economic value could arise.

The Court of Appeal also noted that economic value needed to be factored in and fairly evaluated, somewhere, but it is properly a matter which falls to the judgment of the competition authority as to where in the analysis this occurs. However, there were no grounds of appeal which raised such matters. As above, the criticism of the CMA was one of fact and, as such, outside the scope of the statutory right of appeal. On this basis this ground of the CMA's appeal was rejected.

Flynn's appeal dismissed

In its appeal, Flynn argued that the Tribunal's decision relating to the comparison of products in its portfolio was illogical and/or inconsistent. In addition, that the Tribunal had failed to make a ruling on the "cost pool" issue.

The Court found that, given the purpose behind the Flynn Ground was to ensure that there was no fetter created by findings in the Tribunal's judgment, upon either the ability of Flynn to adduce new evidence or the CMA to re-investigate, there was no need for the Court to express a view upon the particular arguments advanced by Flynn. The ground of appeal therefore failed on the basis that it was advanced upon an inaccurate interpretation of the Tribunal judgment and order for remittal.

What does this judgment mean?

This judgment has further clarified the law in cases of unfair pricing.

- There is no single method to establish an abuse and authorities have a margin of manoeuvre in deciding which methodology to use and which evidence to rely upon.
- However, an authority does not have an unfettered discretion to choose between whether a product's price is unfair "in itself" or when "compared to competing products".
- If a defendant raises other methods or types of evidence then the authority must fairly evaluate them.
- If an authority rejects comparators wrongly or without giving appropriate reasons, its infringement decision will be more vulnerable on appeal.
- Companies should take particular care in setting prices of products which may face limited competition. Such a decision may not just have reputational consequences but lead to legal liability.
- Careful consideration should be given to any substantial increase in the price of such a product including: how far above cost the new price will be; how it compares to rival products; and how it compares to products in other markets. Those considerations should be recorded and legal advice should be sought.
- Even where the government/regulatory authorities have agreed to or acquiesced to a rival product being priced at a higher level, that may not be a sufficient defence.

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