Conditional Rebate Schemes and the More Economic Approach: Back to the Future?

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In 2009, The EU Commission's priority notice (guidance paper) appeared to introduce a new era in the treatment of price-related exclusionary conduct. Being an implementation of the more economic approach the "as efficient competitor" test (hereinafter "AEC test") entered the stage as the relevant yardstick for assessing conditional rebates. Recently, the European courts have ruled on conditional rebates in *Tomra* and *Intel*. Beyond assessing the specific facts at hand, the General Court and the Court of Justice took a stand on the application of the more economic approach to abusive rebates by dominant firms. This article will analyse these rulings and their potential impact on the treatment of rebates under EU competition law.

1 Introduction

In 2009, The EU Commission's priority notice (guidance paper) appeared to introduce a new era in the treatment of price-related exclusionary

conduct.[1] Being an implementation of the more economic approach the "as efficient competitor" test (hereinafter "AEC test") entered the stage as the relevant yardstick for assessing conditional rebates. Recently, the European courts have ruled on conditional rebates in *Tomra*[2] and *Intel*.[3] Beyond assessing the specific facts at hand, the General Court and the Court of Justice took a stand on the application of the more economic approach to abusive rebates by dominant firms. This article will analyse these rulings and their potential impact on the treatment of rebates under EU competition law.[4]

2 The Traditional Approach on Conditional Rebates

According to *Hoffmann-La Roche*[5] and *Michelin I*,[6] fidelity rebates are deemed anticompetitive per se due to their foreclosing effects,[7] which parallel those of exclusive purchasing agreements.[8] In the same vein, retroactive individualized target rebates are considered a per se violation since they generate discriminatory effects and lack objective justification.[9] This form-focused approach to rebates has often been linked to German ordoliberalism and its concept of an "economic constitution" providing the framework for all economic activity.[10]

According to the General Court's[11] ruling in *British Airways*, "for the purposes of establishing an infringement of Art. 82 EC, it is not necessary to demonstrate that the abuse in question had a concrete effect on the markets concerned. It is sufficient in that respect to demonstrate that the abusive conduct of the undertaking in a dominant position tends to restrict competition or, in other words, that the conduct in question is capable of having or likely to have such an effect."[12] While an objective justification defence has been acknowledged by the European courts, it is subject to high thresholds.[13]

3 The Commission's Guidance Paper on Exclusionary Practices

Following an extensive consultation process,[14] on 3 December 2008 the European Commission adopted the "Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings".[15] The guidance paper aims at focussing more clearly on the protection of the competitive process instead of the protection of particular competitors.[16] At the same time, it attempts to provide greater clarity and legal certainty for businesses. In the context of decentralized enforcement under Regulation 1/2003, such self-assessment tools have gained increasing significance.

The guidance paper was held to constitute a significant shift in the Commission's approach on exclusionary practices.[17] Instead of relying on a form-based analysis, the Commission now plans to compare costs and the efficient price to evaluate whether a practice actually has anticompetitive effects.[18] One specific result of this cost-price analysis is the AEC test.

According to the guidance paper "[…] the Commission will normally only intervene where the conduct concerned has already been or is capable of hampering competition from competitors which are considered to be as efficient as the dominant undertaking."[19] In some instances, where the dominant undertaking is an inevitable trading partner ("non-contestable" share of demand), the Commission will look at the "contestable" share of demand. The relevant cost benchmarks that the Commission is going to use are the average avoidable costs (AAC – not including sunk-costs incurred before implementation of the rebate) and long-run average incremental costs (LRAIC – variable and fixed costs).[20] From the application of these thresholds results a three-tier classification of rebate-affected prices: prices below AAC indicate "that the dominant undertaking is sacrificing profits in the short term and that an equally efficient competitor cannot serve the targeted customers without incurring a loss."[21] Prices above LRAIC will not foreclose an equally efficient competitor from the market and the respective practice will usually not be deemed anticompetitive. An effective price between AAC and LRAIC will prompt the Commission to analyse whether other factors, such as the capacity to obtain inputs at a relatively low price, allowed the competitor to offer a viable alternative to the dominant undertaking's product.[22]

4 *Tomra*: The AEC Test in Action – Or Is It?

In 2006, the Commission fined the Norwegian company Tomra, a producer of reverse vending machines, for having abused its dominant position.[23] The Commission held that Tomra had infringed Art. 102 TFEU by engaging in exclusivity agreements, quantity commitments and retroactive rebate schemes with its clients.[24] The agreements – in particular in their cumulative effect and in view of the transparent market – were held to aim at restricting market entry of (potential) competitors.[25] Relying on the *Hoffmann-La Roche*, *Michelin I*, *II* and *British Airways* judgements, the Commission argued that the applied individualized retroactive rebate schemes had effects similar to tying schemes and exclusivity agreements.[26] Accordingly, these agreements could have been justified only in exceptional circumstances.[27]

Tomra filed a complaint to the General Court[28] with one of the objections being that the Commission had, contrary to the guidance paper, not applied the AEC test. The General Court, however, stuck to the form-based approach and rejected Tomra's complaint without profusely discussing the AEC. Yet, reacting to one of Tomra's objections, it held that negative prices were not in themself a sufficient basis for establishing anticompetitive effects.

On further appeal the Court of Justice upheld the General Court's argumentation. It stressed the necessity to consider all relevant circumstances. The Court did not

assess possible "negative prices" but held that "the invoicing of 'negative prices' (in other words prices below cost) to customers is not a prerequisite for the finding that a retroactive rebates scheme operated by a dominant undertaking is abusive."[29] It furthermore relied on the rather form-focused finding that Tomra had granted rebates on a customer's entire purchase, targeted them individually to large customers and keyed them to a customer's estimated entire demand.[30]

All in all, the Court of Justice's *Tomra* ruling is neither a clear dismissal of the AEC test nor its breakthrough. For this time, the Courts did not have to show their colours since the Commission decision was adopted in 2006, and hence it was not imperative to square it with the guidance paper of 2009.

5 *Intel*: Taking a Stance

On 23 March 2009 the Commission imposed the record fine of 1.06 billion euros on the American microchip manufacturer Intel for having abused its dominant position on the market of "chipsets" and other semiconductor components. The case initiated from a complaint by Intel's competitor Advanced Micro Devices (AMD) according to which Intel granted rebates to Dell, HP, Lenovo, NEC and Media-Saturn-Holding for obtaining all or almost all of their demand in computer chips from Intel. According to the Commission, these original equipment manufacturers (OEMs) "not only held a significant part of the market, but were also strategically more important than other OEMs."[31] Furthermore, Intel was sanctioned for having made direct payments to computer manufacturers in order to stop or delay the launch of specific products containing AMD's ◆86 CPUs[32] and to limit the sales channels available to these products.[33]

5.1 The Application of the *AEC* Test in the Commission's Decision

According to the Commission, the guidance paper did not apply to the case because it was published only after Intel had been given fair hearing in 2007.[34] The Commission nonetheless conducted the AEC test as a hypothetical exercise and concluded that the decision was "in line with the orientations set out in the guidance paper."[35] However, the Commission also clarified that the AEC analysis was only

one of several parameters to examine a potentially harmful effect on competition[36] and not "a necessary or absolute test."[37]

It is in line with this cautious application of the AEC test that the Commission categorized Tomra's conduct as "naked restriction",[38] and dismissed a requirement to demonstrate evidence for actual foreclosure by concluding that

> it is necessary to consider all the circumstances particularly the criteria and rules for the grant of the discount and to investigate whether, in providing an advantage not based on any economic service justifying it, the discount tends to remove or restrict the buyers freedom to remove or to choose its sources of supply.[39]

5.2 The Holding of the General Court

Intel turned – just as Tomra had done – to the General Court on the grounds that the Commission had not established actual foreclosure and that it had made mistakes in the application of the AEC test.[40]

In deciding on the appeal the General Court distinguishes three types of rebates. The first category encompasses quantitative rebates which are generally held to be in accordance with a competitive market.[41] The second category, labelled "exclusivity rebates" or "fidelity rebates within the meaning of Hoffman-La Roche", includes rebates granted under the condition that the customer obtains all or most of her supply from the dominant undertaking.[42] These fidelity rebates are held to be incompatible with the objective of undistorted competition.[43] The third category encompasses rebates which are not directly linked to an exclusive or quasi-exclusive purchasing condition[44] but which may have a "fidelity-building effect".[45] In assessing this category it is necessary to consider all relevant circumstances including foreclosure effects and potential economic justifications.[46] As the rebates granted by Intel were held to fall within the second category, the Court rejected the necessity to demonstrate actual foreclosure or to apply the AEC test.

The Court further stated that the capacity to tie customers to a dominant undertaking is inherent in exclusivity rebates.[47] In consequence, exclusivity rebates granted by a dominant undertaking are by their very nature capable of foreclosing

competitors.[48] This is, according to the Court, especially the case because foreclosure effects occurred not only where access to a market was made impossible for competitors but also where access was rendered more difficult.[49] On the other hand the Court recognized the possibility to justify exclusive rebates, for instance by showing objective necessity of the conduct or by demonstrating countervailing efficiency gains which also benefit consumers.[50] In sum, the Court confirmed that the AEC test does currently not constitute a necessary requirement for establishing violation of Art. 102 TFEU.

6 Conclusions

Intel has appealed to the Court of Justice[51] and hence the final word on the application of the AEC test to conditional rebates is not yet been spoken. Tentatively, though, the AEC test appears to turn out as both an integrated and a pruned element of EU competition law.

The strong reliance of both the *Tomra* and the *Intel* courts on pre-existing, pre-more economic approach case law renders unlikely a scenario in which the AEC test becomes the exclusive yardstick for conditional rebates. With regard to this business practice, the AEC test will probably never be more than an additional tool which complements a predominantly form-focused assessment. This result is in line with the need of businesses

and law enforcement for the reliability created by legal rules which are formalized beyond a mere weighing of the economic data at hand.[52] Legal certainty is all the more paramount since market participants are required to self-assess the accordance of their conduct with EU competition law[53] and the enforcement of these rules is decentralized.[54]

This is by no means to say that the AEC test will have only a negligible impact on the future treatment of rebates. Rebates which are not – as the ones mainly dealt with in *Tomra* and *Intel* – exclusive[55] do require a very fact-sensitive approach, crucial part of which may be the AEC test. Even with regard to exclusivity rebates, the *Tomra* and *Intel* decisions underline the possibility of an efficiency defence. As part of this defence, AEC test-like economic considerations can be introduced albeit with the burden of proof on the rebating company. And last but not least, the AEC

test remains a criterion reaffirmed by the Court of Justice in the context of other exclusionary practices, such as margin squeeze or predatory pricing.[56]

The AEC test's not yet definitive status within the framework of EU competition law also affects the Commission's guidance paper. The paper itself explicitly states that it does not constitute a piece of law.[57] From this point of view the paper does not bind national competition authorities or courts but rather determines the Commission's internal priorities. Nonetheless, the paper contains substantive legal statements, some argue that these are an official interpretation of the law,[58] and the paper's view on the AEC test appears to differ from the Courts' approach in *Tomra* and *Intel*. Against this background it did not come as a surprise that the *Intel* court had to rebuff the claim that the Commission had infringed the principle of protection of legitimate expectations by relating to the relevance of the AEC test during the administrative procedure.[59] It seems worthwhile for the Commission to revise the guidance paper and to give the AEC test its metes and bounds, declaring it an additional, important but non-exclusive, tool for assessing potentially anticompetitive behavior – no more, no less. The decisions in *Intel* and *Tomra* could lead the way towards this judicious approach.

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1 Communication from the Commission – Guidance on the Commission's enforcement priorities in applying Art. 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, 2009/C 45/02, 24 February 2009. Available at http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0224(01)&from=EN (all web resources last accessed 12 February 2015).

2 Judgement of the European Court of Justice, Case C-549/10 P, 19 April 2012; Judgment of the General Court, Case T-155/06, 9 September 2010 – *Tomra Systems ASA and Others v. European Commission*.

3 Judgement of the General Court, Case T-286/09 – *Intel Corp. v. Commission.*

4 For more information on rebates under Art. 102 TFEU *see* Kamann and Bergmann (2005), Kallaugher and Sher (2004), Waelbroeck (2005) and Geradin (2009a).

5 Judgment of the European Court of Justice, Case C-85/76, 13 February 1979 – *Hoffmann-La Roche.*

6 Judgment of the European Court of Justice, Case 322/81, 9 November 1983 – *Michelin I*.

7 *Hoffmann-La Roche*, p. 540 at para. [90]; *Michelin I* Judgment, at p. 3475 and p. 3514 at para. [70 ff.].

8 *Hoffmann-La Roche*, at p. 468; Kamann and Bergmann (2005), p. 83, 86.

9 *Hoffmann-La Roche*, at p. 468. *See also* Judgement of the European Court of Justice, Case C-95/04, 15 March 2007 – *British Airways*.

10 Kallaugher and Sher (2004), p. 263, 268.

11 Then still called the Court of First Instance.

12 Judgement of the European Court of Justice, Case T-219/99, 17 December 2003 – *British Airways*, at para. [293].

13 Loewenthal (2005), p. 455, 476 ff. Fuchs and M&#65533;schel (2012), at [154].

14 *See* in this regard the DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses, Brussels,

December 2005, available at: http://ec.europa.eu/competition/antitrust/art82/discpaper2005.pdf.

15 Communication from the Commission – Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, 2009/C 45/02, 24 February 2009. Available at http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0224(01)&from=EN.

16 Guidance paper, at para. [6].

17 Gravengaard and Kj�rsgaard (2010), p. 285.

18 Guidance paper, at para. [20].

19 Guidance paper, at para. [23].

20 Guidance paper, at para. [26].

21 Guidance paper, at para. [26].

22 Rosenblatt and Armengod (2012), p. 49, 50.

23 Commission decision relating to proceedings under Art. 82 of the Treaty and Art. 54 of the EEA Agreement, Case COMP/E-1/38.113, 29 March 2006 – *Prokent-Tomra*.

24 *Prokent-Tomra* Commission decision, at para. [97 ff.].

25 *Prokent-Tomra* Commission decision, at para. [285]. "It has abundantly been shown in this decision that Tomra's practices tended to restrict competition, that is to say, were clearly capable of having that effect. In addition, however, the Commission has investigated the likely restrictive effects of the practices, which is discussed in Section 3.2".

26 *Prokent-Tomra* Commission decision, at para. [97]: "The latter types of agreements or conditions usually relate to quantities representing the entire requirements of the customer or a large proportion thereof within a given reference period. They are often referred to as "high-volume block orders".

27 *Prokent-Tomra* Commission decision, at para. [282 ff.] as stated in *Hoffmann-La Roche*: "Obligations of this kind to obtain supplies exclusively from a particular undertaking, whether or not they are in consideration of rebates or of the granting of fidelity rebates intended to give the purchaser an incentive to obtain his supplies exclusively from the undertaking in a dominant position, are incompatible with the objective of undistorted competition within the common market, because – unless there are exceptional circumstances which may make an agreement between undertakings in the context of article 85 and in particular of paragraph (3) of that article, permissible – they are not based on an economic transaction which justifies this burden or benefit but are designed to deprive the purchaser of or restrict his possible choices of sources of supply and to deny other producers access to the market. The fidelity rebate, unlike quantity rebates exclusively linked with the volume of purchases from the producer concerned, is designed through the grant of a financial advantage to prevent customers from obtaining their supplies from competing producers. Furthermore the effect of fidelity rebates is to apply dissimilar conditions to equivalent transactions with other trading parties in that two purchasers pay a different price for the same quantity of the same product depending on whether they obtain their supplies exclusively from the undertaking in a dominant position or have several sources of supply. Finally these practices by an undertaking in a dominant position and especially on an expanding market tend to consolidate this position by means of a form of competition which is not based on the transactions effected and is therefore distorted."

28 Tomra first appealed to the General Court and then to the Court of Justice.

29 Judgement of the European Court of Justice, Case C 549/10 P, 19 April 2012 – *Prokent-Tomra*, at para. [73]. In more detail *see* Bien and Rummel (2012), Maier-Rigaud and Vaigauskaite (2006). *See also* the Opinion of Advocate General Maz�k delivered on 2 February 2012, Case C-549/10 P – *Prokent-Tomra*, at para. [49 ff.].

30 Judgement of the European Court of Justice, Case C 549/10 P, 19 April 2012 – *Prokent-Tomra*, at para. [75 f.].

31 *Intel* Commission Decision, at para. [12]; Rosenblatt and Armengod (2012), p. 49, 51.

32 Central processing unit.

33 Summary on the *Intel* case by the European Commission, available at http://ec.europa.eu/competition/sectors/ICT/intel.html.

34 *Intel* Commission Decision, at para. [916]. Criticizing this, *see* Geradin (2009b), p. 6.

35 *Intel* Commission Decision, at para. [916].

36 *Intel* Commission Decision, at para. [1155].

37 *Intel* Commission Decision, at para. [1155].

38 *Intel* Commission Decision, at para. [917].

39 *Intel* Commission Decision, at para. [923].

40 Judgement of the General Court, Case T-286/09 – *Intel Corp. v. Commission*, at para. [70].

41 *Ibid*., at para. [75].

42 *Ibid*., at para. [76].

43 *Ibid*., at para. [77].

44 *Ibid*., at para. [78].

45 *Ibid*., at para. [78].

46 *Ibid*., at para. [78].

47 *Ibid*., at para. [86].

48 *Ibid*., at para. [87].

49 *Ibid*., at para. [88].

50 *Ibid*., at para. [94].

51 As apparent from the Court of Justice homepage the appeal is pending; Case C-413/14 P – *Intel Corp. v. Commission*.

52 Urging legal certainty in a "more economic competition law" *e.g*. Immenga and Mestm�cker, Art. 102 TFEU, 5th edn., para. [13]; Dreher (2008), 23, 25 ff. On the difficulties in measuring the (anticompetitive) economic effects of conditional rebates *cf*. Geradin (2009a), p. 59.

53 Articles 1 and 2 of Council Regulation (EC) No. 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (hereafter Regulation 1/2003).

54 On the specific changes under Regulation 1/2003, *see* Gauer et al. (2004).

55 On various categories of rebates *cf*. *supra* note 4.

56 Judgement of the Court, Case C-52/09, 17 February 2011 – *TeliaSonera*; and Judgment of the Court, Case C-209/10, 27 March 2012 – *Post Danmark*.

57 Guidance paper, at [3]. The General Court avoided answering the question relating to an infringement based on a time argument; *Intel* Commission Decision, at para. [157]. On the purposefully unambitious labelling of the paper as mere "enforcement priorities" Lovdahl Gormsen (2010), p. 45, 50.

58 Lovdahl Gormsen, Liza, *ibid*. She argues that the guidance paper is "*in effect* substantive guidelines offering an interpretation of the law". It would be left to the national law to include the guidance paper's content or not. Touching the issue: Bulst and Mehr (2009), p. 703, 718.

59 Judgement of the General Court, Case T-286/09 – *Intel Corp. v. Commission*, at para. [160 ff.]. The Court denied an infringement based on the facts of the case. It held that the Commission had made it clear that the economic assessment was no precondition for the finding of an abuse.