The Pros and Cons of Rebates
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On the use of price-cost tests in loyalty rebates and exclusive dealing arrangements

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Outline

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- Latest experience and challenges of applying the price-cost test
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- Lessons from the French Appeal Court rulings

The implications of the 2017 Intel ruling

- One of the main points of the paper:
  - Although it is imperfect, a price-cost test can be an important addition to a coherent theory of harm
- Corollary of this argument:
  - The 2014 GC ruling was not a step in the right direction as it leaves no room for economic consideration and/or analysis of effects
- The paper was written before the 2017 CJEU Intel ruling
- In a sense, the 2017 CJEU Intel ruling clarifies that the Commission cannot adopt on a form-based approach when dealing with exclusivity agreements and loyalty rebates
- But the ruling leaves open questions for Competition Authorities (e.g. burden of proof, when is it necessary to apply the price-cost test?, etc.)

Latest experience and challenges of applying the price-cost test

- French Competition Authority:
  - Three recent loyalty/retroactive rebates cases
    - Orange (15-D-20)
    - TDF (16-D-11)
    - Umicore (16-D-14)
  - One case undergoing investigations

- Both Umicore and TDF decisions were appealed. The French ‘Cour d’Appel’ has delivered rulings on both

- In all cases but Orange, a price-cost test was performed but the test was not necessarily reported in the final decision (it confirmed the potential problems or was deemed irrelevant)

Latest experience and challenges of applying the price-cost test

1. Measurement issues (1/2)

- Measurement issues are a well known problem, particularly in the case of an as-efficient competitor test (contestable share, incremental/avoidable costs and volumes of dominant firm, discounted and non-discounted prices, etc.)

- Yet, as the paper argues, « *the price cost test should not necessarily apply across all customers or across all the units purchased by a given customer* »

- For example, loyalty rebates may target customers that are necessary to the development of their competitors' business

- In our on-going case, retroactive rebates are:
    - Different for the three categories of customers ("small"/"medium"/"important")
    - Different for each "important" customers (approx. 180)

Latest experience and challenges of applying the price-cost test

1. Measurement issues (2/2)

- Applying the test on a customer basis raises further measurement issues:
  - Collect information at the customer level (rebates grids from contracts, individual volumes (with dom. firm and total), etc.). Problems:
    - Rebates grids sometimes absent from contracts: no information on “counterfactual” prices
    - Prices could depend on types of services chosen by customer
  - The estimation of the contestable share (individual or global?)
  - The relevant costs? (group of customers: incremental vs. individual customers: avoidable ?)
  - Incremental/avoidable costs are means: individual customers’ costs may be lower/higher
  - Etc.

- When analyzing on a customer basis, it is not unlikely for the results to be mixed (e.g. TDF case (see next): some customers affected and others not, some rebates may be considered exclusivity rebates others not, etc.)

Latest experience and challenges of applying the price-cost test

2. Lessons from TDF case (16-D-11) (1/2)

- Case raised the questions of the share of the market affected and of the qualification of exclusivity rebates
- TDF: ex-State monopoly for the diffusion of television (emission of signal received by TV antennas). Still in a dominant position.
- Between 2005 and 2009, TDF used retroactive rebates to sell its services to creators of content during call for tenders.
- Rebates were offered if the creator of content used its services for [75-95]% of the geographical area concerned by the call for tenders
- Rebates were applied to 40% of the market
- French Competition Authority fined TDF for the use of exclusivity rebates

Latest experience and challenges of applying the price-cost test

2. Lessons from TDF case (16-D-11) (2/2)

- Position from the French Appeal Court (dec. 2017):
  - The rebates cannot be considered exclusivity rebates: not defined considering the entire relevant market but only tailored to each call for tenders. In other words, the price charged to a creator of content for a particular geographical area did not depend on exclusivity in other geographical areas.
  - All other parts of the initial decision were confirmed: loyalty rebates, rebate applied if high market share of the dom. firm, non negligible part of the market (40%) affected by the rebates
  - The French Appeal Court considers that:
    - A rebate affecting a limited part of the market still constitutes an abuse by preventing competitors from competing with the dominant firm on this limited part of the market.
    - The reduction of the margins of the competitors hinders their development in a market already suffering from limited competition.

Latest experience and challenges of applying the price-cost test

3. Lessons from Umicore case (16-D-14) (1/2)

- The paper makes an important distinction between exclusive dealing contracts and loyalty (exclusivity) discounts. Yet, in practice, contracts may have features of both
- Umicore: most important supplier for zinc roofs (80% of the market)
- Products not substitutable to other types of roof materials => dom. position
- Contracts offered to distributors between 1999 and 2007: in case the distributor did not respect the exclusivity clauses on sales => loss of rebate. Moreover, the contracts also stipulated conditions on availability of stocks and exclusivity of publicity in favor of Umicore. Contracts covered 70% of the market.
- Fined by the French Competition Authority for exclusivity contracts

Latest experience and challenges of applying the price-cost test

3. Lessons from Umicore case (16-D-14) (2/2)

- In its appeal, Umicore put forward the fact that the firm had produced an AEC test that was never addressed by the French Competition Authority.
- Position from the Cour d’Appel (2018):
  - In the case in question, the court rejected the pertinence of the AEC test as it addressed the loss of rebate due to the exclusivity clause on sales but not the clauses on availability of Umicore stocks and exclusivity of publicity in favor of Umicore. These clauses constitute further obstacles for potential competitors. The existence of these obstacles makes the AEC test irrelevant
  - More generally, the court underlined that there is no obligation to rely on the AEC test.

Lessons from the French Appeal Court rulings

In both cases, the French Appeal Court showed vigilance and severity towards the use of loyalty rebates

May be understandable:

1. Loyalty rebates are not necessarily low prices but can be seen as a tax on sales from competitors
2. Even if the loyalty rebates do not drive competitors out of the market, they generally distort competition on the merits: the dominant firm can constrain its competitors in charging lower prices than it is itself forced to charge to retain or conquer new customers
3. In the absence of efficiency gains, other forms of rebates can be substituted to loyalty rebates (i.e. incremental rebates)
4. As it is the case in Umicore, a number of abuses are not (solely) based on price and it is therefore impossible or irrelevant to apply a price-cost test. However, it does not prevent jurisdictions from condemning the practices.

Thank you for your attention