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What discount structures can a dominant firm use? European Court supplies further guidance

The European Court has given further guidance on how to assess the legality of rebates and discounts offered by dominant firms in a case concerning rebates practised by Post Danmark¹, which at the relevant time enjoyed a statutory monopoly in Denmark for next day postal deliveries.

Post Danmark operated a unitary rebate scheme, which applied to bulk mail services both within the scope of the statutory monopoly (next day delivery) and outside it (delivery in two or three days). Post Danmark ended up with both a monopoly on next day bulk mail and a 70% share of after next day bulk mail. The essential case against Post Danmark was that it was employing a discount structure to leverage its monopoly and achieve or maintain dominance in a related segment where it was subject to competition.

Less extreme and more common cases involve the analogous situation where a dominant firm employs rebate or discount structures which apply across all purchases by the customer, within and outside the segment where the firm is dominant. These structures are problematic because they can in particular penalise competitors operating in the segments where the firm is not dominant. Where discounts apply across all purchases, and are subject to aggregate purchase thresholds, customers may not be able to afford to lose discounts obtained in the dominant segment by transferring purchases in the non-dominant segment to a competitor, and thereby falling below the discount threshold.

In the case of Post Danmark:

- The discount structure applied, as we have noted, to the customer's aggregate purchases for all bulk mailings, including next day and subsequent delivery

- Stepped discount rates increased in line with aggregate purchase thresholds
- The amount of rebate was based on expenditure in a year and was calculated according to the degree to which forecast expenditure was realised
- Discount was applied at the applicable rate retrospectively to all the customer's purchases from "dollar one"
- Post Danmark was super dominant because it had a guaranteed statutory monopoly
- As a result of its statutory monopoly, Post Danmark had significant scope for leveraging economies from its existing network – the statutory monopoly effectively allowed Post Danmark to control 95% of bulk mail in Denmark.

In proceedings between Post Danmark and the Danish competition authority, the Danish court sent several questions to the European Court regarding the circumstances in which rebates practised by dominant firms can be abusive. The European Court held that in deciding whether a rebate was abusive, regard had to be given to all the circumstances. In particular, the Court held that it was not always a requirement that the rebates prevent competition from an equally efficient competitor.

According to the 'as efficient competitor' - or AEC - test (which was set out in the Commission's 2009 guidance on enforcement priorities regarding abusive exclusionary conduct by dominant undertakings²), the dominant firm is entitled to assume that its competitor has the same cost structure when assessing whether the dominant firm's pricing is abusive. Applying this assumption, if, having reimbursed the customer for all its lost rebates and discounts, the competitor could still sell at a profit at the same price (and assuming it had the same cost structure) as the dominant firm, then the dominant firm's pricing is not abusive.

The Court held in this case that it was not necessary to apply the AEC test, as it had also done in the preceding *Intel*³ case. Although this may seem to be a further step away from the AEC test, it is important to note that in this case, Post Danmark was super dominant and, according to the reference from the Danish court, benefitted from significant economies of scale and high entry barriers to the bulk mail market in Denmark. A more accurate read of the case may therefore be that the case demonstrates that we cannot blindly rely on applying the AEC test in circumstances where, due to structural or regulatory reasons beyond the control of the challenging competitor, it is just not realistic to expect that the competitor's costs should be the same as those of the dominant firm. Such a conclusion is supported by the judgment itself, which states that, although there is no obligation to apply the AEC test, this "ought not to have the effect of excluding, on principle" recourse to the AEC test in rebate cases⁴.

Other important factors in assessing the abusiveness of the discount were that customers did not know exactly what rebate they had earned until the end of the year, that a year was considered by the Court to be a fairly long reference period, and that the rebate applied from dollar one, rather than in incremental steps.

The case therefore concerns a very aggressive rebate structure, where the market power of the dominant firm was reinforced by statutory privileges, high entry barriers and significant scale economies. It is perhaps unsurprising that a plea that the AEC test had not been applied failed to impress the Court, just as it also failed to do in *Intel* – in that case, because the rebate was additionally conditional on exclusivity. It may therefore be too easy to view *Post Danmark* and *Intel* as a move away from the AEC test. Rather, these cases show that an examination of all the surrounding circumstances is required in order to determine whether or not the AEC test is a sensible indicator of abuse.

The AEC test is certainly still worth applying in assessing abusiveness of rebates. If a given pricing structure fails the AEC test, it is almost certain to be problematic. However, where other exclusionary factors also exist, the dominant firm should consider the effect of these factors on the ability to compete, even where the AEC test is met. The case also confirms that incremental rebates will be regarded as less problematic than “dollar one” retrospective rebates, and also that shorter reference periods for calculation of rebates will be seen as less anti-competitive.

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- 1 <http://curia.europa.eu/juris/document/document.jsf?text=&docid=169191&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=492320>
 - 2 [http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52009XC0224\(01\)](http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52009XC0224(01))
 - 3 <http://curia.europa.eu/juris/document/document.jsf?text=&docid=153543&pageIndex=0&doclang=en&mode=lst&dir=&occ=first&part=1&cid=494876>
 - 4 Paragraph 58 of the judgment

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