RĪGAS EKONOMIKAS AUGSTSKOLA
STOCKHOLM SCHOOL OF ECONOMICS IN RIGA

SSE Riga Student Research Papers
2010:12 (129)

THE DARK SIDE OF REBATES. ANTITRUST REGULATION IN THE EUROPEAN UNION AS REGARDS TO REBATE STRATEGY

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ISSN 1691-4643
ISBN 978-9984-842-39-4

November 2010
Riga

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Abstract

This diploma project examines competition regulation in the European Union (EU) in regard to rebates. Research is based on comparison of the EU legal system and the United States (US) legal system, insofar as dominance, abuse of dominance, and rebate regulation are determined. The main aim of the diploma project is to establish when pro-competitive rebates inevitably become anti-competitive. The general approach is comparison of theory with practice in European Commission ("the Commission", "Commission") decisions, in particular, the *Intel* case.[1] The *Intel* case forms an empirical base for this diploma project. The main focus is the actual problem of how to determine when rebate strategies become illegal. Much criticism has been levelled at the argumentation of Commission decisions. The research analyses two main criteria: the legal reasoning in Commission decisions, and business reasoning. Research methodology is based on EU and US case law studies and related legal instruments. First, analysis of a dominant position or monopoly is followed by analysis of abuse of dominance by granting conditional rebates in both legal systems. Second, the approaches of both legal systems are compared.

Results of analysis show that the US legal system has more developed rebate regulation than the EU and that Commission authorities have ground for development. The main finding is that legal theory differs from practice: even the Commission is not using its own issued legal instruments. However, the real reason for competition law is doubtful taking into account the recent decision in the *Intel* case. The diploma project emphasizes the problem that the current Commission approach should be revised and that the legal reasoning in Commission decisions is based on case law and ignores the fundamental aim of competition law.

Keywords: abuse of dominance, AMD, anti-competitive, anti-competitive rebates, antitrust, antitrust regulation, Commission, Commission decisions, competition, competitiveness, conditional rebates, dominance, dominant position, Guidance, EU legal practice, EU legal system, Intel, Intel case, pro-competitive, pro-competitive rebates, rebate strategy, rebates, rebates regulation, Sherman act, US legal practice, US legal system.

[1] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07.

Acknowledgements

Signature: …… /Aleksandrs Orlovs/

Date:

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1. Introduction

Competitiveness in nature is a question of survival and competitiveness in the market is a question of wealth.[2] All companies face a great challenge because of globalization at the end of the twentieth century. Globalization was the signal for implementing rapid change, aiming to be more competitive than rivals, aiming to acquire or defeat the weakest companies, to gain more market share, to become dominant[3] in the market, and to be the wealthiest. Business problems increase with the size of companies and one day market leaders` strategies turn from a legal to an illegal tool.

Two market leaders in the computer hardware industry, responsible for central processing units (CPUs) or computer "brain" manufacturing, have considerably changed human evolution in the past forty years.[4] The Intel Corporation (Intel) and Advance Micro Devices Inc. (AMD) have historically competed with each other with the aim of leading the market.[5] Over time, these companies have developed their strategies according to changes in the market. Today, one competition tool is rebate strategy.[6] The problem with rebate strategy appears when companies are trying to determine when this competition tool becomes illegal; what is the line between pro-competitive rebates and anti-competitive: when is the moment of crossing this line?

Intel pro-competitive rebate strategy turned out to be anti-competitive as established by the Commission on 13 May 2009. The Commission decision contains the conclusion that conditional rebates granted by Intel to Dell, Hewlett Packard (HP), NEC, Lenovo, Acer and Media Saturn Holding (MSH) constitute an abuse of a dominant position under the Treaty on the functioning of the European Union[7] (TFEU) Article 102 (ex Article 82 TEC)[8] and Article 54 of the European Economic Area (the EEA) Agreement.[9] Thus Intel business strategy in regard to rebates was found to be illegal and Intel is now under a duty to revise it with the

[2] Smith, A. (2009). *The Wealth of Nations*. New York: Classic House Books New York., p. 47-48.
[3] The term *dominance* is used as a synonym for the term *monopoly*. Nevertheless, during US case discussion the term *monopoly* is mainly used and during EU case discussion the term *dominant position* is used.
[4] Intel Corp. was established in 1968 and Advance Micro Devices Inc. was established in 1969.
[5] AMD filed a Petition for Arbitration on 10 April 1987. Case Nr. 626879.
[6] The term *rebate* is used as synonym for the business term *discount* and as a synonym to the legal term *conditional rebate*. Furthermore, the term *conditional rebate* is used as a synonym for the term *fidelity rebate* and for the term *loyalty rebate*.
[7] Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union [2008] OJ C115.
[8] Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community [2007] OJ C306.
[9] Agreement on the European Economic Area [1994] OJ L1.

aim of avoiding punishment in the future. Yet serious difficulties stand in the way due to the fact that it is not sufficiently clearly stated exactly when legal rebates become illegal.

Another aspect of the problem is related to interpretation of the law by the Commission. This interpretation is constantly changing so that companies may not rely on legal provisions in conducting their business. The time scale shows what business practices are allowed according to TFEU Article 102[10], but these may later be interpreted differently and may be scrutinized by the Commission in light of anti-competitive behaviour. In this case common business behaviour for Intel competing with AMD was declared on 13 May 2009 as a single and continuous infringement of TFEU Article 102 and Article 54 of the EEA Agreement. The Commission decided that this behaviour merited a fine in the amount of EUR 1 060 000 000.[11]

The *Intel* case is indicative evidence of the existing problem. It is important to study the *Intel* case with the aim of discovering the business motivation in Commission decisions. After the decision was made, it received considerable and immediate criticism, with Intel`s adherents arguing that the Intel rebate strategy is a part of stiff competition with AMD, additionally that this business strategy is beneficial for consumers, and "…even if Intel did engage in anti-competitive activity, the fine was much too large."[12]

It is not clearly understandable when the line of legal competition was crossed and company business behaviour became illegal. It is not clear if the Commission relied on any competition business theory in its decision. Furthermore, the rebate strategy of Intel`s competitor AMD was not analysed in the case.

In this diploma project, competition business theory is applied to Intel's behaviour and is analysed with the help of leading authority on competitive business theory, Michael E. Porter. Legal competition theory is analysed within EU and US case studies. Taking into account company size and geographical markets, it is necessary to analyse EU and US practice in rebate strategies in correlation with the Sherman act.[13] This diploma project offers a different approach to analysis of the antitrust[14] regulation problem in the EU in regard to rebate strategy. The diploma project is based on an *Intel* case study. First, legal

[10] From here on in main text referred to only as "TFEU Article 102".
[11] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 1803.
[12] Lande R.H. (2009, June 1). *The Price of Abuse: Intel and the European Commission Decision*. Available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1434985.
[13] The Sherman Antitrust Act, 15 U.S.C.A. § 2 (1890).
[14] The term *antitrust* is used as a synonym for the legal term *competition*. Nevertheless, during US case discussion the term *antitrust* is mainly used and during EU case discussion the term *competition* is mainly used.

issues are reviewed. Second, in the literature review section these issues are analysed in the frame of both legal theory and competition business theory. Further, in the research and discussion section, EU legal practice is compared with US legal practice. Case studies in both legal systems in regard to rebate strategies are analysed. The research aims to clarify economic and business presence in reasoned motivation of Commission decisions. The practical aim of the diploma project is to contribute to: a) companies[15] which regard themselves as being in a dominant position (or a position which may be found dominant) and use rebate strategies with the aim of being prudent with their actions; b) Commission decision makers with the aim of revising their interpretation of competition law; c) students and other lawyers interested in the *Intel* case.

2. Intel case description

Balanced trade and fair competition in the EU is one of the fundamentals stated in the TFEU preamble. The TFEU contains rules regulating competition, in particular TFEU Article 101 (ex Article 81 TEC) and TFEU Article 102. The existence of these rules is a consequence of the main idea of the EU as a single economic community, with fair competition, free movement of goods, persons, services and capital.[16] Thus, the aim of TFEU Article 102 is to protect the EU common market against abuse of a dominant position by one or more undertakings. In order to understand the legal aspect of the rebate strategy problem, this diploma project begins by reviewing the terms of TFEU Article 102 in correlation with the *Intel* case.

The Commission decision contains the conclusion that conditional rebates granted by Intel to Dell, HP, NEC, Lenovo, Acer and MSH constituted an abuse of a dominant position under TFEU Article 102 and Article 54 of the EEA Agreement. One of the conditions for establishing such abuse is "...directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions."[17] In the *Intel* case in particular, Intel had committed a single and continuous infringement of TFEU Article 102 by granting rebates to customers in that it was conditional to customers for obtaining all supplies of x86 CPU from Intel.[18]

[15] The term *company* is used as synonym for the term *firm* and as a synonym for the legal term *undertaking*.
[16] Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union [2008] OJ C115. Article 28-56.
[17] *Ibid.* Article 102.
[18] Product standard based on Intel first 8086 architecture.

The TFEU does not define a dominant position. According to the case law, particularly *Continental Can Company v Commission*,[19] *Michelin v Commission*,[20] and *Hoffmann-La Roche*,[21] discussed in detail later, to establish whether an undertaking holds a dominant position it is necessary to define the relevant product market and the relevant geographical market. In the *Intel* case the Commission defined three relevant product markets: (i) x86 CPUs for desktops, (ii) x86 CPUs for laptops, and (iii) x86 CPUs for servers.[22] The relevant geographical market is the worldwide market, so that the market is not even measured within the EU.[23] Therefore, it can be concluded that the Commission indirectly emphasises the consequences from Intel business activities being very important globally, not merely within the EU.[24]

The finding of a dominant position held by Intel follows from Commission analysis of market share data, also taking into account possible substitution between CPU products as well as analysis of market entry and expansion barriers.[25] The Commission concluded "...that Intel consistently held very high market shares in excess of or around 80%."[26] This additionally illustrates Intel's significant impact on the global economy and technological progress, and thus, too, on human welfare.

Being in a dominant position does not of itself automatically mean abuse of a dominant position. In the *Intel* case the Commission alleged abuse by Intel of a dominant position by paying conditional rebates to certain customers. The Commission concluded "…that the level of the rebate granted by Intel to Dell, HP, NEC between the fourth quarter of 2002 and December 2005 was de facto conditional upon those customers sourcing their x86 CPUs…" exclusively or almost exclusively.[27] Thus, the Commission concluded that these rebates and payments had the effect of restricting the freedom to choose of the respective Original Equipment Manufacturers (OEMs) and of MSH.

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[19] Case 6/72, *Europemballage Corporation and Continental Can Co. Inc v Commission*, [1973] ECR 215. From here on in main text referred to simply as "*Continental Can*" or "the *Continental Can* case".
[20] Case 322/81, *Michelin v Commission*, [1983] ECR 3461. From here on in main text referred to simply as "*Michelin*" or "the *Michelin* case".
[21] Case 86/76, *Hoffmann-La Roche and Co.AG v Commission*, [1979] ECR 461. From here on in main text referred to simply as "*Hoffman-La Roche*' or "the *Hoffman-La Roche* case".
[22] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, paras 815 and 835.
[23] *Ibid.*, para. 836.
[24] The term *globally* is used as synonym for the term *worldwide*.
[25] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, paras 915 and 840.
[26] *Ibid.*, para. 852.
[27] *Ibid.*, para. 1001.

TFEU Article 102, under which the *Intel* case falls, contains two very important components: 1) an undertaking must have established a dominant position; 2) an undertaking in a dominant position has to behave abusively. Abuse of a dominant position by Intel was committed by granting conditional rebates.

The European Court of Justice (the Court) in analysing rebates uses two terms originating in case law: conditional rebates and fidelity discounts.[28] Conditional rebates mean, as the name of the term implies, that rebates are paid to certain customers only if they comply with certain conditions. In the *Intel* case the Commission found that the rebate was *de facto* conditional and was paid under certain conditions:

1) Dell would not receive Meet Comp Program (MCP) rebates from Intel or would not receive the same amounts of MCP rebates if Dell decided not to purchase all input from Intel.[29]
2) HP purchases at least 95% of its corporate desktop with Intel x86 CPUs.[30]
3) NEC purchases at least 80% of its worldwide client PC x86 CPUs requirements from Intel.[31]
4) Lenovo purchases 100% notebook CPUs from Intel.[32]
5) MSH would not receive rebate payment from Intel if it did not exclusively sell PCs with Intel-based CPUs.[33]
6) Acer would receive reduced Exception to Customer Authorized Price (ECAP) payments if Acer launched notebooks with AMD CPUs.[34]

In the *Intel* case the Commission in its conclusion distinguished two discount types as a continuous infringement of TFEU Article 102 and EEA Article 54: granting rebates that were conditional and granting payments that were conditional.[35] Additionally, the Commission specified another marketing programme implemented by Intel: Exception to Customer Authorized Price (ECAP), Lump sum Customer Authorized Price (LCAP), rebate programme for acceleration, and adopting a new technology and purchase programme,[36]

[28] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 920.
[29] *Ibid*., para. 941.
[30] *Ibid*., para. 951.
[31] *Ibid*., para. 973.
[32] *Ibid*., para. 983.
[33] *Ibid*., para. 992.
[34] *Ibid*., para. 425.
[35] *Ibid*., Article 1.
[36] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 176.

marketing programmes such as the Market Development Fund (MDF) tactic, Intel Inside programme, and distribution programme.[37]

3. Literature review

3.1. Legal theory

The literature review section of this diploma project focuses on rebate strategy practice and its interaction with competition law. This section does not study price-cost and other approaches used by authorities to determine the legality of conditional rebates. The main objective of this section is to compare the convergence of legal theory and business theory in practice and in correlation with the *Intel* case. Additionally, analysis covers what other researchers have found in antitrust regulation in regard to rebate strategy.

Leading competition law expert and economist Massimo Motta explains the legal theory of competition in his work "Competition Policy". The main objective of competition policy is the welfare concept. Motta distinguishes two kinds of welfare: welfare, or total surplus; and consumer welfare, or consumer surplus. The total surplus measure "...is a summarising measure of how efficient a given industry is as a whole and does not address the question of how equal or unequal income is distributed, which can be dealt with by other measures..." while consumer surplus "...is the aggregate measure of the surplus of all consumers."[38] Thus, total surplus measures how well the whole industry performs. Total surplus is the sum of consumer surplus and producer surplus.[39] Consumer surplus is measured by the difference between consumer willingness to pay for the product and what the price of the product is. Motta notes that "[i]t is difficult to say whether competition authorities and courts favour in practice a consumer welfare or a total welfare objective."[40] Another objective of competition policy is to defend a smaller firm which "...has often been one of the main reasons behind adoption of competition laws."[41] The aim of this objective is to protect small firms from abuse by large enterprises or companies in a dominant position. Motta points to one of the key objectives of EU policy, namely, to promote market integration: "This is a political objective which is not necessarily consistent with economic welfare. EU competition

[37] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 178.
[38] Motta, M. (2004). *Competition Policy: Theory and Practice.* New York: Cambridge University Press, p. 18.
[39] *Ibid*.
[40] *Ibid*., p. 19.
[41] *Ibid*., p. 22.

law *de facto* forbids price discrimination across national borders. There is no economic rationale for such a different treatment." [42]

Rudolf Peritz identified several interesting objectives in his report on evolution and change in US antitrust law:

> Competition policy should concern itself only with economic efficiency in the form of consumer welfare. [...] We care about competition, not competitors. [...] The rules of reason are concerned with the competitive effects of restraining freedom of contract, with false positives not false negatives. In short, markets do best when they are left alone.[43]

Massimo Motta concludes that "...*a priori*, it is difficult to say whether price discrimination [Author*:* imposing unfair purchase or selling prices or other unfair trading conditions] has a positive or negative impact over welfare."[44] It is questionable whether rebates as discounts might be considered as price discrimination. Motta points out that such rebates might be discriminatory among company customers such as retailers and distributors: "...some types of rebate made by a dominant firm should be carefully monitored because of their exclusionary potential."[45]

A leading modern researcher regarding rebates is Damien Geradin. In his article "A proposed test for separating pro-competitive conditional rebates from anti-competitive ones" with reference to Christian Ahlborn and David Bailey he distinguishes rebates as follows:

1) A type of threshold which can be defined in terms of volume targets (quantity rebates) or percentage of total requirements (market shares rebates) or increase in purchases (growth rebates). When the percentage required is 100% these would be exclusive rebates.
2) The scope of application, whether they are forward looking, i.e. they apply to incremental units above the threshold (incremental rebates) or backward looking, i.e. applying to both units below and above the threshold (retroactive rebates or roll-back rebates).

[42] Motta, M. (2004). *Competition Policy: Theory and Practice.* New York: Cambridge University Press, p. 23.
[43] Peritz R. (2009). Confidential communiqué from Brussels—Antitrust in America: Fugitive on the run. *SMU Law Review*, *62*, p. 633.
[44] Motta, M. (2004). *Competition Policy: Theory and Practice.* New York: Cambridge University Press, p. 23.
[45] *Ibid*., p. 499.

3) The products or set of products to which they apply, whether they apply to one category of products (single product rebates) or across several distinct products (multi-product or bundled rebates).[46]

The Organization for Economic Co-operation and Development (OECD) in its policy roundtable report 2008 notes: "A "loyalty" discount is a lower price offered to customers who buy more than a threshold volume."[47] The OECD in its report overview emphasises that it is hard to distinguish pro-competitive rebates from anti-competitive rebates.

Einer Elhauge and Damien Geradin in their work "Global Competition Law and Economics" emphasise:

> Loyalty discounts and rebates differ in form from traditional exclusive dealing agreements in two ways. First, loyalty discounts or rebates do not impose an absolute obligation to avoid dealing with rivals, but rather condition the receipt of discounts or rebates on buyers restricting their purchases from rivals. […] Second, loyalty discounts or rebates are often less than 100% exclusive. They may, for example, make the receipt of discounts or rebates conditional on buyers making 80% or 90% of their purchases from the defendant, thus restricting rivals to 10-20% of sales to those buyers.[48]

In the *Intel* case, the Commission's approach was that Intel disrupts the market balance by abusing its dominant position by granting conditional rebates to its customers. Much discussion has taken place within the EU and the US as to the real aim of rebates and as to the legal and business side of rebates. Several researchers have already compared approaches in the EU and the US in regard to rebate strategies.

The practice of EU law regarding rebates has also attracted criticism from Simon Bishop, who points out that whenever a firm is in a dominant position the rebate strategy it applies and rebates in general are deemed to be anti-competitive.[49] That is, Commission decisions and the Court's judgments strongly suggest a *per se* prohibition of loyalty rebates for undertakings in a dominant position.[50] He identifies three problems in this current approach: too much emphasis on dominance, a problem in defining the relevant market, and

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[46] Geradin D. (2009). A proposed Test for Separating Pro-competitive Conditional Rebates from Anti-competitive Ones. *World Competition*, *32*, 41-70, p. 44.
[47] Organization for Economic Co-operation and Development. (2008. December 2). *Policy roundtables: Fidelity and Bundled Rebates and Discounts.* DAF/COMP(2008)29. Available at: http://www.oecd.org/dataoecd/41/22/41772877.pdf.
[48] Elhauge, E., & Geradin, D. (2007). *Global Competition Law and Economics.* Oxford and Portland Oregon: Hart Publishing, p. 626.
[49] Elhermann C.D., & Marquie M. (Eds). (2008). *European Competition law annual: 2007. A Reformed Approach to Article 82 EC.* Oxford and Portland Oregon: Hart Publishing, p. 257.
[50] *Ibid*.

purchases from the dominant firm are overwhelming.[51] Thus, Bishop concludes that the determinant is the dominant position. Hence it follows that not being in a dominant position would not raise anti-competitive foreclosure, and that the Commission is placing too much emphasis on the dominant position. Simon Bishop comments that "…dominance can be described as the elephant in the room."[52]

Thus it can be concluded that firms not in a dominant position should be safe when using rebate strategies because no abuse in their behaviour will be established. Quite the reverse, it can be concluded that the risk of being punished appears from Commission efforts to prove a dominant position. The second criterion – abuse of a dominant position, according to Bishop is becoming "meaningless or empty, in the sense that any harm inflicted on competition is assumed to cause harm to competition."[53] Thus it seems that pro-competitive rebates exist only when an undertaking is not in a dominant position, otherwise rebates turn out to be anti-competitive.

Damien Geradin notes that he faced a complication during analysis of the Sherman Act and TFEU Article 102, because he has a similar notion, namely that EU case law establishes a *per se* rule of rebate illegality.[54]

Rafael Allendesalazar comments on Damien Geradin regarding business justification for rebates:

> Of course rebates are fidelity-enhancing. That`s precisely the objective: a dominant firm offers rebates because it wants its clients to buy more of its products. That`s the logic of it. If the competitor authority says, yes, but under these specific circumstances, the rebate produces anti-competitive effects, only *then* would it be appropriate to look at whether the rebate can be justified. It would be *inappropriate* to require a dominant firm to offer such a justification at an initial stage before there has been any showing of specific anti-competitive harm.[55]

Damien Geradin asserts that rebates should not be assessed under *per se* rules because

> …relying on a *per se rule* of illegality would lead to the prohibition of many pro-competitive rebates and would discourage price competition, which is the very behavior antitrust laws should seek to encourage and protect. Instead, competition authorities should adopt an *effect-based* test focusing on

[51] Elhermann C.D., & Marquie M. (Eds). (2008). *European Competition law annual: 2007. A Reformed Approach to Article 82 EC.* Oxford and Portland Oregon: Hart Publishing, pp. 257-258.
[52] *Ibid*., p. 257.
[53] *Ibid*.
[54] *Ibid*., p. 269.
[55] *Ibid*., p. 271.

> the foreclosure effects that can be generated by a rebate granted by a dominant firm and balancing such effects with the efficiencies such a rebate may also create.[56]

In his article "A proposed Test for Separating Pro-competitive Conditional Rebates from Anti-competitive Ones", he proposes a three-step test to distinguish pro-competitive rebates from anti-competitive rebates. These three proposed approaches are not reviewed in this diploma project due to the limited scope of the research.

Pro-competitive rebates turned out to be anti-competitive in several cases in EU case law history, and not a single case has an undertaking won against the Commission. The Commission has made no positive decisions where rebate strategy *per se* would be assumed to be pro-competitive. The *Intel* case is unique in the amount of the penalty (EUR 1 060 000 000). In the past, harm to consumers caused by abuse of a dominant position, particularly in the information technology industry, was not that huge – the greatest fine imposed was on Microsoft: EUR 497 196 304.[57] One more interesting obstacle in the *Intel* case is that the lawsuit is still ongoing at the moment – Intel is appealing the Commission decision.[58]

The Economist recently published an article criticizing the Commission for being prosecutor, judge, and jury and asserting the need to change the rules under which the competition directorate operates.[59] Three main objections were highlighted:

1) the conflicting role of the case teams when the competition directorate decides to investigate a complaint about abusive behaviour from a business rival with potentially anti-competitive consequences;
2) the company is denied a fair hearing, as it is heard only by the case team, not a neutral judge or hearing officer;
3) the final decision on culpability is taken on a vote by 27 politically appointed commissioners, only one of whom may have attended the defendant's hearing.[60]

Currently, much criticism is levelled at Commission action, especially after the *Intel* case decision. The whole adjudication process in the EU has come under criticism, in particular the obsolete approaches used by the Commission in distinguishing pro-competitive from anti-competitive rebates. Apparently, Commission decision makers should implement changes and revise their decision making process.

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[56] Geradin D. (2009). A proposed Test for Separating Pro-competitive Conditional Rebates from Anti-competitive Ones. *World Competition, 32*, 41-70, p. 46.
[57] Case T-201/04, *Microsoft Corp. v Commission*, [2004] ECR II-4463, para. 1080.
[58] Case T-286/09, *Intel v Commission*, Application, [2009] OJ C220.
[59] Competition policy: Prosecutor, judge and jury. (2010, February 20). The *Economist, 950*, p. 57.
[60] *Ibid.*

3.2. Business theory

From the business point of view, rebates are recognized as pro-competitive tools. Today, the leading business strategy expert is Professor Michael E. Porter. In his work "On Competition", Porter defines five competitive forces that shape company strategy: supplier power, customer power, established rivals, new entrants, and substitutes.[61]

Porter`s five competitive forces model is unique and applicable to every industry. The idea of the five competitive forces model is to give an appropriate tool to enable company managers to analyse what kind of competitive forces influence profitability in a certain industry. Thus, knowledgeable managers would be able to develop a competitive and profitable strategy for their company with the aim of positioning their company where competitive forces are the weakest, resulting in more efficient competition with their rivals. Porter notes: "The strength of the competitive forces affects prices, costs, and the investment required to compete; thus the forces are directly tied to the income statements and balance sheets of industry participants."[62]

Supplier power reflects how the suppliers of raw materials or finished goods may affect the manufacturer. Intel's main product is CPU. The products are manufactured by Intel and in this case suppliers would be raw material, vendors, and packaging suppliers. CPUs are made from Silicon dioxide (SiO2), mainly extracted from sand refined with quartz. Then Silicon is melted and turned into mono-crystal silicon-ingot, which is cut into wafers. "Intel buys those manufacturing ready wafers from third party companies."[63] Except for silicon wafer key suppliers, Intel cooperates with other suppliers as well. In their press release of 3 March 2010, Intel honoured 16 companies with their Preferred Quality Supplier award.[64] Thus, from empirical observation it can be concluded that Intel has a wide range of suppliers that have to compete with each other and as a result supplier power is not strong. Additionally, an assumption can be made that those suppliers that manufacture wafers will have high switching costs, because this is a highly specific product. Moreover, suppliers of

[61] Porter M. (2008). The Five Competitive Forces That Shape Strategy. *Harvard Business Review*, p. 1.
[62] Porter E.M. (2008). *On Competition, updated and expanded edition.* Boston: Harvard Business School Publishing, p. 5.
[63] Intel Corp. (2009, May). *From Sand to Silicon. "Making of a Chip" Illustrations.* Available at: http://download.intel.com/pressroom/kits/chipmaking/Making_of_a_Chip.pdf.
[64] Intel Corp. (2010, March 3). *Intel Honors 16 Companies with Preferred Quality Supplier Award*. Available at: http://www.intel.com/pressroom/archive/releases/2010/20100303corp_a.htm.

ready wafers depend on the industry for their revenues.[65] Those factors minimise supplier power.

Customer power, or the power of buyers, is a crucial element for Intel because CPUs are a high-end product with high production costs. One full truck of CPUs might cost a million dollars. For example, price per unit for product i7-980X[66] in March 2010 was $999.[67] Assuming that 1000pcs of CPUs may be loaded in one truck, the total value of these products would be $999 000. Therefore Intel needs efficient supply chain management. The company has to implement an excellent marketing strategy in order to generate demand for their products. Selling high cost products implies maintaining lower inventory level and high stock rotation. Thus, Intel needs a loyal customer base that generates stable demand. Taking into account Intel supply chain management specifics, mainly all products are sold to OEMs. The biggest OEMs are HP and Dell, representing 20% (HP) and 18% (Dell) of Intel revenue in 2008.[68] According to Porter, buyer power is strong if "[t]here are few buyers, or each one purchases in volumes that are large relative to the size of a single vendor."[69] Additionally to OEMs as customers, there are also intermediate customers: "...customers who purchase the product but are not the end user (such as assemblers or distribution channels). These can be analysed in the same way as other buyers, with one important addition."[70] In the *Intel* case such an intermediate customer is consumer electronics retailer MSH. Hence, as those customers are most important in Intel's business, the main focus should be turned to them. As a result, Intel is constantly inventing different marketing strategies (for example its rebate strategy) and expanding services with the aim of keeping customer loyalty. The high possibility that customers may switch to a rival shows strong customer power in Intel's business.

Established rivals are few for Intel. As established in the *Intel* case, Intel has around 80% of market share overall in the x86 CPU market.[71] This means that Intel has a strong position in the market. The strongest rival for Intel is AMD, as is also mentioned in the *Intel*

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[65] Porter E.M. (2008). *On Competition, updated and expanded edition.* Boston: Harvard Business School Publishing, p. 13.
[66] Intel Corp. (2010, March 10). *Intel Spotlights New Extreme Edition Processor, Software Developer Resources at Game Conference.* Available at: http://www.intel.com/pressroom/archive/releases/2010/20100310comp.htm.
[67] Corp. (2010, March 14). *Intel Processor Pricing.* Available at: http://files.shareholder.com/downloads/INTC/779577209x0x357729/DEEBEE81-C386-4EB8-8D9D-F0EA06C57797/Mar_14_10_1ku_Price.pdf.
[68] Intel Corp. (n.d.). *2008 Annual Report. Business.* Available at: http://www.intc.com/intelAR2008/common/pdfs/Intel_2008_Business.pdf.
[69] Porter M. (2008). The Five Competitive Forces That Shape Strategy. *Harvard Business Review*, p. 15.
[70] *Ibid*., p. 16.
[71] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 852.

case: "…it is important to note that there are only two meaningful players on the market for x86 CPU production, Intel and AMD."[72] Currently, it seems that AMD is competing by means of legal proceedings strategy rather than marketing strategies. Established rival power is weaker than customer power. Of course, AMD is a powerful rival for Intel and it was exactly because of this rivalry that the *Intel* case started. Nevertheless, the power of established rivals is weak compared to buyer power, though much stronger than other powers, even if there is only one powerful rival. Professor Porter notes that "…eliminating rivals is a risky strategy."[73]

New entrants to the CPU market will face considerable difficulties, the main one being intellectual property requirements. First, building a CPU is highly complicated because of the technical knowledge required. Second, research and development (R&D) for such a product would require significant financial resources, as would building new competitive products. Thus competition with market leaders would be almost impossible. Market leaders already enjoy supply-side production economies of scale and demand-side benefits from their existing customer network. The Commission also stated in the *Intel* case, referring to AMD's submission of 27 June 2006, p. 1: "…both AMD and Intel have a long history of developing x86 CPUs and have built a significant knowledge base which it will be very costly for a new entrant to replicate."[74] Moreover, AMD noted in its submission of 27 June 2006, p. 1: "…the development of a new generation of [x86] CPUs may take 2.5 years and amount to an R&D expenditure of more than USD 300 million."[75] Thus, high entry barriers to the CPU market exist, so that new entrants' power is weak. Porter also agrees with this statement: "[i]n microprocessors, incumbents such as Intel are protected by scale of economies in research, chip fabrication, and consumer marketing."[76]

Substitutes for the CPU market might be dual. Substitution could occur between CPUs for desktop computers, laptop computers, and server computers. Substitution could also occur between computers, CPUs, and other electronic device CPUs. Substitution between computers was analysed by the Commission in the *Intel* case. The Commission analysed demand-side and supply-side substitution and concluded: "...there is demand-side

[72] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 1781.
[73] Porter M. (2008). The Five Competitive Forces That Shape Strategy. *Harvard Business Review*, p. 12.
[74] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 129.
[75] *Ibid.*, para. 821.
[76] Porter E.M. (2008). *On Competition, updated and expanded edition.* Boston: Harvard Business School Publishing, p. 10.

substitution between CPUs destined for the business/commercial segment and CPUs destined for the private/consumer segment [...] there is no demand-side substitution between non-x86 CPUs and x86 CPUs."[77] If there is substitution between CPUs for desktop computers, laptop computers and server computers, the Commission left this question open.[78] As to supply-side substitution, the conclusion is the same: "...is likely to be supply-side substitutability between CPUs for desktop computers, laptop computers and server computers."[79] The Commission also concluded that there was no "...supply-side substitution between non-x86 CPUs and x86 CPUs."[80] On the other hand, substitution between computers, CPUs, and other electronic devices with a similar function to CPUs can be compared as follows: whether the finished product computer with main component CPUs might be substituted by another finished product but not a computer, for example mobile smart phones. The Commission defined that substitution as "...substitution between CPUs for non-computer devices and CPUs for computers"[81] and also concluded that "...there is no demand-side substitution between CPUs for non-computer devices and CPUs for computers [...] there is no supply-side substitution between CPUs for non-computer devices and CPUs for computers."[82] Thus, as there is no substitution between computers, CPUs, and other electronic device CPUs, substitution power is weak. Weak power of substitution according to Porter might also be concluded from the obviously high cost to customers of switching to a substitute, even if substitution were available.[83]

It can be concluded that the Intel rebate strategy aligns with Porter's "Five Competitive Forces" theory and proves it. As the strongest force is customer power, Intel's implemented rebate strategy serves to generate demand from customers and to aid competition against established rivals. Therefore Intel's execution of its rebate strategy is logical and correct from a business competition theory point of view.

[77] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 814.
[78] *Ibid*.
[79] *Ibid.*, para. 819.
[80] *Ibid*., para. 824.
[81] *Ibid*., para. 808.
[82] *Ibid*., para. 831.
[83] Porter E.M. (2008). *On Competition, updated and expanded edition*. Boston: Harvard Business School Publishing, p. 18.

4. Methodology

This diploma project adopts a qualitative focus on the rebate strategy problem. Much of the data comes from primary sources in the shape of EU and US case law studies. Methodology in collecting case law data is based on two criteria: 1) cases involving abuse of a dominant position 2) abuse of a dominant position involving rebate strategy. The main reason for these two criteria is to explore the *Intel* case deeply in correlation with similar cases within the EU and the US.

In summary of case law data, certain argumentation used by the competition authorities in their decisions is analysed:

a) finding of a dominant position;

b) finding of abuse of a dominant position;

c) definition of terms: pro-competitive and anti-competitive rebates.

The validity and reliability of collected data is ensured by the fact that data are created by a competent legal institution. All decisions in every item of case law are made in accordance with the law of each particular country or union of countries. Thus, in selecting case law data, it is presumed that all decisions made by the competition authorities are made legally *per se*.

Case law research analyses and compares the approaches of the EU and the US. That is, certain argumentation practice in decisions of the EU competition authority is compared to certain argumentation practice in decisions of the US competition authority. Great effort has been devoted to analysis of business validity used in decision argumentation. All empirical bases for the research are presented mainly by the *Intel* case except for information of a confidential nature. The purpose of the research is not to reject findings of a dominant position as a fact or findings of abuse of a dominant position as a fact. The purpose of the research is to clarify the element of business validity used in decision argumentation in regard to rebate strategies.

5. Research and discussion

5.1. EU case law studies

The EU case law studies section of this diploma project focuses on EU cases falling under TFEU Article 102. The main aim of this section is to analyse argumentation which the

competition authorities use in their decisions in those cases where companies` rebate strategies are found anti-competitive. Therefore, the criteria in selecting case studies are: 1) cases involving abuse of a dominant position within the EU; 2) abuse of a dominant position is committed by using a rebate strategy.

When looking at the argumentation used in competition authorities' decisions, it is necessary to analyse the objectives of TFEU Article 102. The TFEU does not provide a single certain and clear definition of terms: dominant position, abuse of a dominant position, anti-competitive rebates. All definitions of these terms can only be found in decisions of particular cases; hence, the diversity of cases and the time scale of cases have widened the interpretation of TFEU Article 102. The once very narrow interpretation corridor of TFEU Article 102 can already be compared to a wide interpretation tunnel more recently. At the end of the twentieth century, Christian Joerges expressed a similar opinion: "European law has a lot in common with a sleeping dog. It is there, but does not get much attention. And yet, suddenly the sleeping dog becomes a watchdog; all of a sudden it wakes up – and bites."[84]

Abuse of dominant position

One definition of the term "dominant position" appears in the *Continental Can* case.[85] To be found to be in a dominant position, undertakings should have power to act independently from other competitors, suppliers, or purchasers. The important condition that affects the essence of a dominant position is the market share which the undertaking enjoys. In *Continental Can* it was stressed that the undertaking is empowered to behave independently by determining prices or by controlling production or a significant part of production. Thus, it is not necessary to have full dominance in actions in a certain market, but it is enough to have significant power to influence the market without taking into account other players in the same market.

A clearer definition of a dominant position can be found in *Hoffmann-La Roche*.[86] The Commission defined this as follows:

> …Dominant position relates to a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, its customers and ultimately of the consumers. Such a position does not

[84] Neergaard U.B. (1998). *Competition and competences: The tensions between European competition law and anti-competitive measures by the Member States*. Copenhagen: DJOF Publishing, p.V.
[85] Case 6/72, *Europemballage Corporation and Continental Can Co. Inc v Commission*, [1973] ECR 215.
[86] Case 86/76, *Hoffmann-La Roche and Co.AG v Commission*, [1979] ECR 461.

> preclude some competition, which it does where there is a monopoly or a quasi-monopoly, but enables the undertaking which profits by it, if not to determine, at least to have an appreciable influence on the conditions under which that competition will develop, and in any case to act largely in disregard of it so long as such conduct does not operate to its detriment.[87]

A similar but more precise definition of the term "dominant position" further appears in *Michelin.*[88] The Commission defined:

> [a] dominant position [a]s a position of economic strength enjoyed by an undertaking which enables it to hinder the maintenance of effective competition on the relevant market by allowing it to behave to an appreciable extent independently of its competitors and customers and ultimately of consumers.[89]

Hence the economic strength to behave independently in the relevant market is emphasised. Later in the judgment it is stressed that the relevant market should be taken into account in order to investigate the possibly dominant position of the undertaking. This involves analysing product characteristics and supply and demand on the market as well. Thus the Commission highlights the need to delimit the relevant market from the geographical market.[90]

As a result, additionally to economic strength and independent behaviour (to some extent) on the market, two terms appear in the Commission interpretation of TFEU Article 102: relevant product market and relevant geographical market. After *Hoffmann-La Roche* and *Michelin*, the Commission considers relevant product market and relevant geographical market in every case falling under TFEU Article 102.

In the *Intel* case, the Commission in defining the relevant market followed not only the definitions from previous case judgments, but followed more current documents such as the "Commission Notice on the definition of relevant market for the purposes of Community competition law" ("the Commission Notice").[91] The Commission Notice was used in analysis of demand-side substitution and supply-side substitution in the *Intel* case.[92] In the Commission Notice, demand-side is defined as:

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[87] Case 86/76, *Hoffmann-La Roche and Co. AG v Commission*, [1979] ECR 461, para. 4.
[88] Case 322/81, *Michelin v Commission*, [1983] ECR 3461.
[89] *Ibid.*, para. 6.
[90] *Ibid.*, para. 21.
[91] Commission notice on the definition of the relevant market for the purposes of Community competition law [1997] OJ C372.
[92] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, paras 793 and 816.

> [f]rom an economic point of view, for the definition of the relevant market, demand substitution constitutes the most immediate and effective disciplinary force on the suppliers of a given product, in particular in relation to their pricing decisions[93]

and supply-side is defined as:

> supply-side substitutability may also be taken into account when defining markets in those situations in which its effects are equivalent to those of demand substitution in terms of effectiveness and immediacy.[94]

Thus, the Commission in their most recent decisions, when operating with the terms "relevant product market" and "relevant geographical market", stick to the definitions provided in the Commission Notice:

1. A relevant product market comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their prices and their intended use.[95]
2. The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those area.[96]

It can be concluded that the Commission does not have a detailed formula for defining a dominant position due to the fact that every undertaking is different and unique. According to the case law, identifying an undertaking being in a dominant position is highly complex so that the dominance of each undertaking should be analysed within every particular case. Such indicators as economic strength, market power, the notion of individual behaviour, market share size, relevant product market, and relevant geographical market are interpreted ever more widely with every year that passes.

In the recent *Intel* case the Commission analysed Intel dominance in accordance with already mentioned case law such as *Michelin* and *Continental Can* and in accordance with *Tetra Pak v Commission*,[97] *Promedia v Commission*,[98] *Irish Sugar v Commission*,[99] *United*

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[93] Commission notice on the definition of the relevant market for the purposes of Community competition law [1997] OJ C372, para. 13.
[94] *Ibid*., para. 20.
[95] *Ibid*., para. 7.
[96] *Ibid*., para. 8.
[97] Case T-83/91, *Tetra Pak v Commission*, [1994] ECR II-755. From here on in main text referred to simply as "*Tetra Pak*" or "the *Tetra Pak* case".
[98] Case T-111/96, *ITT Promedia NV v Commission*, [1998] ECR II-2937. From here on in main text referred to simply as "*Promedia*" or "the *Promedia* case".

Brands and United Brands Continental v Commission,[100] and *Atlantic Container Line* and *Others v Commission*.[101]

In *Tetra Pak* the Commission in defining the relevant product market and the geographical market concluded that "Tetra Pak held approximately 89% of the market in aseptic cartons and 92% of that in aseptic machines in the same territory."[102] In *Promedia* it was easier for the Commission to define a dominant position because "Belgacom had a statutory monopoly in respect of voice telephony services in Belgium until 1 January 1998."[103] Thus, there was no discussion determining market share size. In *Irish Sugar* in summary it is stated "[a] market share of over 50% in itself constitutes evidence of the existence of a dominant position on the market in question."[104] In *United Brands* it is stated "…that UBC [United Brands Continental]`s share of the relevant market is always more than 40% and nearly 45%."[105] Thus, to be found to be in a dominant position, the Commission determined a limit of market share of 40%. Unfortunately, in the *Intel* case the *Atlantic Container Line* case is not related to a dominant position at all.

As a result, the main argument in identifying Intel as being in a dominant position is based on size of market share: "[i]n this regard, the Commission will first assess market shares in the relevant market (section 3.2), and will then analyse barriers to expansion and entry in the market (section 3.3)."[106] In its analysis regarding the relevant geographical market of Intel the Commission concluded that the geographical market of Intel is worldwide.[107] The legal logic of the market shares argument is understandable, but in the *Intel* case it is clear to every person familiar with the information technology industry that Intel's worldwide CPU market share is obviously much higher than any other competitor. Hence, according to the Commission's conclusion, it is possible to assume that size of market share is the main criterion for holding a dominant position *per se*. Indirectly the Commission

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[99] Case T-228/97, *Irish Sugar plc v Commission*, [2001] ECR I-5333. From here on in main text referred to simply as "*Irish Sugar*" or "the *Irish Sugar* case".
[100] Case 27/76, *United Brands Company and United Brands Continental BV v Commission*, [1978] ECR 207. From here on in main text referred to simply as "*United Brands*" or "the *United Brands* case".
[101] Case T-395/94, *Atlantic Container Line and Others v Commission*, [1995] ECR II-595. From here on in main text referred to simply as "*Atlantic Container Line*" or "the *Atlantic Container Line* case".
[102] Case T-83/91, *Tetra Pak v Commission*, [1994] ECR II-755, para. 13.
[103] Case T-111/96, *ITT Promedia NV v Commission*, [1998] ECR II-2937, para. 3.
[104] Case T-228/97, *Irish Sugar plc v Commission*, [2001] ECR I-5333, para. 4.
[105] Case 27/76, *United Brands Company and United Brands Continental BV v Commission*, [1978] ECR 207, para. 108.
[106] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 840.
[107] *Ibid*., para. 836.

agrees with this opinion in *Hoffmann-La Roche*: "…very large market shares are highly significant evidence of the existence of a dominant position…"[108]

Massimo Motta especially stresses the importance of the two components of TFEU Article 102: a dominant position and abuse of a dominant position.[109] Thus, to be dominant in the market or to be in a dominant position is not illegal according to EU law – what is illegal is abuse of a dominant position, as is precisely stated in TFEU Article 102.

According to Massimo Motta, it is perfectly legal that a company in the market builds strong market power by using different marketing strategies.[110] The concluding part of the *Intel* case states that Intel`s abuse of a dominant position was committed by granting rebates to certain customers. Moreover, the term "rebates" in the body of the *Intel* case is defined as conditional rebates.[111]

Any company can be in a dominant position and implement competitive marketing strategies. These activities, by default, cannot be recognized as an abuse of a dominant position. As regards business perspectives or theory of economic efficiency, Massimo Motta points out that EU law "…does not want to punish firms just because they are better, more successful, or even luckier, than others, as this would reduce incentives for firms."[112]

Abuse of a dominant position was defined in *Hoffmann-La Roche*:[113]

> [t]he concept of abuse is an objective concept relating to the behaviour of an undertaking in a dominant position which is such as to influence the structure of a market where, as a result of the very presence of the undertaking in question, the degree of competition is weakened and which, through recourse to methods different from those which condition normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition.

Michelin,[114] in addition to referring to *Hoffmann-La Roche*, argues that "[f]or the purposes of establishing an infringement of Article 82 EC [TFEU Article 102], it is sufficient to show that the abusive conduct of the undertaking in a dominant position tends to restrict

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[108] Case 86/76, *Hoffmann-La Roche and Co. AG v Commission*, [1979] ECR 461, para. 5.
[109] Motta, M. (2004). *Competition Policy: Theory and Practice.* New York: Cambridge University Press, p. 34.
[110] *Ibid.*, p. 35.
[111] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 925.
[112] Motta, M. (2004). *Competition Policy: Theory and Practice.* New York: Cambridge University Press, p. 36.
[113] Case 86/76, *Hoffmann-La Roche and Co.AG v Commission*, [1979] ECR 461, para. 91.
[114] Case T-203/01, *Michelin* v *Commission*, [2003] ECR II-407, para. 239.

competition or, in other words, that the conduct is capable of having that effect." The Court went even further in *Compagnie Maritime Belge*:[115]

> …the fact that the result sought is not achieved is not enough to avoid the practice being characterized as an abuse of a dominant position within the meaning of Article 86 [TFEU Article 102] of the Treaty. […] The fact that [competitor's] market share increased does not mean that the practice was without any effect, given that, if the practice had not been implemented, [competitor's] share might have increased more significantly.

In *France Telecom*[116] the Court rejected the appellant's claims by stating that

> …the lack of any possibility of recoupment of losses is not sufficient to prevent the undertaking concerned reinforcing its dominant position, in particular, following the withdrawal from the market of one or a number of competitors, so that the degree of competition existing on the market, already weakened precisely because of the presence of the undertaking concerned, is further reduced and customers suffer loss as a result of the limitation of the choices available to them.

The Court of First Instance used similar reasoning to that in *France Telecom* in its *British Airways*[117] ruling, when declining British Airways' argument that its activities had no exclusionary effect on the market. The Court on appeal sustained the reasoning of the Court of First Instance by noting that "…in paragraphs 272 and 273 of the judgment under appeal, the Court of First Instance explained the mechanism of those schemes."[118] In the *Intel* case, abuse of a dominant position in the Commission decision was also based on such case law as: *Kanal 5 and TV 4*,[119] *AKZO v Commission*,[120] and *Irish Sugar*.[121]

Quantity discounts and fidelity rebates

Abuse of a dominant position in this diploma project is analysed only within the frame of abuse of a dominant position resulting from using rebates. The first definitions of quantity discounts and fidelity rebates appear in *Hoffmann-La Roche*: "…a system of fidelity

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[115] Joined Cases T-24/93, T-25/93, T-26/93, T-28/93, *Compagnie maritime belge transports SA and Compagnie maritime belge SA, Dafra-Lines A/S, Deutsche Afrika-Linien GmbH & Co. and Nedlloyd Lijnen BV v Commission*, [1996] ECR II-01201, para. 149.
[116] Case C-202/07, *France Télécom SA v Commission*, [2009] ECR 00000. From here on referred to in main text simply as "*France Télécom*"or "the *France Télécom* case".
[117] Case T-219/99 , *British Airways plc v Commission*, [2003] ECR II-05917, para. 293. From here on referred to in main text simply as "*British Airways*" or "the *British Airways* case".
[118] Case C-95/04 P, *British Airways plc v Commission*, [2007] ECR I-2331, para. 96.
[119] Case C-52/07, *Kanal 5 and TV 4*, [2009] OJ C 32.
[120] Case C-62/86, *AKZO Chemie BV v Commission*, [1991] ECR II-2969, para. 70.
[121] Case T-228/97, *Irish Sugar plc v Commission*, [2001] ECR I-5333, para. 111.

rebates, that is to say discounts conditional on the customers…";[122] and "…the fidelity rebate, unlike quantity rebates exclusively linked with the volume of purchases from the producer concerned, is designed through the grant of a financial advantage to prevent customers from obtaining their supplies from competing producers…";[123] and "…the effect of fidelity rebates is to apply dissimilar conditions to equivalent transactions with the other trading parties in that two purchasers pay a different price for the same quantity of the same product depending on whether they obtain their supplies exclusively from the undertaking in a dominant position or have several sources of supply."[124]

Abuse of a dominant position in implementing rebate strategies by La Roche was found to be an abuse within the meaning of TFEU Article 102 according to the Commission:

> ...the exclusivity agreements and the fidelity rebates complained of are an abuse..., on the one hand, because they distort competition between producers by depriving customers of the undertaking in a dominant position of the opportunity to choose their sources of supply and, on the other hand, because their effect was to apply dissimilar conditions to equivalent transactions with other trading partners, thereby placing them at a competitive disadvantage, un that Roche offers two purchasers two different prices for an identical quantity of the same product depending on whether these two buyers agree or not to forego obtaining their supplies from Roche`s competitors.[125]

As a result, the rebate strategy implemented by La Roche in contracts with their partners was regarded as a fidelity rebate and found to be an abuse of a dominant position. That was the first case law and the first such interpretation of TFEU Article 102.

Furthermore in *Michelin* a definition for quantity discount and loyalty rebates appears: "…quantity discount, which is linked solely to the volume of purchases from the manufacturer concerned, a loyalty rebate, which by offering customers financial advantages tends to prevent them from obtaining their supplies from competing manufacturers…"[126]

In the *Intel* case conditional rebates are introduced based on case law:

> …an undertaking which is in a dominant position on a market and ties purchasers - even if it does so at their request - by an obligation or promise on their part to obtain all or most of their requirements exclusively from the said undertaking abuses its dominant position within the meaning of Article 82 EC [TFEU Article 102], whether the obligation in

[122] Case 86/76, *Hoffmann-La Roche and Co.AG v Commission*, [1979] ECR 461, para. 7.
[123] *Ibid*., para. 90.
[124] *Ibid*., para. 8.
[125] *Ibid*., para. 80.
[126] *Ibid*., para. 13.

> question is stipulated without further qualification or whether it is undertaken in consideration of the grant of a rebate. The same applies if the said undertaking, without tying the purchasers by a formal obligation, applies, either under the terms of agreements concluded with these purchasers or unilaterally, a system of fidelity rebates, that is to say discounts conditional on the customer's obtaining all or most of its requirements - whether the quantity of its purchases be large or small - from the undertaking in a dominant position […] the extent that a rebate prevents customers from obtaining supplies from competitors of the dominant firm, the same legal assessment may apply if the rebate applies only to a segment of the identified market.[127]

For the ground for conditional rebates in the *Intel* case, the Commission draws from several already judged cases.

Nicholas Economides comments on the Commission decision in that the contestable part of the market can be small: "[t]he impact of the loyalty discount is correctly applied to the contested units, where its effect is large, rather than to all units, which include the portion of the monopolist`s sales that are not contested and would have remained with the monopolist in the absence of a discount."[128] The same author further concludes that the Commission price-cost test is better than others, but it does "…not tak[e] into account product differentiation and the fact that even a inefficient competitor can constrain a dominant firm`s pricing and thereby increase consumer surplus."[129]

The Guidance

A year ago, on 29 February 2009, the Commission issued the Guidance on the Commission`s enforcement priorities in applying TFEU Article 102 to abusive exclusionary conduct by a dominant undertaking ("the Guidance").[130] In the Guidance, the Commission coordinates the approach on determining market power, how to define consumer harm, and on defining special forms of abuse, such as exclusive dealing, tying and bundling, predation and refusal to supply and margin squeeze.

When determining market power, the Commission refers to the capability of an undertaking to profitably increase prices above a competitive level for a significant period. "Increase prices" includes the power to maintain prices above a competitive level and is used

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[127] Case 86/76, *Hoffmann-La Roche and Co. AG v Commission*, [1979] ECR 461, para. 921.
[128] Economides N. (2009, June 29). *Loyalty/Requirement Rebates and the Antitrust Modernization Commission: What is the Appropriate Liability Standard?* Available at: http://ssrn.com/abstract=1370699.
[129] *Ibid.*
[130] Communication from the Commission — Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings [2009] OJ C45.

as shorthand for the various ways in which the parameters of competition, such as prices, output innovation, the variety or quality of goods or services can be influenced to the advantage of a dominant undertaking and to the detriment of consumers.[131] The Commission indicates that market share provides a useful first indication, but other factors such as market conditions will be assessed, as well as entry barriers and countervailing buyer power.[132]

Regarding conditional rebates, the Commission defines these as rebates granted to customers to reward them for a particular form of purchasing behaviour. The usual nature of a conditional rebate is that the customer is given a rebate if its purchases over a defined reference period exceed a certain threshold, the rebate being granted either on all purchases (retroactive rebates) or only on those made in excess of those required to achieve the threshold (incremental rebates). These rebates by themselves are not illegal, yet if used by dominant undertakings can also have actual or potential foreclosure effects on competition.[133]

When evaluating the effects of rebates on the market, the Commission will calculate the long-run average incremental cost (LRAIC) and the average avoidable cost (AAC) of the dominant undertaking. If the effective price is consistently above the LRAIC of the dominant undertaking, this would normally allow an equally efficient competitor to compete profitably notwithstanding the rebate. The Commission states that in those circumstances the rebate is normally not capable of foreclosing anti-competitively. On the other hand, if the effective price is below AAC, as a general rule the rebate scheme is capable of foreclosing even equally efficient competitors. When effective price is between AAC and LRAIC, the Commission will investigate by evaluating other factors.[134]

The Guidance has introduced a long awaited economic approach to competition investigations by explaining the factors that the Commission considers during an investigation. Regarding abuse of a dominant position by rebate strategies, the Commission introduces LRAIC and AAC, which were not expressly examined in previous case law.

Richard Duncan states that the "Guidance thus eschews any strict requirement of below-cost pricing before a dominant firm`s loyalty rebate programme can violate art.82

[131] Communication from the Commission — Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings [2009] OJ C45., C45/8.
[132] *Ibid.*, p. 9.
[133] *Ibid.*, p. 13.
[134] *Ibid.*

[TFEU Article 102], a position consistent with 30 years of decisions by the ECJ [the European Court of Justice]."[135]

Damien Geradin points out: "Although this Guidance paper is not flawless, it was seen as a positive development by the vast majority of commentators as it "modernized" the application of Article 82 EC [TFEU Article 102]."[136]

However, in the *Intel* case, when the Guidance was to be applicable, the Commission seems to be returning to the older case law and has not relied on the Guidance as would be expected. In the *Intel* case the Commission stated that "...the Guidance paper is not intended to constitute a statement of the law and is without prejudice to the interpretation of Article 82 [TFEU Article 102] by the Court of Justice or the Court of First Instance."[137]

5.2. US case law studies

The US case law studies session of this diploma project focuses on US cases falling under the US Sherman Act ("the Sherman Act"). The main aim of this section is to analyse the argumentation of competition authorities used in their decisions in those cases where undertakings` rebate strategies are found to be anti-competitive. Therefore, the criteria in selecting case studies are: 1) cases involving abuse of a dominant position or monopolisation within the US; 2) abuse of a dominant position or monopolisation involves a rebate strategy.

The Sherman Act, Section 1, prohibits contracts which restrain trade: "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal."[138] Further, Section 2 prohibits monopolization: "[e]very person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony…"[139] Dominant position regulation under the EU TFEU Article 102 is similar to monopoly regulation under the Sherman Act Section 2.

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[135] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3)*, p. 169.

[136] Geradin. D. (2009, October 16). *The Decision of The Commission of 13th May 2009 in the Intel Case: Where is the foreclosure and consumer harm?* Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1490114

[137] Summary of Commission Decision of 13 May 2009 relating to a proceeding under Article 82 of the EC Treaty and Article 54 of the EEA Agreement (Case COMP/C-3/37.990 — Intel), [2009] OJ C227/07, para. 916.

[138] The Sherman Antitrust Act, 15 U.S.C.A. § 2 (1890).

[139] *Ibid*.

The US Department of Justice ("the DOJ") in 2008 issued a competition and monopoly report on single-firm conduct under Section 2 of the Sherman Act ("the Report").[140] The EU Guidance is similar to the Report. The Report coordinates the approach on how to determine monopoly power, includes standards for exclusionary conduct, price predation and tying, bundled discounts and single-product discounts, refusal to deal with rivals and exclusive deals.

The Report has already been criticised by the Federal Trade Commission (FTC): "[t]hree of the five FTC Commissioners went so far as to issue a public statement rebuking the DOJ Report as placing the interests of firms with monopoly power "ahead of consumers"."[141] FTC Commissioners Harbour, Leibownitz, and Rosch stated: "[t]he Report also goes beyond the holdings of the Supreme Court cases upon which it relies. The Federal Trade Commission (FTC) does not endorse the Department's Report."[142]

Monopoly

The DOJ identifies monopoly power in the Report:

> …monopoly power is conventionally demonstrated by showing that both (1) the firm has (or in the case of attempted monopolization, has a dangerous probability of attaining) a high share of a relevant market and (2) there are entry barriers - perhaps ones created by the firm's conduct itself – that permit the firm to exercise substantial market power for an appreciable period. Unless these conditions are met, defendant is unlikely to have either the incentive or ability to exclude competition.[143]

In determining whether a competitor possesses monopoly power in a relevant market, courts typically begin by looking at the firm's market share. Although the courts "…"have not yet identified a precise level at which monopoly power will be inferred," they have required a dominant market share.[144]

Thus the US authorities also focus on firm high share of the relevant market to determine monopoly power. Based on case law analysis, the DOJ states that "…market share

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[140] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[141] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3)*, p. 148.
[142] *Statement of Commissioners Harbour, Leibowitz and Rosch on the issuance of the Section 2 Report by the Department of Justice*. Available at: http://www.ftc.gov/os/2008/09/080908section2stmt.pdf.
[143] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[144] *Ibid*.

of greater than fifty percent has been necessary for courts to find the existence of monopoly power."[145]

Monopoly power in the US is distinguished from the EU term dominant position. Defining the significance of a dominant market share, the DOJ stated: "…monopoly power requires more than a dominant market share."[146] A high market share does not mean that monopoly power exists *per se*, but it is "…one of the most important factors in the Department`s examination of whether a firm has, or has a dangerous probability of obtaining, monopoly power."[147]

Richard Duncan with reference to the *DuPont* case[148] notes: "...US courts have always relied heavily (although not exclusively) on market share data to serve as a filter or screen."[149] Additionally, beside the market share approach stated in the Report, monopoly power may also be seen as direct evidence of high profits, price-cost margins, and demand elasticity. But further it is stated that this approach "...is not likely to provide an accurate or reliable alternative to the traditional approach of first defining the relevant market and then examining market shares and entry conditions when trying to determine whether the firm possesses monopoly power."[150]

Exclusionary conduct, price predation and tying, bundled discounts and single-product discounts, refusal to deal with rivals and exclusive deals are potentially recognized in the Report as monopolisation or an attempt to monopolise any part of free-trade. "The outcomes of exclusive dealing claims generally rise and fall on two issues: (i) whether the defendant possesses a dominant share of the market and monopoly power; and (ii) whether the monopolist`s exclusive dealing provisions have the scope, severity and reach to preclude competitors from effectively entering the market and competing."[151] Richard Duncan

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[145] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[146] *Ibid.*
[147] *Ibid.*
[148] *United States v. E.I. DuPont de Nemours & Co*, 351 U.S. 377, 391 (1956).
[149] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3),* p. 150.
[150] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[151] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3),* p. 151.

concludes this from *Tampa Elec. Co. v Nashville Coal Co.*[152] and *Geneva Pharm. Tech. Corp v Barr Labs.*,[153] *United States v Microsoft*[154] and *Ryko Mfg. Co v Eden Servs*.[155]

The conclusion of the Report clearly states that if a firm has a market share greater that 50% this is a signal for the courts of the existence of monopoly power and if the firm "...maintain[s] a market share in excess of two-thirds for a significant period and the firm's market share is unlikely to be eroded in the near future, the Department believes that such facts ordinarily should establish a rebuttable presumption that the firm possesses monopoly power."[156]

Single-product discounts

The Report states: "[s]ingle-product loyalty discounts often are pro-competitive, but they can be anti-competitive under certain limited circumstances."[157] Thus it can be presumed that the DOJ recognizes loyalty discounts by default as a pro-competitive tool, only with some exceptions. To compare, the EU approach recognizes rebates as anti-competitive *per se*. The anti-competitive effect arises "…when a significant portion of a customer's purchases are not subject to meaningful competition, the DOJ recognizes the possibility that single-product loyalty discounts might produce an anti-competitive effect even though the discounted price overall of a customer's purchases exceeds the seller's cost."[158]

The Report determines two kinds of rebates which are related to rebate strategies: bundled discounts and single-product loyalty discounts. In the Report, bundled discounting is defined as consisting "in the practice of offering discounts or rebates contingent upon a buyer`s purchase of two or more different products, including bundled rebates where the amount of rebates a customer receives in based on the quantities of multiple products bought over some period"[159] and states that "bundled discounting is common, usually benefits consumers, and generally does not raise antitrust concerns."[160]

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[152] *Tampa Elec. Co. v Nashville Coal Co*, 365 U.S. 320 (1961).
[153] *Geneva Pharm. Tech. Corp v Barr Labs.*, 386 F. 3d 485 (2d Cir. 2004).
[154] *United States v Microsoft*, 253 F.3d 34 (D.C. Cir. 2001).
[155] *Ryko Mfg. Co v Eden Servs.*, 823 F.2d 1215, 1233 (8d Cir. 2005).
[156] U.S. Department of Justice. (September 2008). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[157] *Ibid.*
[158] *Ibid.*
[159] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[160] *Ibid.*

Single-product loyalty discounts "…may be conditioned, for example, on the quantity of product purchased… …or on the percentage of needs purchased […] The discounting seller may offer such discounts to all customers or to a single customer." The report uses the term "single-product loyalty discounts" to refer to these kinds of discounts and focuses on situations where the firm engaging in the practice has monopoly power (or the prospect thereof) over the product in question. "[161]

In the US, rebate regulation went much further than it did in the EU:

> …single product loyalty discounts may be anti-competitive in certain circumstances, such as where the resulting price of all units sold to a customer is below an appropriate measure of cost. Further, commentators and panelists generally agree that even where a single product loyalty discount is above cost when measured against all units, such a discount may in theory produce anti-competitive effects, especially if customers "must carry a certain percentage of the leading firm's products.[162]

Richard Duncan notes that "[l]oyalty rebates contain elements of both predatory pricing and exclusive dealing..."[163]

Thus the Report clearly states that "…commentators agree that single product loyalty discounts are most often pro-competitive, they also agree that these discounts can be anti-competitive where they bring the total price on all units sold below an appropriate measure of cost and there is a likelihood of recoupment."[164] Hovenkamp's opinion mentioned in the Report stresses the rebate illegality obstacle: "…loyalty discount might be anti-competitive as a result of denying rivals economies of scale…" and "[d]iscounting is presumptively pro-competitive and should be condemned only in the presence of significant market power and proven anti-competitive effects."[165]

"Some panelists and commentators have suggested that single-product loyalty discounts can be anti-competitive where customers must buy a certain percentage of their

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[161] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[162] *Ibid.*
[163] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3)*, p. 167.
[164] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[165] *Ibid.*

needs from the monopolist and the discount is structured so as to induce them to buy all or nearly all needs beyond that uncontestable percentage from the monopolist as well." [166]

It can be concluded that US practice is backing the rebate strategy considering that rebates as discounts are pro-competitive *per se*. Only under certain circumstances, such as if the firm has a dominant position (monopoly) and monopoly power, might rebates become anti-competitive.

Damien Geradin analyses the same question and concludes: "[i]n the US, the fear of lessening price competition together with the acknowledged difficulty of distinguishing pro-competitive rebates from anti-competitive ones has led to a strong presumption that conditional rebates are legal unless they can be proved predatory."[167]

EU approach v. US approach

In *Virgin Atlantic*[168], Virgin lost its case because it could not show harm caused to consumers: "Virgin failed to show how British Airways' competition harmed consumers."[169] Later in a similar case but in Europe, in *British Airways*[170] the Commission found abuse of a dominant position by British Airways and based this abuse on *Hoffmann-La Roche* and *Michelin*. The harm caused to consumers was not considered as in *Virgin Atlantic*, but the Commission "…focused its analysis on the British travel agent services market, concluding that British Airways was a necessary business partner to such agents."[171] Richard Duncan with reference to the OECD notes "…under EC competition law, there is a tendency not to permit fidelity discounts in the case of companies with substantial market power."[172]

Drawing parallels with the recent *Intel* case, Damien Geradin notes: "[a]n important question […] is whether antitrust intervention was at all needed in a market characterized by increasing output, decreasing prices and sustained innovation. These characteristics alone

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[166] U.S. Department of Justice. (2008, September). *Competition and Monopoly, Single-firm conduct under Section 2 of the Sherman Act.* Available at: www.usdoj.gov/atr/public/reports/236681.htm.
[167] Geradin D. (2009). A proposed Test for Separating Pro-competitive Conditional Rebates from Anti-competitive Ones. *World Competition, 32,* 41-70, p. 45.
[168] *Virgin Atlantic Airways Limited v British Airways Plc* case, 257 F.3d 256. From here on in main text referred to as "*Virgin Atlantic*" or "the *Virgin Atlantic* case".
[169] *Ibid*., para. 4.
[170] Case C-95/04 P, *British Airways plc v Commission*, [2007] ECR I-2331.
[171] Duncan R., & McCormac B. (2008). Loyalty & fidelity discounts & rebates in the U.S. & EU: will divergence occur over cost-based standards of liability? *Sedona Conference Journal, 9*, p. 136.
[172] *Ibid*.

should raise serious doubt about claims of anti-competitive foreclosure and consumer harm, especially when they are made by competitors."[173]

Richard Duncan points out that "[f]rom the foregoing cases, one sees expressed the political mission of the Commission to force the integration of the common market through its competition policy; but the need for greater economic analysis has also received acknowledgement at the Commission level".[174] Commenting on the Report, Duncan states: "[t]he DOJ Report reflects, more than creates, continuing divergence between US and EU law on single-firm conduct."[175]

Comparing the market shares threshold in the EU and the US, these are 40% against 50% respectively. Richard Duncan, comparing market share thresholds in both legal systems, concludes "…the more serious the abuse, the lower the required market share threshold."[176] Despite market share size and in regard to rebates, Damien Geradin points out: "[i]n any event, whether or not conditional rebates are anti-competitive does not depend on the *form* of such rebates."[177] Hence, he emphasizes the business grounds of discounts.

Damien Geradin concluded in his research that "US courts have generally shown greater defense to conditional rebates adopted by dominant firms, but the case law remains unsettled, notably in the area of bundled rebates."[178] Richard Duncan agrees with this opinion: "...loyalty rebates still carry substantially more risk of being struck down in the European Union than in the United States..."[179]

Further, Duncan states "[p]erhaps for the European competition authorities fully to embrace a cost-based standard for judging loyalty and fidelity discounts and rebates reflects a reluctance to give dominant firms a functional pass on programs that essentially mirror

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[173] Geradin. D. (2009, October 16). *The Decision of The Commission of 13th May 2009 in the Intel Case: Where is the foreclosure and consumer harm?* Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1490114.

[174] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3)*, p. 155.

[175] *Ibid*. p. 148.

[176] *Ibid*. p. 151.

[177] Geradin D. (2009). A proposed Test for Separating Pro-competitive Conditional Rebates from Anti-competitive Ones. *World Competition, 32,* 41-70, p. 47.

[178] *Ibid.* p. 41.

[179] Duncan R., & Coleman C., Daniel H., Haleen P. (2009). Litigating single-firm conduct under the Sherman Act and the EU Treaty: divergence without end, or change we can believe in? *Global Competition Litigation Review. 2(3)*, p. 171.

formal exclusive dealing regimes […] appear now to be moving to introduce cost-based analysis, to avoid striking down rebate programs that have a pro-competitive justification".[180]

In spring 2009, the US Antitrust Division applied a more rigorous standard with focus on the impact of exclusionary conduct to consumers: "…as of today, the Section 2 report will no longer be Department of Justice policy. Consumers, businesses, courts and antitrust practitioners should not rely on it as Department of Justice antitrust enforcement policy."[181]

The Assistant Attorney General in charge of the Department`s Antitrust Division, Cristine A. Varney, stated: "…withdrawing the Section 2 report is a shift in philosophy and the clearest way to let everyone know that the Antitrust Division will be aggressively pursuing cases where monopolists try to use their dominance in the marketplace to stifle competition and harm consumers…" and that "…the Division will return to tried and true case law and Supreme Court precedent in enforcing the antitrust laws."[182]

6. Conclusions and recommendations

This section summarizes analysis of the case studies. The conclusions are drawn based on the practice of EU law and US law in correlation with business theory framework and empirical observation. The results of the research do not solve the problem of the EU law attitude to rebate strategy, but undercover it. Conclusions validate "the dark side of rebates" in the EU and raise new questions for further research.

EU legislative acts do not define rebates. The case law uses the terms "fidelity rebates" and "loyalty rebates", which are currently recognized as conditional rebates in soft law. Additionally, EU legislative acts, except for TFEU Article 102, do not contain thorough definitions of the terms "dominant position" and "abuse of a dominant position". All terms and interpretations in decisions are based on case law. Interpretation of these terms is not yet revised; on the contrary, interpretation of these terms is being widened. The Guidance shows Commission enforcement priorities in applying TFEU Article 102, but the Commission in the Intel case was not applying the Guidance.

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[180] Duncan R., & McCormac B. (2008). Loyalty & fidelity discounts & rebates in the U.S. & EU: will divergence occur over cost-based standards of liability? *Sedona Conference Journal*, *9*, p. 145.
[181] U.S. Department of Justice, (2009, May 11), *Justice Department withdraws report on antitrust monopoly law.* Available at: http://www.justice.gov/opa/pr/2009/May/09-at-459.html.
[182] *Ibid.*

As a result, under EU law an undertaking is regarded as being in a dominant position when it has a considerable volume of market share. The EU in the Guidance determines that this should be not less than 40% while in the US the Report determines that it should not be less than 50%. Determining market share size is necessary to take into account certain geographical markets and relative product markets. To be in a dominant position, a company should have economic strength and behave independently from rivals, purchasers, or suppliers, or should have monopoly power (US).

After a claim is raised under TFEU Article 102, the aim of the Commission is to prove the undertaking to be in a dominant position, then to prove abuse of a dominant position. In general, the main aim is to protect consumers from harm by an undertaking being in a dominant position and abusing that position. In reality it looks like a competition between the Commission and the particular undertaking; the Commission cannot lose this "competition game" and will prove that the undertaking is operating illegally.

Analysis of EU case law studies suggests the following equation: if the Commission proves that an undertaking is in a dominant position, then the Commission also proves that this undertaking abuses its dominant position. Thus according to the EU approach, legal practice differs from legal theory. In EU law practice, being in a dominant position means *per se* abuse of a dominant position.

Results of analysis show that pro-competitive rebates turn into anti-competitive in the EU by decision of the Commission. As there is no certain definition in EU law of pro-competitive and anti-competitive rebates, case law practice highlights that rebates (either pro-competitive or anti-competitive, as these are not yet legally defined) granted by an undertaking in a dominant position are always anti-competitive *per se*. Results of analysis of US case law show the opposite US approach towards rebates compared with the EU approach. US law by default considers that rebates benefit consumers and generally do not raise antitrust foreclosure. Thus, rebates are considered as pro-competitive *per se*.

The first moment when a pro-competitive rebate strategy might turn into an anti-competitive rebate strategy could be Commission evaluation of the size of market share of a particular undertaking. When the size of market share is big (according to case law studies, size of market share should be analysed *ad hoc*) there is a risk that the business of the undertaking might be investigated by the Commission. In other words, there is no certain moment when legal rebates become illegal, which means undertakings never know when their rebate strategy will fall under TFEU Article 102.

Legal practice in the US in regard to rebate strategies does not differ from legal theory. According to US law practice, it is presumed that rebates are considered as a legal tool only with some exceptions. In the US the field of rebate strategy application is studied in much more detail than in the EU. This might also be concluded not only from case law studies, but also from a historical-empirical point of view: The Sherman Antitrust Act was adopted much earlier than the predecessor of TFEU Article 102 in the EU.

In both legal systems, competition law aims to protect consumers from harm caused by a monopoly undertaking (or undertakings in a dominant position). The *Intel* case is an example of the existence of a parallel aim in EU law. It might be interpreted that EU competition law also protects competitors. Perhaps the real aim is to "to win the competition game".

The Commission should revise their interpretation of rebate strategy application. US antitrust practice as to rebate strategy is an example for the Commission to follow. Moreover, the Commission should evaluate not only the legal and economic side in argumentation in their decisions, but also evaluate the business side. A major step forward was issuing the Guidance, but the Guidance has no worth if the Commission does not apply it.

Rebate strategy from a business perspective is a competitive tool. Damien Geradin stresses: "[i]t is hard to deny that rebates are an important source of efficiencies in terms of price reduction, economies of scale and faster fixed cost recovery, economies of scope and reduction of transaction costs, avoiding double marginalization, providing incentives for customers to supply complementary services, risk-sharing between suppliers and customers, etc."[183] Results of analysis show that pro-competitive rebates might become anti-competitive, thus showing "the dark side of rebates". Thus, results of analysis also show that in Europe "the dark side of rebates" is much "darker" than in the US.

This does not mean in itself that the EU approach is incorrect; it means that decision makers in the Commission should look at this problem from a different angle and observe the practice of other colleagues (in this case, the US). Thus, Commission decision makers should revise the argumentation concept in their decision by not only measuring their argumentation based on case law within the EU, but also taking into account other doctrines outside the EU.

A rephrased concept of competition regulation in the EU in regard to rebate strategy would be: every undertaking may compete with other rivals and use rebate strategies so far as

[183] Geradin. D. (2009, October 16). *The Decision of The Commission of 13th May 2009 in the Intel Case: Where is the foreclosure and consumer harm?* Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1490114.

that undertaking "wins the competition game" and gains more market share. From the moment when an undertaking, implementing fair competition action such as using pro-competitive rebates, increases their market share (of course, on the relevant product and geographical markets), some of these fair competitive actions will turn into anti-competitive actions. This works simply: the undertaking which "lost the game" and lost a portion of market share will take "the winner" to the Commission. As recent practice shows, the Commission "protects rivals" from an "unfair" competitor in a dominant position.

Undertakings that implement rebate strategies should constantly evaluate their market share size by analysing their related product and geographical markets. Thus, those who might consider themselves as being in a dominant position and using rebate strategies should be prudent in further business steps. Additionally, US undertakings which are using rebate strategies should be more prudent in operations in the EU because of the authorities' different interpretation of similar antitrust regulation. Thus, those companies that implement rebate strategies in their worldwide distribution channel should revise their marketing strategies, distinguishing those executed in the US from those executed in the EU.

Results of analysis in this diploma project raise questions for further research. It is not sufficiently clear who really gains from penalties imposed by the Commission. As the aim of antitrust regulation is to protect consumers from harm caused by a dominant undertaking, penalties will surely harm particular undertakings. On the other hand, will this "undertaking harm" protect consumers? The real gain from penalties imposed on a dominant undertaking for consumers is not really visible. It is possible to postulate two main beneficiaries.

First, the Commission. The Commission in this way contributes to its own financing (as the fine goes to the Commission bank account) by imposition of penalties. From the business perspective, the biggest gain (the biggest fine it is possible to impose) is from the biggest worldwide market players, as fines are limited to 10% of an undertaking's annual revenue. Hence, the expression "strategy as ecology", coined by Marco Iansiti and Roy Levien.[184] This is an ecosystem where the Commission somehow depends on the activities of dominant undertakings. It is a hunger to punish those who are big and rich.

Second, rivals. Clearly, if the Commission punishes an undertaking because it abuses a dominant position by granting conditional rebates, rivals of that undertaking will benefit immediately from penalties imposed on it. At the same time, those rivals might use a similar rebate strategy and also grant conditional rebates to the same customers. In the *Intel* case the

[184] Iansiti M., & Levien R. (2004). Strategy as Ecology. *Harvard Business Review*, pp. 417-428.

Commission evaluated only Intel's business strategy; marketing tools implemented by AMD were not evaluated.

Additionally, it is not clear why the Commission regards consumer interests to be very narrow. The same undertaking Intel is involved in many charity projects including social and corporate responsibility,[185] education,[186] and the environment.[187] Intel supplies jobs for thousands of people and pays millions of dollars in taxes worldwide. The behaviour of granting conditional rebates is also criticized as positive action, because the rebate itself is a discount. Thus, consumers will gain from rebates because the price will be lower. And after considering all these facts, do consumers or society gain from Commission behaviour? Was Commission intervention necessary? It rather seems that rival AMD had more to gain from Commission action. Another moral side of the fine is observed in company operation coverage. The fine is imposed on Intel as a corporation, not the EU Intel office. Thus, the fine will affect all worldwide Intel operations, and indirectly all people involved outside the EU. Hence the Commission with EU jurisdiction harms companies "outside" the jurisdiction.

When will the hunger of the Commission be satisfied and who will be next? *The Financial Times* identified an upcoming competition between two giants – Google and Microsoft. The next "game player" will be the giant company Google Inc ("Google"). Three companies lodge a complaint with the Commission against Google, complaining that Google abuses its dominant position by headlining in their search engine results other products owned by Google.[188] Hence, as the Commission will not revise their approach towards judging competition cases and will not change their argumentation used in Commission decisions in previous competition cases, this might cost Google EUR 2 365 000 000.[189] That is the maximum the Commission can impose on Google.

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[185] Intel Corp. (n.d.). *Corporate Responsibility*. Available at: http://www.intel.com/intel/corpresponsibility/index.htm?iid=gg_about+intel_gcr.

[186] Intel Corp. (n.d.). *Education*. Available at: http://www.intel.com/intel/education/index.htm?iid=gg_about+intel_education.

[187] Intel Corp. (n.d.). *Environment*. Available at: http://www.intel.com/intel/environment/index.htm?iid=gg_about+intel_environment.

[188] Waters R., Tait N. (2010, February 24). Google faces Brussels antitrust scrutiny. *Financial Times*. Available at: http://www.ft.com/cms/s/2/46018520-20da-11df-b920-00144feab49a.html.

[189] According to case law, a fine could not reach more than 10% of company revenue. Google revenue in 2009 was 23,650,563. Finance report available on: http://investor.google.com/releases/2009Q4_google_earnings.html.

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