DISCOUNT POLICIES IN US AND EU ANTITRUST ENFORCEMENT MODELS: PROTECTING COMPETITION, COMPETITORS OR CONSUMER WELFARE?

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1. **Introduction**

The modernization of EU and US antitrust regimes that has occurred in the last decade has renewed interest in the antitrust community to find an appropriate enforcement model for restrictive conducts. Indeed, the longtime struggle between harm to competitors and harm to consumer welfare has fuelled the debate on the proper legal standard to be endorsed in the enforcement of exclusionary acts.\(^1\) Each conduct that may lead to an anticompetitive outcome, for example, unilateral practices, collusion or mergers, has undergone a process of re-thinking of the substantive, as well as the procedural tests to be applied. This process, as regards the EU, has in particular led towards the adoption of a criterion based on efficiency considerations, and hence more focused on an economic analysis of the context in which this type of behaviour occurs. In this respect, we have experienced a substantial convergence between the European and the US jurisdictions, the latter being historically characterised by a more widespread use of the “rule of reason” analysis.\(^2\)

However, despite this phenomenon of convergence, also assisted by the improvement in the transatlantic cooperation between antitrust agencies, differences in the application of fundamentally similar laws have emerged; and sometimes even in the evaluation of the same practices. The discrepancies between the two models are still important in the field of exclusionary conducts and discounts in particular.\(^3\) Or at least this was the case before the 2003 decision in the much debated

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Le Page v. 3 M decision⁴, as we argue in this paper. In fact, while in a first phase exclusionary conducts in general and rebates in particular were in the US assessed under a consumer welfare standard, which was based on the effects of the practice on both competitors and consumers, the case law and the decisional practice at EU level has endorsed a more formalistic model, that at times overlooks the economic analysis of the context in which the conduct takes place, namely, the effects of the practice. As a result, exclusionary conduct decisions by the Commission of the European Communities (“Commission”) and by the EU courts have been sometimes heavily criticized for sheltering inefficient competitors and for chilling the very essence of the competitive process.

Recent developments that have occurred on both sides of the Atlantic in the field of exclusionary rebates seem to have, nevertheless, reduced the inconsistencies between the US and EU approaches. The outcome of this process, though, as we claim in this paper, is hardly satisfactory; indeed, Le Page is regarded as a step backward from an effect-based standard to a new test more focused on assumptions. The few recent cases that have followed Le Page have not yet marked a clear position, as some have rejected the Le Page test while others have applied the same standard. By comparison in the EU, we have experienced an opposite trend: the recent Discussion Paper on the application of Article 82 of the EC Treaty to exclusionary abuses has marked a move towards an effect-based approach.⁵ This effort is to be welcomed as it attempts to provide clearer rules on the distinction between lawful and exclusionary rebates. However, the way in which the effect-based test is construed, in particular the way in which the Commission reckons the share of contestable sales that should be left open to competition on the basis of which discounts by dominant firms are assessed casts some doubts on the appropriateness of the model suggested. These doubts are reinforced by the outcome of the first decision adopted after the publication of the Discussion Paper in which the Commission applied the new test.

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⁴ 324 F. 3d 141; 2003 U.S. App.
Therefore, while the path indicated by the Commission in the Discussion Paper seems to point in the right direction, there might still improvements to be made in the definition of the new enforcement model. This is because, although exclusionary conducts may at times disadvantage rival firms and unduly raise their costs, any market behaviour by a firm that has a significant market position will necessarily disappoint competitors, but could very well benefit consumers. It is for this reason that a formalistic approach based on assumptions is unconvincing.

In this paper, by summarising the main business justifications highlighted by the economic and business literature underlying the adoption of quantitative, or so-called “linear pricing”, and non-quantitative rebates, the so-called “non linear pricing” or “all-units/rollback rebates”, we come to the conclusion that even non-linear pricing has specific and well rooted economic and business motives.

In the review of US and EU case law on discounts we highlight the enforcement standards that have been endorsed on both sides of the Atlantic in the different phases that have characterised the relevant case law. Placing greater emphasis on the most recent developments, such as Le Page and its subsequent case law, the Discussion Paper, as well as the recent Tomra decision, we outline the differences in approach before and after Le Page and the Discussion Paper.

Finally, drawing from the case law and the decisional practice, we focus on the competitors’ harm test comparing the advantages and the disadvantages of the models that have been endorsed in the EU and the US.

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6 All-unit/rollback rebates are referred here rebates applied to all the units of product/service purchased by the client.
2. **The Economics of Rebates**

Contrary to what is claimed by a part of the economic and business literature, the justification underlying quantitative rebates (linear pricing) is quite simple: selling more units creates more revenues. Hence, since discounts are an output enhancing practice, the presumption, from a legal point of view, should be that they are lawful.

Even non-linear pricing has a business justification: because a firm might be unwilling to sell all its units at a lower price, as this would lower revenues, it can still sell more if it directs the discount only at incremental units. As we discuss below, even non-linear pricing or so called all-unit/rollback rebates, is in some settings compatible with undistorted competition. After all, the simple fact that discounts are such a common practice in the marketplace should mean that there are valid business motives for their adoption, even by firms with market power.

As a starting point, linear pricing may well reflect efficiencies experienced in the production process in the form of economies of scale, the recovering of client-specific investments or they can be simply learning curve benefits. The existence of such benefits justifies the downward translation of the cost savings in the attempt to expand demand. Linear pricing may also reflect improved manufacturing and sales capability which is then logically transposed to purchasers. In other words, rebates may be a legitimate tool to manage the production and sale risk. This has also been recognized by the OECD: “For suppliers, even those who enjoy a significant market power, who have low marginal costs of supply and high fixed costs, any threat of withdrawal of purchases or goodwill by a large buyer carries a significant business risk. Volume discounts are often a reaction to this risk.” Moreover, from a purely business perspective, linear pricing is a good way of increasing rebates at the margin while leaving consistent profits for the non incremental units.

In addition, all-unit and market share discounts can serve as a mechanism to provide strong incentives for the purchaser (when this is a retailer) to engage in promotional activities and, subsequently align the retailer’s and the manufacturer’s interests when monitoring the distribution activity is costly and burdensome. This is particularly valid in settings in which the distributor provides an added value to the products or services sold, and the manufacturer is interested in the retailer’s promotional effort. Instead of resorting to detailed legal arrangements that attempt to

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cover all the retailers’ activities, the parties are better off - and sales are increased - if the distributor’s reward is dependent on its achieved target sales or on the share of its requirements that are fulfilled by the supplier. The sales of the manufacturer’s product should be a good proxy of the distributor’s efforts.

As rightly pointed out in the Office for Fair Trading Economic Discussion Paper on Selective Price Cuts and Discounts, market share rebates have a pro-competitive feature that distinguish them from quantitative rebates, in that they “might be particularly well suited to lowering input costs for downstream firms of different sizes and thereby encouraging them to compete more effectively on price. Share of needs rebates (unlike volume discounts) allow small buyers to obtain similar discounts to large buyers. Thus, when offered by suppliers to intermediate markets, these rebates might encourage downstream competition which, in turn, should mean that the discounts are passed on substantially to consumers.”\(^\text{10}\)

This view is also shared by part of the economic literature that has stressed that all-unit discounts can arise profitably even in the absence of any exclusionary motive.\(^\text{11}\) On the one hand, rollback rebates can solve double marginalisation problems, since they allow the manufacturer to “[extract] surplus from the retailer with inframarginal payments without distorting its incentives at the margin”.\(^\text{12}\) In other words, all-units discounts are a valid alternative to a double pricing system: they are used instead of applying a unit price of marginal cost plus a fixed fee. They allow the identification of the target quantity to be sold to obtain the profit maximizing price for both the manufacturer and the retailer, as well as the percentage discount off the price. On the other hand, empirical analysis shows that the manufacturer and the retailer are better off with an all-unit discount contracts, rather than with a two-part tariff contract or a contract in which the discount is granted on incremental units.\(^\text{13}\)

\(^{10}\) Office for Fair Trading, *Selective price cuts and fidelity rebates*, quoted, p. 108.


\(^{12}\) S. Kolay, G. Shaffer, J.A. Ordover, quoted, p. 433. This situation occurs when demand is known by both the manufacturer and the retailer.

\(^{13}\) This situation occurs in a setting in which there is incomplete information, i.e. when the retailer has private information about consumers’ demand.
3. **US AND EU CASE LAW ON DISCOUNTS**

3.1 **US CASE LAW**

3.1.1 **INTRODUCTION**

Since there are solid economic and business justifications underlying the adoption of discounts even by a dominant firm, one would expect that the challenging of such practice is subject to a high standard of proof, so as to guarantee that rebates are prohibited only when they seriously undermine competition. Given their widespread use in the market case law and legal scholarship on the subject did not evolve in the US until rather recently. While an antitrust claim in single rebates has been based solely on a predation test, the standard has been somehow less clear for bundled rebates. Indeed, even if the potential for a company with market power in one market to leverage its benefits in another market has long been suggested by part of the antitrust literature,\(^{14}\) until *Le Page* courts have been wary to admit suits in a multi-product setting only based on a mere discount claim: proof of unlawful tying was requested. The idea one gets when looking at cases of the pre-*Le Page* era is that courts have in general felt that it was beyond their ability to identify rebates that threaten competition without running the risk of chilling legitimate price competition. As a result, the rule of law derived from *Brooke Group* and applied since then has appeared straightforward: in order to establish anticompetitive injury from a rival’s low prices, a plaintiff had to prove that, as a result of the discount, the monopolist’s prices fall below an appropriate measure of the rival’s costs.

Conversely, *Le Page* lowered the standard for antitrust liability in bundled rebates cases partially blurring the distinction between lawful and exclusionary conduct. The Third Circuit ruled that the principle that above-cost prices are *per se* lawful does not apply in the case of multi-product discounts. As we shall see below, the problem raised by *Le Page*, i.e. the need to identify clearer instances in which bundled rebate schemes are unlikely to cause concern, is not only a theoretical one. In the aftermath of *Le Page*, several antitrust lawsuits have been brought by competitors challenging the monopolist’s discount scheme. The conclusion reached in some of these judgments suggest that courts are starting to recognize the shortcomings of the *Le Page* approach.

By comparison, the approach developed in the EU has followed an opposite path. The case law has, from the outset, endorsed a strict and at times inconsistent approach vis-à-vis discounts, often equating them to *de facto* exclusive dealing without necessarily investigating the real foreclosure effect. The Discussion Paper, by contrast, has tried to introduce clearer rules; although we argue

\(^{14}\) See, for example, P. E. Areeda, H. Hovenkamp, *Antitrust Law*, § 768 b2.
that some of these rules are not always consistent with the existence of undistorted competition, this
effort is highly commendable. The standard applied in the recent Commission’s decisional practice
seems to show the shortcomings of some of the basic ideas underpinning the treatment of rebates, as
we shall see in the last part of Section 4.

3.1.2 SINGLE PRODUCT AND BUNDLED REBATES PRIOR TO LE PAGE

As pointed out earlier, in the pre-Le Page era, discount practices were assessed on a pure predation
standard. SmithKline v. Eli Lilly\textsuperscript{15} is not a straightforward pricing case, but rather a mixed
discount/tying one. Lilly was dominant in the manufacturing of a special type of antibiotics
(cephalosporin) which were supplied to hospitals, and held a market share well in excess of its
competitors, including SmithKline. In order to expand its market position in antibiotics different
than those for which Lilly was dominant – and which were exposed to strong competition – Lilly
instituted a bundled rebate scheme according to which hospitals were entitled to benefit from a 3%
bonus rebate provided that they combined the purchases of the products manufactured in monopoly
with those of the drugs exposed to competition. The scheme, however, provided that if the complete
bundle was not purchased from Lilly, the hospital was denied the bonus rebate on all purchases of
the entire group of antibiotics.

The Court found that Lilly’s discount program had a foreclosure effect on competitors since, in
order for rivals to win some of Lilly’s clients, they had to match the bonus rebate awarded on the
overall purchases of the bundle of products. This meant, in practice, that competitors had to offer an
average discount ranging from 16% to 35% as opposed to the 3% rebate applied by Lilly.

The Court retained that this was an illegitimate leverage of monopoly power because of the
bundling issue rather than for the exclusionary effects of the rebates. Indeed, after having
established that the antibiotics part of the bundle belonged to different product markets (in
particular, cephalosporin and non-cephalosporin antibiotics), the Court held that, “the act of willful
acquisition and maintenance of monopoly power was brought about by linking products on which
Lilly faced no competition (…) with a competitive product (…). The result was to sell all three
products on a non-competitive basis in what would have otherwise been a competitive market.”

\textsuperscript{15} 575 F.2d 1056.
California Computer v. IBM\textsuperscript{16} concerned a case of discounts coupled with design changes. In particular, IBM had introduced a new central processing unit ("CPU") system which was sold at a price considerably lower than other disk drives. As is common in the high tech market, competition took place through reverse engineering by IBM’s competitors which were able to undersell IBM’s disk driver by improving the product design. Following IBM’s discounts, all of the plug compatible manufacturers reduced their own prices below those applied by IBM. As a response to this competition, IBM further reduced its prices through the introduction of a new discount scheme.

Having suffered losses as a consequence of this pricing policy, California Computer instituted a lawsuit for violation of § 1 and 2 of the Sherman Act, claiming, amongst other things, that IBM’s introduction of new CPUs and disk drives together with the connected discount policy prevented it from effectively competing with IBM. By affirming a district court judgment which had found in favour of IBM, the Court of Appeal held that since IBM’s motivation to apply discounts was the result of competition from rival manufacturers, the fact that a competitor was excluded did not constitute a violation of § 2 of the Sherman Act.

In particular, the Court found that “[w]here the opportunity exists to increase or protect market share profitably by offering equivalent or superior performance at a lower price, even a virtual monopolist may do so.” At the same time, the Court did not rule out the possibility that such price competition could be found to be predatory, either because the prices are below marginal or average variable costs, or because evidence could demonstrate predatory intent.

Transamerica II\textsuperscript{17} concerned a situation similar to California Computer in which IBM responded to the vigorous competition by independent plug-compatible manufactures through both the redesigning of the interface between the CPU and the peripherals (manufactured by competitors) and the introduction of discounts on new products. Transamerica believed that IBM pricing behaviour was predatory and had caused it to incur substantial losses. The Court found that since the contested prices exceeded average total costs, California had to provide evidence that IBM’s prices had risen once competitors had left the market. As California Computer failed to provide sufficient evidence, the Court found in favour of IBM. The judgment recognized that IBM’s discount practice constituted normal price competition, even if it implied exclusion of competitors.

\textsuperscript{16} 613 F. 2d 727.
\textsuperscript{17} 698, F.2d 1377.
Barry Wright v. Grimmell\(^\text{18}\) provides a clear example of the strict approach followed in the US in condemning discounts schemes. Pacific, a large producer of mechanical snubbers,\(^\text{19}\) supplied Grimmell with snubbers to be installed in pipe systems for nuclear power plants. In order to obtain an alternative source of supply, Grimmell agreed to help Barry Wright – a competitor of Pacific – to develop a new line of snubbers that Grimmell would buy once manufactured.\(^\text{20}\)

Pacific realized that, due to the cooperation with Barry Wright, Grimmell had reduced its purchases, and so offered Grimmell a consistent discount on future orders (25%-30%). As a result of this price reduction, Grimmell cancelled its orders with Barry Wright and decided to fulfil its entire requirements with Pacific. Barry Wright then sued Pacific for violation of §2 of the Sherman Act on the ground that Pacific’s discounts had tortuously prevented Barry Wright from supplying Grimmell.

The case deals with a typical situation in which a discount practice by a monopolist prevents a competitor from supplying a monopolist’s client. The district court first and then the Court of Appeal for the First Circuit ruled in favour of Pacific on the ground that Barry Wright had not proved that Pacific’s discount policy was aimed at excluding Barry Wright. Indeed, since price cuts offered by Pacific were above average total costs and incremental costs, Barry Wright had to prove recoupment, that is to say, that Pacific increased (or would have increased) prices once Barry Wright had exited the market.

It is worth mentioning that the Court gave considerable weight to the efficiencies underlying Pacific discount scheme. In particular, the Court found that:

(i) the price cuts were justified by the economies of scale created by Grimmell’s large order;
(ii) the contract with Pacific meant for Grimmell a guaranteed and stable source of supply;
(iii) Pacific was able to better plan its production policy and avoid overcapacity.

The Court also stated that the fact that a discount contract by a monopolist ties a customer and forecloses competitors is not in itself a proof of restriction of competition.

This case clearly shows that the burden of proof to be overcome by a plaintiff is much more onerous than the one established in EU case law and practice and which has been recently reaffirmed in the Discussion Paper.

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\(^{18}\) 724 F.2d 227.
\(^{19}\) These are shock absorbers used in building pipe systems for nuclear power plants.
\(^{20}\) Snubbers are bought on medium long-term basis; contracts cover a period of two/three years.
Ortho Diagnostic v. Abbott\textsuperscript{21} provides a useful illustration of the standard applied for the assessment of rebates under the Sherman Act prior to Le Page. The controversy involved Ortho’s claim that Abbott violated antitrust laws by entering into a contract with the Council of Community Blood Centers (“CCBC”) which allowed CCBC members to obtain advantageous prices if they purchased a package of four or five blood screening tests from Abbott.\textsuperscript{22} The blood tests were offered in a bundle of five units, and fewer other tests were sold individually. The price for the bundle proved to be lower than that applied where the products were purchased individually. The effect of the rebate scheme on competitors, including Ortho, was that, in order to supply the CCBC, a rival firm had to compensate the client for the loss of the discount it would have obtained from Abbott as a consequence of meeting part of its requirements with other suppliers.

In line with the previous case law, the District Court claimed that the pricing policy of a monopolist can be challenged only on predation grounds. In particular, the Court found that where a monopolist faces competition on only part of a complementary group of products and offers products both as a package and individually, with the consequence that competitors are forced to absorb the difference between the bundled and unbundled prices, in order for the behaviour to be considered as illegitimate, the plaintiff has to show that: “(a) the monopolist has priced below its average variable costs or (b) the plaintiff is at least as efficient a producer of the competitive products as the defendant, but that the defendant’s pricing makes it unprofitable for the plaintiff to continue to produce”.

According to the Court “any other rule would entail too substantial a risk that the antitrust laws would be used to protect an inefficient competitor against price competition that would afford substantial benefits to consumers.”

The issue of tie-in effects of discounts is dealt with in Concord Boat and others v. Brunswick Corporation.\textsuperscript{23} Brunswick, a manufacturer of drive marine engines with a market share above 70%, offered market share discounts to boat builders and dealers. In particular, Brunswick guaranteed to customers that purchased a certain percentage of their engine requirements from it a rebate which increased in proportion to the quantity of products purchased. Brunswick’s initiative was followed by competitors that instituted market share discount programs, without, however, any great success. Rival boat builders then filed an antitrust suit alleging, among other things, that Brunswick had used

\textsuperscript{22} Abbott accounted for 70-90\% of the blood screening test market.
discount programs to monopolize the market in violation of Section 1 and Section 2 of the Sherman Act.

The Court found in favour of Brunswick and held that the plaintiffs had failed to provide sufficient evidence on the foreclosure of a substantial share of the relevant market. In particular, Brunswick prices were above costs and its rebate policy in no way led to exclusivity, as it did not require boat builders to commit themselves to Brunswick for any specified period of time. Purchasers were free to walk away from the contracts at any time and, in fact, many did switch to competing engine manufactures when better prices were proposed.

The divergent approaches followed in the US and the EU is also illustrated by the Virgin Atlantic v. British Airways litigation. In the first act of the saga Virgin Atlantic challenged, among other things, British Airways’ discounts and loyalty programs. The claims were dismissed on the ground that Virgin had not provided, on a summary judgment, enough evidence to prove that British Airways’ discount schemes had a foreclosure effect.

The second part of the litigation was similarly unsuccessful for the plaintiff. This time Virgin argued that British Airways’ incentive agreements with travel agents (which provided an extra commission payment each time an agent reached a certain sales target) was aimed at introducing additional flights which competed with Virgin routes. Furthermore, Virgin alleged that this was anticompetitive in that caused rivals to lose market shares and also alleged that British Airways bundled routes on which it operated in monopoly with routes with which it was open to competition. The plaintiff claimed that customers flying both on routes on which British Airways held a monopoly and on those on which it faced competition, were prompted to fly with British

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24 Section 1 of the Sherman Act prohibits “every contract, combination in the form of trust or otherwise, or conspiracy, in restrained of trade or commerce.” To prove a Section 1 violation, a plaintiff must show an agreement in the form of a contract, combination, or conspiracy that imposes an unreasonable restrained on trade. See Willman v. Heartland Hosp. E., 34 F.3d 605, 610 (8th Cir. 1994), cert. denied, 514 U.S. 1018, 131 L. Ed. 2d 218, 115 S. Ct. 1361 (1995).

25 Section 2 of the Sherman Act prohibits “monopolizing or attempting to monopolize....any part of the trade or commerce among the several States...”. To establish a Section to violation, plaintiffs must show that: 1) the defendant possessed monopoly power in the relevant market and 2) the defendant willfully acquired or maintained this monopoly power by anti-competitive conduct as opposed to gaining that power as a result of “a superior product, business acumen, or historical accident” (United States v. Grimmell Corporation 384 U.S. 563, 570-71, 16L Ed. 2 d 778, 86 S. Ct. 1698 (1966).

26 For a similar reasoning, see Western Parcel Express v. United Parcel Serv. Of Am., Inc., 190 F.3d 974, 976 (9th Cir. 1999).


28 In particular, Virgin claimed that British Airways’ conduct foreclosed its access to five routes, namely between Heathrow and San Francisco, Washington D.C., Chicago, Los Angeles and New York.
Airways on the competitive routes because of their incentives even on routes where the competing carrier’s service proved less expensive.

The District Court rejected both claims on the ground that Virgin had failed to produce supporting evidence of its allegations and, in particular, the plaintiff had not provided any evidence about the actual incremental revenues induced by the incentive program nor about the actual costs incurred in carrying the additional passengers. Furthermore, Virgin had neither provided any evidence of the effects of British Airways’ incentives on the specific routes on which Virgin claimed to have suffered particular damage. Nor did Virgin prove that the bundled rebates resulted in predatory pricing and that there was a causal link between British Airways’ incentives and the choice not to fly with Virgin. The decision was upheld by the Second Circuit on appeal.

3.1.3 LE PAGE

The much debated Le Page v. 3M decision represents a turning point in the approach towards rebates, although, as discussed below, the position of the Court is similar to the one adopted in Smith Kline v. Eli Lilly.

The case concerned a restrictive pricing practice adopted in the transparent tape market, dominated in the labelled transparent segment by 3M and Le Page, which held a significant market position in the private label segment. In order to reinforce its market position, also partly due to the fact that distribution patterns were evolving so that private label tape was gaining momentum, 3M introduced a massive discount campaign targeted especially at Le Page’s clients. The rebate was offered for the purchase of a variety of 3M product lines and the scheme set customer-specific growth targets in each product line. This resulted in the size of the rebate being linked to the number of product lines in which the targets were met. In turn, the number of targets met by the buyer determined the rebate received on its overall purchases. Consequently, Le Page alleged that the loss suffered (the market share decreased from 14.4% to 9.5%) was a consequence of 3M’s discount scheme.

Virgin’s economic expert (Douglas Bernheim) compared the additional rebate - that would have to be paid as a percentage of additional revenues if customers met the incentive targets by increasing sales - to the average cost of carrying passengers. As remarked by P. Greenlee and D. Reitman (Distinguishing Competitive and exclusionary Uses of Loyalty Discounts, quoted), “since the additional rebates plus the average variable cost of serving additional passengers exceeded the additional revenues that would be earned under the incentive program, [Virgin’s economic expert] concluded that the incremental sales were priced below cost” (p. 446).


Such as Health Care Products, Home Care Products, Home Improvement Products, Stationery Products, etc.
In analyzing the anticompetitive effect of bundled rebates, namely, the foreclosure of “portion of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer”\(^{32}\), the Court quoted SmithKline, and found that the effect of the discount program was to exploit 3M’s monopoly position in labelled tape in order to expand into the private label segment. The file also included evidence showing that 3M was determined to force Le Page out of the market and to subsequently raise prices.

The Court held that the Brooke Group test could not apply in multi-product settings. It then ruled that the discount scheme created the same effect of an exclusive dealing contract, which, given 3M’s monopoly position, was to be considered in breach of § 2 of the Sherman Act.

In reaching this conclusion, the Court applied a test based on the substantial evidence of the exclusionary effects created by the scheme, such as the considerable amount of the discounts offered, testimony of purchasers, and internal documents showing 3M’s “predatory” intent. Interestingly enough, the dissent opinion criticized the majority conclusion, quoting evidence showing that Le Page was an inefficient competitor and its market shares were decreasing because of factors other than 3M’s discount scheme.

It would appear that Le Page does not really represent an assessment of rebates as such, as it can be argued that 3M’s price schemes had, in effect, a foreclosure effect on competitors. Whether this was the consequence of legitimate competition or it was rather part of a much wider anticompetitive strategy set in place by 3M to the detriment of its competitors (especially Le Page) is a matter of opinion. On hearing the evidence produced at the trial, the Court of Appeals for the Third Circuit concluded it was apart of a wider anticompetitive strategy. However, an important aspect of the judgment is the focus on the non-replicability of the price scheme, not at an economic level, but on the diversity of the bundle of products offered, which is an aspect already emphasised in Smith-Kline v. Lilly.\(^{33}\) This point will be discussed further below.

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\(^{32}\) Emphasis added.

\(^{33}\) A similar point has been raised by the Commission in the assessment of the competitive effects of conglomerate mergers (so-called ‘portfolio power’). In particular, in the context of consumer products, the Commission has claimed that the combination of different brands through portfolio power could operate a barrier to entry. See, for example, Case M. 938, Guinness/Grand Metropolitan, [1998], O.J.E.C. L 288/24, §§ 38-42. Case M. 774, Saint Gobain/Wacher-Chemie/NOM, [1997] O.J.E.C. L 247/1. The portfolio power offence was raised also in sectors different from consumer products. For instance, in GE/Honeywell, the Commission held that due to the combination of GE and Honeywell’s products the merged entity would have been capable of offering packages of products and services not replicable by rival firms (Case M.2220, [2004] L 48/1, § 350).
3.1.4 Post-Le Page Case Law

The Supreme Court’s decision to decline 3M’s petition for certiorari has not ended the debate on bundled rebates in the US. On the contrary, the post-Le Page era has been characterised by an intense antitrust litigation initiated by competitors that challenged the monopolist’s discount schemes. In some judgments the approach applied by the Third Circuit in Le Page has been seriously questioned.

In JBDL v Wyeth-Ayerst Laboratories34 (“Wyeth”), it was alleged that Wyeth, holding market power in the manufacturing of conjugated estrogens (Premarin), had limited consumers’ access to a product competing with Premarin. In particular, in order to maintain Premarin’s exclusive position as a conjugated estrogen, Wyeth conditioned the discounts to the purchase of Premarin and of other Wyeth drugs. JBDL argued that the described covenant had an exclusivity effect that caused pharmacies to be unwilling to risk their rebates on a wide range of products; the district court in Ohio rejected this claim on several grounds. The court held that when dealing with practices widely recognized as pro-competitive such as price-reducing rebates, the standard to be met in order to prove a foreclosure effect is high; furthermore, Wyeth’s exclusivity clause did not prevent pharmacies from buying competing non-conjugated estrogens. In conclusion, the court remarked that the ruling in Le Page had the effect of favouring a less efficient competitors35 and of precluding legitimate price cutting that benefited consumers.

A reversal of Le Page is also to be found in Masimo v. Tyco Health Care Group LP (“Masimo”) in which Masimo alleged violations of antitrust laws against Tyco in the pulse oxymetry product market. The plaintiff claimed that Tyco had used its dominant market position to prevent hospitals from purchasing Masimo’s pulse oxymetry products through exclusive or de facto exclusive contracts with hospitals. While the court denied Tyco’s motion for summary judgment, the trial court set aside the jury’s finding on the plaintiff’s bundling claim. The court held that the plaintiff had failed to provide sufficient evidence as to the presumed anticompetitive effects of the bundling. In particular, the judgment disregarded Le Page by stating that, in the absence of predation or of tying, a company offering a discount on a bundle of products ought not to face liability under Section 2 of the Sherman Act.

34 485 F.3d 880.
35 This was the dissenting opinion’s approach in Le Page. See above § 3.1.3.
The possibility of at least one firm competing with the same bundle of products as an element to exclude liability under the *Le Page* standard is discussed in *Invacare Corp. v. Respironics, Inc.*[^36] and in *Applied Medical Resources Corp v. Ethicon Inc et al.* ("*Ethicon*"). Invacare and Respironics both manufactured medical devices to treat obstructive sleep apnea, so-called PAPs (positive airway pressure[^37]). Invacare challenged Respironics’ practice of selling its PAPs and masks in low-priced bundles to sleep laboratories[^38].

The court granted Respironics motion for summary judgment on the monopolization claims primarily on two grounds. The predatory pricing charge was unfounded as a matter of law, as Invacare had not proved that Respironics priced below an appropriate measure of its costs; moreover, as a matter of fact, although Respironics did admit that it supplied hundreds of thousands of masks for free to sleep laboratories, sales to sleep laboratories did not constitute a relevant market, and thus the court dismissed Invacare’s predatory pricing claim. The court held that selling at prices below cost only to some customers in the overall market did not state a predatory pricing claim.

The court also dismissed Invacare’s claim based on Respironics’ use of bundled discounts for customers that purchased both PAPs and masks. The court distinguished Invacare’s claims from those of the plaintiffs in *Le Page*, where a monopolist allegedly bundled monopoly and non-monopoly products and prevented competitors selling the non-monopoly product from competing on an equal footing. In this case, instead, Invacare and Respironics (as well as other competitors) sold both PAPs and masks (and several other companies bundled them together) and, thus, Invacare was able to compete with Respironics by selling the same bundle. The court also noted that Invacare did not contend that the PAP/mask bundles sold by Respironics were priced below cost.

Similarly, *Ethicon* stands for the importance that competition from rivals’ bundles plays in out a Section 2 liability under the *Le Page* standard. The case involved bundled sales by Johnson & Johnson ("*J&J*") of sutures and endomechanical products by providing lower prices on sutures only to those hospitals that committed to purchase large quantities of both types of products from J&J. The jury issued a verdict stating that J&J had not engaged in exclusionary conduct, as it faced

[^37]: These devices blow air through a hose into a mask worn by the patient during sleep.
[^38]: Patients with OSA often go to sleep laboratories for diagnosis and treatment, and may first test and be prescribed masks and PAPs at these laboratories – making the laboratories an important gateway to the market.
competition on the bundle of products from US Surgical; it also held that the bundled rebates resulted in lower prices for purchasers.  

A further reversal of Le Page is to be found in the Ninth Circuit decision in Cascade Health Solution v. Peace Health, where, in rejecting the standard set by the Third Circuit, the court states that:

“To prove that a bundled discount was exclusionary or predatory for the purposes of a monopolization or attempted monopolization claim under Section 2 of the Sherman Act, the plaintiff must establish that, after allocating the discount given by the defendant on the entire bundle of products to the competitive product or products, the defendant sold the competitive product or products below its average variable cost of producing them”.

3.2 EU CASE LAW

3.2.1 INTRODUCTION

The case law of the European courts and the decisional practice of the Commission on abuses and in particular on discounts is not particularly developed. The Commission has pursued only a few cases and even fewer have been litigated before the CFI or the ECJ. The Commission and the EC courts have showed a rather formalistic approach often based on mere assumptions rather than on the analysis of the effects of the conduct. This line of reasoning was also confirmed by the most recent decisions issued by the Commission and the ECJ as discussed in this section.

3.2.2 EARLY CASES

A first line of cases, with the exception of Michelin I, did not deal exclusively with discounts as such, but the rebate was just one of the practices put in place by the dominant firm to tie-in customers. In these cases, the exclusionary intent of the practice was less controversial, as it resulted from documental evidence or from specific advantages granted to customers exposed to competition.

39 In re Hypodermic Products Antitrust Litigation [No. 05-CV-1602 (JLL/CCC) (D. N.J. June 29, 2007)], a district court of New Jersey denied Becton’s motion to dismiss three class action complaints challenging its use of loyalty rebate programmes in connection with the sale of hypodermic needles. The complainants claimed, inter alia, that the defendant’s purchasing programs, through which Becton was bundling the sale to healthcare agents of different product lines bundled together and was offering considering financial benefits in exchange of exclusivity had a foreclosing effect on rival firms. In particular, since many of Becton’s competitors were smaller, specialized companies that sold fewer products, and in some instances only a single product, they were unable to profitably match Becton’s structured offers across product lines. These arguments were accepted by the district judge.

40 479 F.3d 726, 727 (9th Cir. 2007).
Hoffmann-La Roche\textsuperscript{41} was one of the first decisions where the compatibility of a rebate system with Art. 82 was called into question. The case concerned a series of practices, including exclusive supply obligations, so called “English Clauses”, and discriminatory sale conditions. In particular, the discount schemes set in place by Hoffmann-La Roche provided for either a fixed rebate which was dependent on the quantity purchased or a progressive rebate proportional to the percentage of the purchaser’s requirement that was bought from Hoffmann-La Roche. The Commission, upheld by the ECJ, denied the quantitative nature of the progressive rebate and found that it constituted a “specially worked out form of fidelity rebate”.\textsuperscript{42} Since the discount increased with the quantities bought from Hoffmann-La Roche, it represented a powerful incentive to obtain the maximum percentage of its requirement from the dominant firm and had the effect of excluding competitors.\textsuperscript{43}

Michelin \textsuperscript{44} dealt with a system of discounts granted by Michelin to its tyre dealers which was based on the dealers’ turnover of Michelin tires in the previous year. The variation in the discounts granted were limited (between 0.2% and 0.4%), but the criteria to qualify for a discount were not known in advance by the dealer. While Michelin justified the rebate system arguing that it allowed to better plan its production process, the Commission held that the calculation of the rebate over a long reference period (one year) had the effect of increasing pressure on the buyer to “reach the purchase figure needed to obtain the discount or to avoid suffering the expected loss for the entire period.”\textsuperscript{45} The ECJ also held that the pressure on the dealers was increased by the lack of transparency of the system, in particular, by the fact that the rules changed frequently and such changes were not communicated in writing to the dealers, creating uncertainty as to the predictability of their targets.\textsuperscript{46}

British Gypsum\textsuperscript{47} is only partially a rebate case. It dealt with several practices: exclusive supply, prior delivery of products to certain customers and quantity rebates granted to buyers who were not importing plasterboards. The CFI upheld the Commission’s finding of the abusive nature of the exclusive supply clauses as well as of the priority delivery obligations; the latter were entered into with clients not dealing with competing suppliers and, therefore, they had a clear foreclosure nature. The same conclusion was attained with regards to quantity rebates as they aimed at the exclusion of foreign suppliers. Documentary evidence proving the exclusionary intent of the scheme was also

\textsuperscript{41} Judgment of 13 February 1979, Case 85/76, [1979], p. 461.
\textsuperscript{42} § 98 of the Judgment.
\textsuperscript{43} § 100 of the Judgment.
\textsuperscript{44} Judgment of 9 November 1983, Case 322/81, [1983], p. 3461.
\textsuperscript{45} § 81 of the Judgment.
\textsuperscript{46} § 83 of the Judgment.
\textsuperscript{47} Judgment of 1 April 1993, Case T-65/89, [1993], p. II-389.
taken into account in the Commission’s and the CFI’s assessments. It is worth emphasising that, contrary to *Michelin I* and *Michelin II*, the discounts were granted on the basis of anticipated annual turnover targets.

*Irish Sugar* concerned a combination of pricing and other commercial practices put in place by Irish Sugar which had approximately 90% of the Irish market. In particular, by granting rebates to customers intending to export their final product to other Member States, Irish Sugar was found to have discriminated vis-à-vis its industrial customers. The discrimination was aggravated by the fact that the level of the rebate varied according to the customer concerned, the period in question, or the Member State towards which the export was directed. Irish Sugar was also deemed to be applying discriminatory “border rebates”, which were, in effect, granted to customers who because of their proximity to the border were exposed to competition from other Member States imports. The CFI strongly criticised this form of “meeting competition” although in *Eurofix-Bauco/Hilti* (as well as in other cases), Hilti was permitted to engage in price reductions to meet competition from rivals.

In addition, Irish Sugar was found to have applied an abusive scheme of fidelity rebates to clients who met certain sales objectives; as a result, some of the targeted customers refrained from purchasing from competing suppliers.

Furthermore, Irish Sugar was also found to be applying a system of selective discounts targeted at customers of competing sugar packers. These rebates were based on the customers’ purchases from Irish Sugar, calculated over a reference period of six months (April-September 1993), and structured in a way that the reference period started before the launching of new brands of sugar by competing manufacturers. Finally, border rebates were abusive in that they were not justified on economic grounds, such as for instance economies of scale linked to the sales volumes. The rebates were instead applied when the price difference between Northern Ireland and Ireland was such as to induce cross-border sales.

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48 A similar position is expressed in the Discussion Paper (§ 176).

49 Commission’s Decision 88/138, of 22 December 1987, [1988] O.J.E.C. L 65/19. In the Annex, including the Undertakings submitted by Hilti, it can be read: “*Hilti AG, for itself and on behalf of its wholly-owned subsidiary companies in the EEC, undertakes in good faith: (…) (b) to implement, for direct fastening products, in a manner consistent with the undertakings contained in (a) and subject only to the three exceptions listed below, a discount policy based on precise organic and transparent quantity/value discount schedules applied uniformly and without discrimination; The three exceptions referred to above are: (i) meeting a competitive offer”(...).

50 The Commission had also found abusive the fact that Irish Sugar had agreed with one wholesaler and one retailer to swap competing retail sugar products for its own product under the threat of a withdrawal of the preferential discounts hitherto granted to them, thereby preventing new products being resold at competitive conditions and consolidating Irish Sugar dominant position (§§ 226-234).

51 See § 173 of the Judgment.
aware of the possible anticompetitive nature of the rebate schemes. The fidelity rebates were also condemned because they were set as to cover the whole of the customers’ purchases and, as a consequence, resulted in the customer not purchasing from competing suppliers.

In Compagnie Maritime Belge, an issue of rebates and predatory prices was similarly involved. A liner-shipping conference (Cewal), found to be collectively dominant, was charged with setting in place anticompetitive exclusionary pricing practices, so called “fighting ships”, as well as other related practices. The abuse consisted in placing a vessel on berth alongside the outsider vessel, charging at the same time lower rates than those of the outsider and distributing the losses suffered by the fighting ships among the members of the conference. The peculiar feature of Compagnie Maritime Belge is that a different ruling, a rather cryptic one, was rendered on unconditional price cuts. While the rule under the Akzo test is that price below average variable costs are presumed abusive and prices above average variable costs but below average total costs may be abusive when they are part of a plan to eliminate a competitor, the finding of the Community courts in Compagnie Maritime Belge was that even price cuts above average total cost might, in exceptional circumstances be abusive, depending on the characteristics of the case.

3.2.3 The Most Recent Cases: Michelin II and British Airways

Michelin II is a pure rebate case and concerned several discount schemes. Michelin set in place a quantity rebate system which provided for an annual refund expressed as a percentage of the turnover achieved by the dealer with the applicant; the discount rate increased gradually according to the quantities purchased. Michelin also allowed an invoice rebate and an “end-of-the year” rebate. Under the first system, rebates were granted on the basis of the number of new products purchased in the three previous years. Dealers wishing to obtain a larger invoice rebate were required to sign a contract taking into account increased sales targets. The “end-of-the year” rebate was attributed to dealers that managed to reach a specific turnover target in terms of sales of Michelin’s tyres as compared to sales of competing tyres, and who achieved significant sales in certain product categories.

52 Judgment of 16 March 2000, Joined cases C- 395-396/96 P.
53 See also Commission’s Decision 35,141 of 10 March 2001, Deutsche Post AG, [2001] O.J.E.C. L 125/27. The case dealt, inter alia, with a system of fidelity rebates set in place by Deutsche Post which conditioned the granting of the discount on the customers entrusting all (or nearly all) of their mail orders to Deutsche Post.
54 § 7 of the Judgment.
55 §§ 14 and 16 of the Judgment.
The abusive nature of the rebate scheme focused on two main elements: the calculation of the discount on the dealer’s entire turnover with Michelin and the length of the reference period - one year.\(^{56}\) As to the second element, the CFI recalled the rule already established in *Michelin I*, according to which the use of a long reference period to calculate the discount has the effect of increasing the pressure on the buyer to reach the sales target. From such a perspective, the scheme scrutinized in *British Gypsum* was different in that the rebates granted were determined on the basis of the anticipated annual turnover and not on the basis of the actual turnover. The result being that there was no readjustment of the discount for a customer whose annual turnover was lower than that initially anticipated; thus, there was significantly less pressure on the buyer to make additional purchases.

The calculation of the discount on the basis of the overall dealer’s turnover was found to be abusive in that it created a greater incentive on the dealer to purchase from Michelin as compared to the case where the discount was calculated ‘by tranche’. Indeed, while in a scheme in which the discount calculated ‘by tranche’ the discount is granted only on the extra units purchased, the effect of the overall turnover discount is to reduce the price of the whole amount purchased in the reference period. In addition, a further element of pressure was added by the significant variation in the discount rates between the lower and the higher steps.

As to the existence of any justification for the discount scheme, the CFI found that Michelin had not established that the scheme was efficiency-related, for instance, discounts were not based on cost savings linked to economies of scale.\(^{57}\) The Commission also challenged a further discount by Michelin, a “service bonus system”, which allowed the dealer to obtain a certain amount of points on the basis of which rebates were awarded depending on the commitments entered into in a number of areas. Points were based on the services provided by the dealer - for example promotional services or the supply of statistical data - and on the sales of Michelin products in the specific region where the dealer was placed, i.e. not a quantity discount.\(^{58}\) If a given threshold was exceeded, the dealer was entitled to receive a bonus corresponding to a percentage of the turnover achieved with Michelin.

The Commission challenged the service bonus on two grounds. First, the system breached Art. 82 in that Michelin had a too wide margin of discretion in assessing compliance by the dealers with the

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\(^{56}\) Shorter reference periods have been in general considered compatible with Art. 82. See, for instance, the *Coca-Cola* case, where a reference period of three months was accepted (XIXth Report on Competition Policy, §50).

\(^{57}\) See § 108 of the Judgment.

\(^{58}\) § 115 and followings of the Judgment.
commitments entered into and thus, in granting the discount. The Commission found that such “subjectivity” was unfair, and, therefore, abusive, since too much pressure was put on the dealer. Second, the system was loyalty inducing, in that the points to be earned by the dealer were linked to its capability to match or exceed the forecast sales of specific Michelin products. While the court recognized that the target set were not onerous to meet, it stated that, “it cannot be denied that, through the commitment in question, the applicant, by granting a financial advantage, sought to prevent dealers from obtaining supplies from rival manufacturers” (§ 160).  

**British Airways** 60 concerned a system of incentives established by British Airways with their travel agents in the United Kingdom, which allowed agents to receive payments in addition to their basic commission. Different types of discounts were under scrutiny:

(i) a performance reward scheme, calculated on a sliding scale and based on the extent to which a travel agent increased its sales of BA tickets from one year to the following;

(ii) an additional commission related to the growth of BA’s share in their worldwide sales;

(iii) a further bonus calculated on the basis of the amount of BA international and domestic tickets sold. 61

As in **Michelin II**, the Commission challenged the structure of the scheme, namely the fact that once the threshold triggering the rebate was passed, the rebate was granted on all the sales made in the relevant period and not only on the incremental tickets purchased after the threshold was reached. The scheme had multiple effects. It implied a strong loyalty inductive effect on sales close to the thresholds: “when a travel agent is close to one of the thresholds for an increase in commission rate selling relatively few extra BA tickets can have a large effect on his commission income”.62 This meant that a competitor wishing to give a travel agent an incentive to divert some sales from BA had to offer a very high commission, which covered and possibly exceeded the discount given on all the BA tickets sold in the reference period. Moreover, the scheme also had the effect of discriminating between travel agents. The court even discussed the justification of the discount scheme in terms of efficiencies arising out of the reduction in the number of unsold seats and rejected such argument, holding that: “the consideration for ticket sales carried out by an agent once the latter’s sales growth target had been reached represented an additional cost, in the form

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59 The case was confirmed on appeal by the Court of Justice (Judgment of 15 March 2007, Case C-95/04 P, not yet reported).
61 §§ 9 to 17 of the Judgment.
62 § 23 of the Judgment.
of retrospective application of the increased commission to all BA tickets sold during the reference period in question, which was liable to be equal to, or greater than, that profit”. 63

The CFI’s judgment was appealed before the ECJ and Advocate General Kokott in her opinion proposed to dismiss the appeal. Two aspects are worth mentioning for the purposes of our analysis. First, Advocate General Kokott suggested that individual sales targets cause competition concerns not only because of the amplified effect they produce in that they are linked to the travel’s agent overall sales, but also because of the very essence of the target. In other terms, “if a contractual partner is offered a rebate or bonus for achieving over a given reference period the same, or a higher, turnover in the dominant undertaking’s products than in the comparable period of the preceding year, even a partial switch to products of competitors can become less attractive for him. In this way, the dominant undertaking can exercise pressure on its contractual partners and bind them to itself”. 64 As we shall see further, there are settings in which target rebates not only are justified, but might be even pro-competitive (see Section 2 and 4).

Second, the Opinion is unclear on the issue of the length of the reference period. While recalling that the foreclosure effect of a rebate scheme has to be assessed in light of all the circumstances of the particular case, Advocate Kokott states that one has to look at both the length of the of the reference period in absolute terms and how far back the relevant period for comparison lies. In this respect, “one cannot exclude the possibility that even a system in which reference is made month by month to periods lying one year back will, on account of the continual incentive it gives to increase the turnover, result in long-term binding of the contractual partner to the dominant undertaking, making it hard for him to switch to the competition”. 65 This element seems to have been overcome in the Discussion Paper, since the Commission does not consider that the length of the reference period is important in establishing the loyalty inducing effect of the rebate program. 66

The case was decided on 15 March 2007 and the ECJ dismissed the appeal upholding the CFI’s analysis. It is worth noting that when dealing with the alleged discrimination in relation to travel agents, the court stressed that the standard of proof to be met in order to substantiate a

63 § 289 of the Judgment.
64 § 48 of the Opinion.
65 § 95 of the Opinion.
66 See § 161 of the Discussion Paper. Moreover, according to Rigaud, “the length of the reference period does not allow any conclusions with respect to switching costs. As a result, the length of the reference period cannot be considered as a suitable indicator for sound competition policy because the quantities associated with a certain reference period will vary across industries” (F. P. Maier-Rigaud, Switching Costs in Retroactive Rebates – What’s Time Got To Do with It? (Working Paper 2005).
discrimination claim under Art. 82 (c) does not require proof of “an actual quantifiable deterioration of the business partners taken individually”; it is sufficient to provide evidence that “the behaviour of the undertaking in a dominant position tends, having regard to the whole of the circumstances of the case, to lead to a distortion of competition between those business partners”.

3.3 **CONCLUSIONS ON THE EU AND THE US APPROACHES**

The analysis shows that the US cases before *Le Page* were more focused on consumer harm rather than on competitors’ harm. The first cases reveal a lenient approach vis-à-vis price competition. Not only is the competitors’ harm test applied, but is also endorsed in a strict version: in order for a discount scheme to be condemned, the effect of the conduct must be the eviction of competitors from the market. Any other outcome on competitors has been considered as incompatible with the existence of foreclosing effects.

While in the EU the assessment of compatibility of a discount scheme with competition rules is mainly based on a presumptive analysis, less emphasis is put on the burden of proof and so, the competitors’ harm standard is not endorsed. We shall see that a different approach was suggested by the Discussion Paper (see Section 4), although in the first rebate case following the adoption of the paper the Commission seems to be still following a rather formalistic approach. This explains why a great deal of focus is placed on the use of rebates as a means to attain exclusivity, which under specific circumstances is prohibited in the EU if set in place by dominant firms.

Even if this approach might prove correct and convenient from a enforcement policy standpoint in cases where the discount scheme has the only aim of foreclosing rivals (see the cases on discounts granted to clients exposed to imports from other countries), there is, nevertheless, a wide range of circumstances in which it is unconvincing. In some cases, competition from rival firms is not precluded and the only result of applying a formalistic approach is to chill the most genuine acts of competition. We discuss the issue in Section 5.

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67 See § 145 of the Judgement. The same reference to the “tendency” to restrict competition, although through a more indirect wording, is also found in *Michelin II* (§ 59), *Hoffmann La-Roche* (§ 90), *Irish Sugar* (§ 114).
4. THE DISCUSSION PAPER AND RECENT EU DECISIONAL PRACTICE

4.1 INTRODUCTION

The above analysis shows that the central tenet in the assessment of rebates, that is, the use of the competitors’ harm test, has been applied differently in the EU and the US. As outlined earlier, one might even argue that, before the Discussion Paper, in the EU the evaluation of discounts was not based on a real effects-based test, since both the Commission and the European courts have preferred an assumption-based approach.

From this perspective, we have seen that that the case law on Article 82, in general, and on rebates in particular, has evolved unsatisfactorily. European courts have developed arguments which were at times unclear and confusing and often based on a formalistic approach rather than looking at the effects of the practices. This has led to the perception that EC legislation applies not only to conducts which are abusive but also to pro-competitive actions, when they are set in place by large companies which are deemed to be in a dominant position.

It is for this reason that the Discussion Paper represents a substantial effort by the Commission to define a consistent approach in the analysis of highly debated topics. However, while the Commission tries to overcome some of the difficulties created by the case law, it is submitted that there is still room for improvement in the methodology used with regards to both the general approach followed in assessing exclusionary discount practices and the way in which effect is measured.

4.2 THE MODEL FOR THE ASSESSMENT OF REBATES PROPOSED BY THE DISCUSSION PAPER

4.2.1 THE TEST ENDORSED BY THE DISCUSSION PAPER

Before analysing in detail the model for the assessment of rebates proposed in the Discussion Paper it should be mentioned that, from a more general enforcement policy standpoint, the Commission identifies the “central concern” in the assessment of exclusionary conducts as the need to prevent abusive behaviour which results in harm to consumers. As pointed out, “[t]he central concern of Article 82 with regard to exclusionary abuses is thus foreclosure that hinders competition and

68 §§ 54, 55 and 56.
thereby harms consumers”.69 This approach reflects the general view that the main focus of competition laws should be the protection of the competitive structure of the market in order to preserve and enhance the welfare of consumers. As widely recognised, though, the introduction of the consumer welfare standard involves that, from a practical point of view, enforcement policies should be based on the application of a strict standard of evidence, based on the identification of harm to consumers.

In this regard, while the Discussion Paper correctly identifies the main objective as the protection of consumer welfare, the method suggested to appraise the restrictive nature of abuses raises some doubts. In fact, rather than evaluating the practice on the basis of the harm it produces to the consumer welfare, the Commission classifies a series of commercial practices that are presumed to lead to the exclusion of an as efficient competitor.70 These conducts are, as we shall see below, presumed abusive unless objectively justified or based on efficiencies motives. It appears, therefore, that the Commission is reintroducing the same approach endorsed by EU case law.

4.2.2 THE “AS EFFICIENT” COMPETITOR TEST

A formalistic approach may be criticised if one considers that there is a whole series of conducts, such as for example rebates, which imply a prima facie benefit for the consumer. The Discussion Paper deals with this problem by introducing an effect-based approach: the “as efficient” competitor test.

However, if exclusion of a competitor is the standard and the “as efficient” competitor test is ill-defined, there is a risk that lawful rebates are considered restrictive, which might entail the protection of less efficient companies. In this respect, the central problem is how the notion of the “as efficient” competitor proposed in the Discussion Paper is defined. This issue is linked with that of the competitors’ harm test which we discuss in Section 5.

One of the limits of the notion of the “as efficient” competitor suggested by the Discussion Paper is the definition of barriers to entry which are used to characterise a market and to examine whether competition is effectively restrained.71 This element is of particular relevance in our analysis, because of the central role of the “as efficient” standard in the definition of anti-competitive effects. The Commission includes among the “exogenous” barriers to entry also economies of scale and

69 § 56. This point was first raised in Europeamballage and Continental Can (Judgment of 21 February 1973 Case C6-72 §26) and then recalled in British Airways (§106).
70 § 63.
71 § 34-40.
financial strength. One should, therefore, think that these elements are factored out when evaluating the size of the “as efficient” competitor. This may lead to finding abuses even in practices that would be justified in cases where competition is defined as taking into account a competitor enjoying a corresponding level of financial strength and economies of scale and not instead a less efficient one.

As regards rebates specifically, one must recognize that the Discussion Paper goes a long way to tackle the issues left open by the case law in terms of economic analysis of the instances in which rebates lead to exclusion. Indeed, besides introducing for the first time an effect-based approach, the Discussion Paper provides a detailed analysis of the method to be used to calculate the foreclosing effects of discounts on rival firms. \(^2\) Basically, this consists in determining a “commercially viable” portion of supplies that is to be left open to competition. The idea is to examine the effect of the rebate policy on the price which should be offered by a competitor willing to conquer its share of the market. If this is lower than costs, then the rebate is held exclusionary.

While this criterion is very ingenuous and draws a benchmark for the analysis which until now was missing in the case law, it crucially depends on the share that the new entrant is assumed to acquire to enter the market. The lower the share, the higher will be the impact of rebates on the firm attempting entrance, and the more likely the restrictive effect of the rebate. In this respect, assuming that a competitor is unable to “compete for an individual customer’s entire demand”\(^3\) the Commission calculates the portion of sales that should be “contestable”. It is argued that if such shares are calculated in a too restrictive way, i.e. they are too small, this will unjustifiably enhance the effect of even a legitimate discount policy. In other words, if, given its size, a competitor can acquire just a limited portion of a customer’s demand, the price that will have to be offered in order to compensate the last discount on its overall sales will have to be particularly low; which would lead to a challenge as anti-competitive any discount policy. Therefore, one might wonder whether the methodology used by the Commission could be considered as having the effect of sheltering less efficient firms from legitimate competition.

It is further submitted that the calculation of small “viable shares” is also linked to the conservative notion of “as efficient” competitor endorsed by the Discussion Paper. In principle, if, as suggested, economies of scale and scope, and financial strength are not considered barriers to entry (see above, Section ii of the General Remarks), the result may be that the “as efficient” competitor would be

\(^2\) §§ 152 to 171.

\(^3\) § 154.
able to bid for larger “viable shares” of sales, with the consequence that the room for legitimate rebates policy would increase. This is clearly shown by the outcome of the Tomra case.

As for bundled discounts, the rule proposed in the Discussion Paper is that a rebate does not threaten competition if the incremental price that customers pay for each of the products of the bundle is above the long run incremental costs of the dominant company. In this case, an equally efficient competitor that supplies only some (or one) of the products/services in the bundle should be able to compete with dominant firm.

4.3 **THE TOMRA DECISION**

The Tomra case was of particular interest to the antitrust community as it was the first EU rebate case after the publication of the Discussion Paper. Tomra, a Norwegian manufacturer of reverse vending machines was found to be dominant in several national markets, where it held a market share of approximately 80%. The contested behaviour included several practices, notably exclusivity agreements, individualised quantity targets tailored to customers’ needs so as to cover its overall requirements, and retroactive rebates. During the period in question (i.e. between 1998 and 2002), both Tomra’s market shares and those of its competitors remained quite stable. The Commission also acknowledged that there had been no successful entry in the market, but rather, on the contrary, certain competitors had left as a result of insolvency or of acquisitions.

In particular, the Commission analysed the position of competitors and of the price they would have to pay in order to win the contestable part of demand and applied the competitors’ harm test envisaged in the Discussion Paper. Although the details of the decisions are not yet available, we try to analyse the conclusions reached by the Commission.

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74 Long run incremental costs, for this purpose, include all costs incurred to supply a specific product/service, with the exclusion of common costs.

75 For an application of the notion of long run incremental cost as a standard to assess unlawful cross-subsidization, see the Commission’s Decision IV.35.141, *UP/Deutsche Post*, of 23/3/2001, OJ L 125, 05.05.2001, p. 27. See also the OFT decision of 17/12/2002, *BskyB*, CA98/20/2002. The Modernization Commission proposed to found the assessment of bundled rebates on a similar test. The Commission has in fact suggested that courts should challenge multi-product discounts if the following conditions are satisfied: “(1) after allocating all discounts and rebates attributable to the entire bundle of products to the competitive product, the defendant sold the competitive product below its incremental cost for the competitive product; (2) the defendant is likely to recoup these short-term losses; and (3) the bundled discount or rebate program has had or is likely to have an adverse effect on competition” (Antitrust Modernization Commission, Report and Recommendations, April 2007, p. 99)

76 As of 8 October 2007, the text of the decision was not yet published. The decision has been challenged before the CFI (ase T-155/06).
One might wonder whether even if some players have left the market as a result of acquisitions, this does not necessarily mean that they are not active anymore. Similarly, the status of insolvency is not incompatible with the permanence on the market.

A second problem lies with the calculation of the price that competitors should practice in order to compete away from Tomra the contestable part of the demand. The calculation measures the price that would make the customer indifferent between buying from Tomra or from a competitor. This is the unit price that the competitor has to offer to compensate the customer for the discount he would forego by not meeting the discount threshold. The Commission’s reasoning is summarised by the following passage:

“For simplicity imagine a situation where demand is indeed above the threshold, i.e. demand is 120 and the threshold is 100. The base price $p$ is assumed to be 1 and the rebate is 10%. Tomra now considers the worst case scenario, where a customer has bought 99 units from Tomra at a price of 1 and thus requires 21 more units by definition. Tomra now claims that the unit price a competitor would need to offer to make the customer indifferent between that competitor and Tomra is $(21 \times .9 - 99 \times .1)/21 = 3/7 = 0.43$ (16), a price that may well be above cost and feasible for any competitor. Unfortunately, it is far from clear why a competitor would want to do so to begin with. Assuming profit maximizing behaviour on the part of the competitor, it would make much more sense to forego the last unit and sell only 20 units at a price of .9 for total revenues of 18.”\textsuperscript{77}

On the basis of the above assumptions, the Commission concludes that a rational profit-maximizing competitor would give up the sale of the last unit of product, the unit that if the customers stay with Tomra triggers the application of the discount, in order to sell the remaining 20 units at a higher price.

The problem we encounter with such reasoning is that as outlined in Section 4.2, if the calculation of the price is made on a very small part of contestable demand, in the Commission’s case, 21 units, the price that the competitor would have to bid in order to win sales from the dominant firm would be particularly low (0.43). If, on the contrary, the same calculation is made on a larger part of demand, the resulting price that the competitor would have to apply would be higher, and, thus more reasonable. For instance, supposing that the contestable part of demand were 41 units, the

\textsuperscript{77} See Maier-Rigaud, Vaigauskaite, Prokent/Tomra, a textbook case?, quoted, p. 23.
resulting unit price that the competitor would have to bid is 0.7. Moreover, as the unit price increases, the bigger the share of contestable demand.

The above seems to suggest that the competitors’ test suggested in the Discussion Paper and endorsed in Tomra is a rather flimsy. The result of calculating the price that a competitor has to pay on a very small part of contestable demand could well have the effect of sheltering inefficient firms from legitimate price competition.

\[\frac{(41 \times 0.9 - 79 \times 0.1)}{41} = 0.7.\]

Indeed, in such case the calculation would be: \( (41 \times 0.9 - 79 \times 0.1) / 41 = 0.7. \)
5. FINDING THE APPROPRIATE ENFORCEMENT MODEL: EFFECT-BASED VS. PRESumptive APPROACH

The discussion so far shows that there are several unsolved issues in the assessment of dominant firms’ pricing policies and they have been addressed differently in both the EU and US. With the assessment of unconditional rebates and on the role of the competitors’ harm standard as a focus, we claim that such standard should be used in the EU as it was in the US prior to Le Page. Indeed, the ruling in Le Page puts the assessment of rebates based on the competitors’ harm test on much weaker grounds, in that the Court seems to have preferred a presumptive approach. In this section, we identify several instances in which a presumption based approach proves problematic from an economic perspective and where instead the use of the competitors’ harm test allows to identify lawful conducts.

5.1 STRAIGHTFORWARD CASES

As a starting point, there are settings in which the anti-competitive object of the rebate scheme can be easily deduced from its structure and there is no doubt that such measures should be condemned. This is, for example, the case of BPB Industries, in which rebates were granted to customers who were not importing plasterboard from rival suppliers or of Irish Sugar, in which buyers intending to export their final product to other Member States – and so not competing with Irish Sugar – benefited from the discount. In such cases, the approach followed in the EU entails no burden of proof of any exclusionary effect, since the ‘restrictiveness’ of the practice lies in its object. One could speculate whether in the US, even such cases, would be judged under a rule of reason method.

A further tenet is that linear pricing, or so-called “volume” or “quantitative” discounts, do not necessarily raise antitrust concerns, for two sets of reasons. First, because the price paid is only function of the quantities purchased; the discount is unconditional on the buyer’s purchasing

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80 For an example of standard volume rebates considered compatible with Art. 82, see Interbrew (IP/04/574, Commission closes probe concerning Interbrew’s practices towards Belgian beer wholesalers). In this case, Interbrew had set a discount scheme which the Commission considered abusive as it lacked of transparency. The discount was paid on invoice for the volumes of each category of beer purchased by the wholesaler in the course of the calendar year following the reference period. In particular, wholesalers only knew he discount rate corresponding to the volume range in which their own purchases for the various types of beer happened to fall and the rates corresponding to the volume ranges situated just above and just below that range. The Commission required Interbrew to make know to all wholesalers all rates applicable to all volume ranges.
behaviour, for example, on the buyer satisfying a specific amount of its requirements with the supplier. This element is of relevance in the approach followed in Europe because, under a pure volume discount, buyers are not subject to any pressure in order to satisfy their requirements with the dominant firm and, in addition, there is no uncertainty as to the price they will finally get to pay.

Second, quantitative discounts are presumed lawful as they reflect economies of scale incurred by the supplier in selling larger quantities. It is, thus, considered legitimate for the dominant firm to transfer downstream cost savings obtained at the research, production or distribution stages.

5.2 **EXCEPTIONS TO STRAIGHT FORWARD CASES**

There are, however, exceptions to this general rule, since as emphasized by the Commission, even unconditional rebates can serve an exclusionary purpose, i.e. they can have an exclusionary outcome. This is when reductions in price result in predation.

Moreover, a problem might arise if the discount scheme is tailored to the buyer’s needs so that its overall requirements are fulfilled by the dominant firm alone, this has the same effect as an exclusivity covenant. In this respect, the EU approach differs from the one followed in the US. In the EU, a dominant firm that, through a discount scheme, sets in place a *de facto* exclusivity will be found to infringe Art. 82. No analysis is carried out, about the definite or potential likelihood of a rival to win a share of the dominant firm’s sales.

In comparison, enforcement of exclusivity agreements in the US is based on a stricter standard. In order for a plaintiff to claim a Section 2 violation, foreclosure of a substantial part of the market must be shown. And the burden of proof seems difficult to meet if other suppliers are present in the market. This was the finding in *Concord Boat* where the Supreme Court rejected the plaintiff’s argument that the effect of the share discount offered by Brunswick was to tie-in boat builders. The Court held that Brunswick’s prices were not predatory and the discount scheme did not foreclose a substantial share of the market.

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81 The issue was raised in the first Microsoft case, where the Justice Department stressed that: “While the Department recognizes that volume discount pricing can be and normally is pro-competitive, volume discounts can also be structured by a seller with monopoly power (such as Microsoft) in such a way that buyers, who must purchase some substantial quantity form the monopolist, effectively are coerced by the structure of the discount schedule (as opposed to the level of price) to buy all or substantially all of the supplies they need from the monopolist” [United States v. Microsoft, 59 Fed. Reg. 42,845, 42,854 (Aug. 19, 1994) (Proposed Final Judgment and Competitive Impact Statement)].

82 For a similar reasoning, see *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 245 (1984) (O’Connor J., concurring) where the Court stated that exclusive dealing “is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal”.

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Even straightforward cases have, therefore, been addressed differently in the EU and in the US. While in the US the replicability of the monopolist’s strategy by competitors implies that discount has no restrictive effects, in the EU the analysis of the status of competition was not part of the standard of evidence until the adoption of the Discussion Paper. In fact, the simple “tendency” of a practice to distort competition was considered sufficient to substantiate an Art. 82 claim.

5.3 **COMPETITORS’ HARM: (I) THE PROBLEM**

The central point in the evaluation of pricing conducts remains the competitors’ harm test, that is to say if it should be taken into account at all to prove an exclusionary conduct and how it should be measured. In this section, we advocate the adoption of such test and we draw arguments from the differences between the EU and US approaches. We remark that the endorsement of a competitors harm standard allows to avoid or limit Type II errors and to prohibit only cases which effectively decrease consumer welfare. This was the approach suggested in the Discussion Paper, as outlined earlier.

Critics of the EU approach emphasize that one of the problems with the Commission’s practice and with the case law in general is that while pro-competitive aspects are not part of the test, the anticompetitive effects of loyalty rebates are presumed and there is no analysis of harm to competitors. The two elements are linked in that under the EU test no weight is given to harm to competitors and this is because anticompetitive effects are presumed; indeed, as stated by the CFI, “for the purposes of applying Article 82 EC, establishing the anticompetitive object and the anticompetitive effect are one and same thing.”

The reason why the competitors’ harm test should be instead applied is simple: if competitors can supply all or part of the customer’s requirements, discounts can prove healthy for the competitive process. Rivals will be urged to compete with the dominant firm to fulfil all or just part of a buyer’s needs, and might be even forced to win the contestable part of the supplies on levers other than price such as innovation, promotion, after sale services, etc.

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83 In what follows we assume that the competitors’ harm test equals the analysis of the existence of rivals in the market and the possibility for them to compete away all or part of the dominant firm’s supplies.


85 § 241 of the *Michelin II* judgment.
But if this is true, then great caution should be used in condemning a discount scheme when competitors are active on the market. Some scholars correctly point out that if rivals already operate in a market, they can easily react to the dominant firm’s pricing policy by offering competitive discounts. Moreover, the simple fact that competitors are present on the market might imply that they have already dropped their fixed costs, so that an exclusionary strategy will barely succeed.\(^{86}\) This means that since evicting already active rivals is more difficult than deterring entry, in cases where competitors are already present on the market, the burden of proof should be higher.\(^{87}\)

Once we agree on the use of an effect-based approach, it is fundamental to properly construct the competitors’ harm test in order to avoid committing Type II errors and in doing so protect inefficient competitors.

### 5.4 Retroactive Rebates Do Not Always Lead to Foreclosure

How is then the problem dealt with in the EU and the US? In the EU there are different scenarios that can be outlined: in some cases the exclusionary nature of a pricing scheme has been assessed without having regard to either the existence or the capability of competitors to match the dominant firm’s conduct. This is the reasoning we find in cases such as \textit{Hoffmann-La Roche, Michelin I} and \textit{Michelin II}\(^{88}\) where neither the Commission’s decisions nor the Courts’ judgments focused on the existence of competitors and on their ability to duplicate the monopolist’s pricing policy.

This approach is rather worrying as the existence of competitors in the market should imply that competition can potentially take place. Which is why there should be a thorough investigation of the impossibility to replicate the monopolist’s pricing practice.\(^{89}\)

In a different line of cases, competitors’ harm has been included in the test to assess the dominant’s firm pricing policy, although in a rather loose and unsatisfactory way. In such cases, while the existence of competitors is relevant, their ability to match the dominant firm’s pricing policy is not

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\(^{87}\) This leads to the point made in Section 4.2 and 4.3.

\(^{88}\) For an analysis of this aspect, see A. Heimler, \textit{Price below cost and loyalty discounts: are they restrictive and if so when?}, […]., p. 4, 10.

taken into account. In other words, even if there is no harm to competition because rival firms are already present in the market and they manage to erode the monopolist’s market share, the monopolist’s conduct can be held exclusionary. Following this reasoning, even if the dominant undertaking is losing ground to its rivals, the discount practice is found exclusionary given that, in its absence, competitors would have grown more than they did. To quote the CFI in several instances, “it is very probable that the fall in the [dominant firm’s] market share and in its sales prices would have been greater if the practices criticized in the contested decision had not been applied.”

The Discussion Paper and Tomra case mark a change in the EU approach, in that replicability of the offer by competitors is effectively scrutinised, even if the test applied still leaves certain issues open.

The approach followed in the US, at least before Le Page, seems diametrically opposite. In the first place, the standard applied to assess the monopolist’s pricing strategies is predation, at least as far as single product rebates are concerned. In order to get a favourable judgment, plaintiffs have to prove that the defendant’s prices were below a certain measure of cost, for example average variable costs. Cases like Grimmel, Concord Boat, California Computer, and Ortho Diagnostic exemplify this very tenet. The competitors’ position and the harm suffered as a result of the monopolist’s discount strategy does not even come into play if the price is above AVC.

In addition to this, new entries and reduction in the monopolist’s market share indicate a lack of foreclosing or evicting effect. More importantly, a further element of the absence of foreclosure is the profitability of the plaintiff’s business, which is in clear contrast with the test applied in the EU.

Furthermore, US courts do not rule out the possibility for the monopolist to react to rivals’ competition; indeed, such a possibility is considered lawful if exercised within the limits of predation. As stated in California Computer, “[w]here the opportunity exists to increase or protect market share profitably by offering equivalent or superior performance at a lower price, even a

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90 See Michelin II, § 245, Compagnie Marittime Belge, § 149 and British Airways, § 298.
91 See Concord Boat.
92 See Ortho Diagnostic, where the Court ruled that “[w]hile the fact that Abbott has priced each component of its package above average variable cost is not alone sufficient to protect it from Section 2 liability, there remains Abbott’s contention (...) that there can be no liability here because Orthos’ blood assay business (...) remains profitable.”
virtual monopolist may do so.” In particular, in Grimmell, the fact that a discount contract by a monopolist tied a customer and foreclosed competitors has not been found to be in itself a problem. The same reasoning was applied in Concord Boat, where the plaintiffs complained about the overreaction on behalf of Brunswick to the discount programs introduced by rivals. The Eight Circuit rejected this argument stating that the plaintiffs had not provided sufficient evidence of a consistent market foreclosure resulting from Brunswick’s pricing policy.

The rule is even clearer for bundled rebates: before Le Page, the standard to be met to claim a Section 2 violation was particularly strict: the plaintiff had to prove below cost pricing and a lack of profitability to match the monopolist’s price, notwithstanding the competitor’s same level of efficiency.93

The Commission and the European courts, instead, look with much more caution at the dominant’s firm reaction to rivalry from competing market players. In the Discussion Paper, conducts in response to competitors’ behaviour are viewed as acts of “discipline”, or “marginalization”, in possible breach of Art. 82.

The different outcome reached in Europe and in the US in the litigation between Virgin Atlantic and British Airways describes well how a different measurement of the competitors harm with regard to the same conduct leads to opposite results. As described above, Virgin was unsuccessful in its US litigation as it did not provide sufficient evidence in support of its claim that the incentive agreements entered into with travel agents caused competitors to lose sales and market shares. A similar allegation, however, was raised successfully before the Commission and the European Courts. The Commission’s decision, the CFI’s judgment and AG Kokott’s opinion do not even discuss the adequacy of Virgin’s burden of proof, as they presume that the retroactive nature of the rebate is exclusionary. The fact that the scheme applied to all sales made by a travel agent before the target was reached, made it unprofitable for a travel agent to offer services to competing airlines even for a small part of its requirements, as this would imply losing the rebate on all the sales

93 In Ortho Diagnostics, the Court ruled that “(...) only price cutting that threatens equally or more efficient firms is condemned under Section 2. In consequence, this Court holds that a Section 2 plaintiff in a case like this – a case in which a monopolist (1) faces competition on only part of a complementary group of products, (2) offers the products both as a package and individually, and (3) effectively forces its competitors to absorb the differential between the bundled and unbundled prices of the product in which the monopolist has market power – must allege and prove either that (a) the monopolist has priced below its average variable cost or (b) the plaintiff is at least as efficient a producer of the competitive product as the defendant, but that the defendant’s pricing makes it unprofitable for the plaintiff to continue to produce. Any other rule would entail too substantial a risk that the antitrust laws would be used to protect an inefficient competitor against price competition that would afford substantial benefits to consumers”.

achieved in the relevant period. The ECJ’s judgement goes even further as the Court states that the mere tendency to distort competition is a sufficient ground for an Art. 82 violation.

5.5 TRYING TO SKETCH A DIFFERENT COMPETITORS’ HARM TEST FOR SINGLE REBATES

The assumption based approach appears unconvincing even for retroactive rebates in a number of circumstances. To begin with there is at least one setting in which even retroactive rebates do not necessarily have a foreclosure effect on existing or new suppliers. This is when the customer’s total demand over the relevant contractual period exceeds the threshold quantity triggering the rebate. As long as supplies by a rival firm do not exceed the difference between the client’s total demand and the quantity set in the discount threshold, the customer would still buy from the dominant firm a quantity that allows it to qualify for the discount.\(^{94}\) If this is the case, multiple supplies can co-exist and the rebate scheme does not cause any exclusion.

Another instance in which retroactive rebates do not have any foreclosure effect is when competitors can compete on the same scale as the monopolist. As stressed by the Commission in the Discussion Paper, a major problem with retroactive rebates is that, in order for rivals to be able to win sales from the dominant supplier, they are forced to offer a particularly low price. Assuming that the threshold quantity triggering the rebate covers the entire customer’s demand, a competitor might have to price its products low enough so as to compensate the client for the rebates foregone by not meeting the threshold. But if predation is the standard, not always is the price that competitors are forced to apply below marginal costs; hence rivals are not driven out of the market nor is entry deterred. This is the case when competitors can produce at the same scale as the dominant firm and are able to introduce a comparable all-unit discount.\(^{95}\) One might question whether this was the setting in *British Airways* given that the airline market, while dominated by BA, accounted for major companies capable of competing at least potentially at the same scale as BA. A similar issue was discussed in *Michelin II*, where the defendant objected that Continental and Pirelli were major worldwide competitors benefiting from the same economies of scale as Michelin and were, therefore, able to offer similar rebate schemes.\(^{96}\) Moreover, even if in the Discussion Paper the Commission seems to have endorsed an effect-based approach, there are shortcomings

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\(^{94}\) This point has been raised by G. Federico, *When are rebates exclusionary?*, European Competition Law Review, [2005], p. 479. See also A. Heimler, *Pricing below cost and loyalty discount: are they restrictive and if so when?*, p. 6, who suggests that: “discounts are only lost if additional purchases from a competitor impede the retailer from achieving the established target.”

\(^{95}\) See B. H. Kobayashi, *The economics of loyalty discount and antitrust law in the United States*, p. 4.

\(^{96}\) See D. Waelbroeck, *Michelin II: a per se rule against rebates by dominant companies?*, Journal of Competition Law and Economics, [2005], p. 159.
when following a formalistic approach in defining the competitors’ harm test, as shown by the unsatisfying outcome reached in *Tomra*.

The above analysis shows that, as regards single product rebates, there is a fundamental difference between the EU and the US approach. While in Europe the enforcement of rebates is based either on an assumption based approach or on a formalistic effect-based test, the US has applied a full rule of reason method. The level of price is, therefore, compared with the costs incurred and the capability of competitors to match the monopolist prices is also part of the test.\footnote{As stressed by P. Greenlee and D. Reitman, (Distinguishing Competitive and exclusionary Uses of Loyalty Discounts, quoted) this is the right test because “if a firm increases its target requirement and the profits from the incremental sales fall below the additional discount that is paid under the new loyalty program, then the new loyalty program is inconsistent with a competitive use of the loyalty discounts, and suggestive of some other, possibly exclusionary motive” (p. 452).} This appears to be a sound approach. The difference in the enforcement policies endorsed on both sides of the ocean is not merely theoretical, because the same cases can have a different outcome with the consequence that a pricing policy by the same company, which is allowed in the US, might be prohibited in Europe; this result is clearly unsatisfactory. Furthermore, and most importantly, there are certain circumstances in which an assumption based approach leads to the wrong outcome, as the discount does not preclude other suppliers from selling to the same client or, even better, rivals can duplicate the monopolist’s offer.

While all the above limits were overcome by the case law that preceded *Le Page*, the assessment of pricing practices following *Le Page* stands on somehow weaker grounds, in that the Third Circuit seems to have followed an assumption based approach as discussed below.

### 5.6 THE TEST FOR BUNDLED REBATES

As already outlined, *Le Page* constitutes a major reversal in the assessment of rebates as in previous case law the standard for assessing the lawfulness of discount schemes was based on predation alone. As a matter of fact, the Court in *Le Page* ruled out the use of the predation test for multi-product settings. The focus of the exclusionary effect while not clearly stated, seems to refer mainly to the fact that 3M used the monopoly position held in the Scotch-brand tape to foreclose sales of private label through tying rebates. In addition, in the analysis of 3M’s pricing policy no weight was given to the capability of competitors, and of *Le Page* in particular, to match 3M’s offer. This is all the more odd as *Le Page* was a long-time player in the private-brand tape and had managed to attain a significant market position.
As mentioned earlier, the focus on tying bundles is not totally new, as a similar test was applied already in *SmithKline v. Eli Lilly*. However, the restatement of such a principle raises some concerns for a number of reasons, which are clear if we take the bundle aspect out of the analysis for a while. The first problem we find is that 3M’s rebate should have been seen as a normal discount scheme, even if it was offered by a company holding a monopoly position, and thus should have been judged under a predation standard. This aspect is of relevance since, according to such a rule, presumably Le Page’s claim would have been rejected. Arguably, the Third Circuit took a much more cautious approach, stating that:

“[a]ssuming that Brooke Group should be read for the proposition that a company’s pricing action is legal if its prices are not below its costs, nothing in the decision suggests that its discussion of the issue is applicable to a monopolist with its unconstrained market power (…) a monopolist is not free to take certain actions that a company in a competitive (or even oligopolistic) market may take (…)”

This position is far from that assumed in rulings such as *California Computer, Transamerica II, Grinnell*, and especially of *Ortho Diagnostics*, where the predation test was expressly used to measure the foreclosure effect of the bundled rebates.

The reason why this switch is worrying is clearly shown if we look at the other part of the charge against 3M: the application of a discount over a wide range of products. This, according to the Court, could not be offered by other firms in the market, and in particular by Le Page. Indeed, the principle that multi-product rebates have *per se* an exclusionary effect appears unconvincing if not supported by the evidence of the specific case, that is to say, if it is not proved that competitors are unable to react to the introduction of a rebate over a wide variety of products. 98

Again, this criticism is not irrelevant, because the ability of rivals to compete away sales from the monopolist through the offer of bundled rebates is much more concrete than what has been considered by the Third Circuit in *Le Page*.

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98 The exclusionary nature of bundled offers was dealt with, among other things, in the recent *Microsoft* judgment (Judgment of 17 September 2007, Case T-201/04, *not yet reported*), where the CFI (upholding the Commission’s findings) confirmed that discounts can be used as a means to perform an illegal tying under Art. 82(d). The Court states that: “it does not follow from either Article 82(d) EC or the case-law on bundling that consumers must necessarily pay a certain price for the tied product in order for it to be concluded that they are subject to supplementary obligations within the meaning of [Art. 82(d)].”.

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As has been pointed out by some scholars, there are cases in which, even in multi-products settings, a competitor manufacturing a single product/service can still subtract market shares from a monopolist applying an above cost price and, thus, is not forced out of the market.\textsuperscript{99} In particular, in multi-package price settings, it is more likely that the multi-product firm faces competition at least in some of the products which are part of the bundle. If this is the case, rivals can subtract sales at least for some products and thus they can exercise pressure on the monopolist.

A second element deals with the time frame of the discount: are long term multi-package discount schemes really worrying from an antitrust standpoint? The answer should be no for two reasons. If the result of the multi-item pricing policy is to push the single-product firm to a price close to its marginal costs – in order to compete with the multi-product firm - this shouldn’t be challenged under antitrust standards. Ultimately, pricing close to marginal costs is what competition should be all about. Nor should one be concerned if the outcome of the multi-product pricing strategy is that the single firm is forced to diversify its commercial strategy and market new products, even if this entails substantial lowered costs.

If the test to establish that a pricing strategy is anticompetitive is that the only rational justification for the conduct is exclusion of competitors, a multi-product pricing strategy raising rivals’ costs might run foul of the prohibition, provided that competitors are not forced out of the market. We have seen though that the EU endorses a stricter test of raising rivals’ costs, according to which a simple loss in competitors sales might be found foreclosing, even if exit from the market is not the final outcome.

In other terms, bundled rebates should not be treated differently than single rebates, thus, if the rebate is above cost, it should not be considered anticompetitive. The \textit{Le Page} court clearly did not apply such a standard of proof and that there is no discussion in the judgment about the amount of price reductions Le Page had to incur in order to match 3M prices. From this perspective, the standard endorsed in the Discussion Paper, i.e. the reference to long run incremental costs, seems more appropriate.

Rebates by dominant firms has become a highly debated topic in antitrust law also because recent developments in EU and US regimes have left certain unsolved issues.

The Discussion Paper represents a significant change in the exclusionary rebates and the Commission is expected to issue the final guidelines on the application of Art. 82 to exclusionary abuses in the next months. The definition of an appropriate competitors’ harm test is extremely important as shown by the outcome reached in Tomra (and in the recent ECJ judgment in British Airways), which is not encouraging. A standard rooted in the rivals’ ability to match the dominant firm discount policy would help catching the restrictive practices without sheltering inefficient firms. The interest in the definition of the appropriate enforcement standard is even more relevant if one considers that the guidelines will be enforced by national courts and national competition authorities across Europe and hence the risk of inconsistent approaches seems great.

In the US, the standard set for the assessment of bundled rebates by the Le Page judgment has been criticized by several recent judgments. Hence, one could expect that the Supreme Court takes the occasion to provide some clarifications, possible adopting a more favourable rule vis-à-vis bundled discounts, as also advocated by the Modernization Commission.

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