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PRICE DISCRIMINATION UNDER EC COMPETITION LAW: THE NEED FOR A CASE-BY-CASE APPROACH

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I. Introduction

Price discrimination is one of the most complex areas of EC competition law.[1] There are several reasons for this. First, the concept of price discrimination covers many different practices (discounts and rebates, tying, selective price cuts, discriminatory input prices set by vertically-integrated operators, etc.) whose objectives and effects on competition significantly differ. From the point of view of competition law analysis, it is thus not easy to classify these practices under a coherent analytical framework. Second, there is a consensus among economists that the welfare effects of the (various categories of) price discrimination are ambiguous. It is hard to say *a priori* whether a given form of price discrimination increases or decreases welfare. The response to this question may indeed depend on which type of welfare standard (total or consumer) is actually pursued. Moreover, even if one agrees on a given standard, the welfare effects of discriminatory prices generally depend on factual issues, such as whether it increases or decreases total output. Third, the exact scope of Article 82(c), the only Treaty provision dealing with discrimination, is not entirely clear. While the European Commission (hereafter, the "Commission") and the Community courts have applied Article 82(c) to many different practices, there are good reasons to believe that this provision should be applied to a limited set of circumstances, most forms of discrimination being adequately covered by Article 82(b) or other provisions of the Treaty.

Against this background, the main objective of this paper is to throw some light on the compatibility of price discrimination with EC competition law. In order to do so, this paper does not seek to propose a grand unifying theory that would provide a single test offering a way to distinguish between practices compatible and incompatible with the EC Treaty. Instead, we offer an analytical framework which distinguishes between different

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[1] There is, however, a relatively abundant legal and economic literature on the subject. On the economics of price discrimination, see Derek Ridyard, "Exclusionary Pricing and Price Discrimination Abuses under Article 82 – An Economic Analysis", (2002) 6 *European Competition Law Review*, 286; Dennis W. Carlton and Jeffrey M. Perloff, *Modern Industrial Organization*, Third Edition, Addison-Wesley, 1999, Chapter 9; Jean Tirole, *The Theory of Industrial Organization*, The MIT Press, 2003, Chapter 3; Hal R. Varian, "Price Discrimination and Social Welfare", (1985) 75 *American Economic Review*, 870; Richard Schmalensee, "Output and Welfare Implications of Third Degree Price Discrimination", (1981) 71 *American Economic Review*, 242; For a legal analysis of price discrimination under Article 82 of the EC Treaty, see Michel Waelbroeck, "Price Discrimination and Rebate Policies under EU Competition Law", (1995) *Fordham Corporate Law Institute*, 148.

categories of price discrimination depending on their effects on competition. Different tests may thus be needed to assess the compatibility of the practices belonging to these categories with EC competition law. Another objective of the paper is to show that Article 82(c) should only be applied to the limited circumstances where a non-vertically integrated dominant firm price discriminates between customers with the effect of placing one or several of them at a competitive disadvantage vis-à-vis other customers (secondary line price discrimination). In contrast, Article 82(c) should not be applied to pricing measures designed to harm the dominant firm's competitors (first line price discrimination) or to fragment the single market across national lines. As will be seen, relying on Article 82(c) to condemn such practices goes against the letter and the spirit of this provision and may also apply a wrong test to such practices. It is also not necessary since other Treaty provisions can be used to achieve this objective.

This paper is divided into six parts. Part II attempts to define the concept of price discrimination, identify the conditions for price discrimination to occur, and describe the main forms of price discrimination. Part III discusses the welfare effects of price discrimination. It seeks to show that such effects cannot be determined *a priori*, but on the contrary need to be assessed on a case-by-case basis. Part IV seeks to identify the exact scope of Article 82(c). This provision has been used by the European Commission and the Community courts to condemn practices that should have been assessed under other provisions of the EC Treaty. It also tries to determine why Article 82(c) has been intensively applied by the Commission and the Community courts instead of more adequate provisions. Part V provides an analytical framework for examining the various categories of price discrimination imposed by dominant firms. It divides price discrimination practices into three categories depending on whether they create primary line injury, secondary line injury or involve geographic price discrimination and/or measures facilitating this form of discrimination. Our analysis of these three categories follows the same pattern. We first analyse the main types of practices belonging to these categories and discuss the relevant case-law. We then discuss whether Article 82(c) was the right legal basis to be applied in these cases or whether another legal basis may have been more adequate. Eventually, we discuss whether the case-law is in line with economic theory. Finally, Part VI contains a short conclusion.

II. Definition, conditions, and different forms of price unfairness

In this Part, we successively attempt to define the concept of price discrimination, identify the conditions for price discrimination to occur, and describe the main forms of price discrimination.

A. Definition of and conditions for price discrimination

Article 82(c) of the Treaty does not provide a definition of price discrimination. It simply considers as an abuse the fact for one or several firms holding a dominant position of "applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage". The European Court of Justice

(hereafter, the "ECJ") has extended this notion of abuse to the converse situation of the application of similar conditions to unequal transactions.[2] Article 82(c) as interpreted by the ECJ thus means that some forms of price discrimination may be considered as abuses of a dominant position. By contrast, it does not provide a clear economic test allowing to distinguish price discrimination from other business practices.

Scholars have, however, provided economic tests helping to identify price discrimination. For instance, in his famed antitrust book, Richard Posner explains that:

> "Price discrimination is a term that economists use to describe the practice of selling the same product to different customers at different prices even though the cost of sale is the same to each of them. More precisely, it is selling at a price or prices such that the ratio of price to marginal costs is different in different sales [...]".[3]

This definition is helpful in that it provides an objective criterion, i.e. the presence of different ratios of price to marginal costs (i.e. rates of return), to identify the occurrence of price discrimination. It also suggests that different prices for the same product do not necessarily amount to price discrimination as such difference may be justified by cost variations.

It is generally admitted that several conditions must be present for price discrimination to occur:

- A firm must have some market power (i.e., the ability to set supra-competitive prices) to be able to price discriminate. Otherwise, it cannot succeed in charging any consumer above the competitive price. As scenarios of perfect competition are extremely rare, most firms enjoy some degree of market power and thus price discrimination can be observed even in highly competitive markets. Dominance is not essential for price discrimination to occur, although it is only in situation of dominance that price discrimination may be considered abusive in EC competition law.

- The firm must have the ability to sort consumers depending on their willingness to pay for each unit. The level of information enjoyed by a firm over its customers may in turn determine the forms of price discrimination it decides to put in place. Firms enjoying only imperfect information about its customers' willingness to pay will only be able to imperfectly price discriminate.

- The firm must be able to prevent or limit the resale of the goods or services in question by consumers paying the lower price to those who pay the higher price. In some cases, resale is impossible due to transaction costs (e.g., transport costs from high to low price areas), while in others firms adopt contractual or other

[2] See ECJ, 17 July 1963, *Italian Republic v Commission*, 13-63, ECR-165 in the context of the ECSC Treaty.

[3] Richard Posner, *Antitrust Law*, Second Edition, University of Chicago Press, Chicago and London, 2001 at 79-80.

measures to prevent arbitrage between consumers (e.g., prohibition of resale as part of terms of sale).[4]

Absent one or several of these conditions, price discrimination is impossible or at least unlikely to succeed.

B. Different forms of price discrimination

As pointed out by Carlton and Perloff, the objective of all methods of price discrimination is to "capture as much consumer surplus as possible".[5] But this can be achieved through different forms of price discrimination:

- First degree price discrimination occurs when a firm is able to perfectly discriminate between consumers, that is when it enjoys the ability to charge the maximum each consumer is willing to pay for each unit of a given product or service. Most economists, however, agree that this scenario can almost never be observed in practice as first degree price discrimination assumes that the firm has perfect knowledge of its customers' willingness to pay, an assumption which is unlikely to be met in most markets.[6]

- Second degree price discrimination occurs when a firm sets a price per unit which varies with the number of units the customer buys. This can be achieved through volume discounts whereby the price of a unit varies depending on the quantity purchased by the buyer or the adoption of a two-part tariff whereby the consumer pays a flat fee independent of the quantity purchased plus a variable fee which depends on the quantity purchased.

- Third degree price discrimination takes place when a firm charges different prices to different groups of customers depending on their elasticity of demand. Consumers with high elasticity of demand will be charged higher prices than those with low elasticity of demand (Ramsey pricing).

The distinction between first, second and third degree discrimination is only of limited relevance in the competition law analysis context as it tells little about the effects of competition generated by the different forms of price discrimination it distinguishes.

III. Welfare effects of price discrimination

The purpose of this Part is not to provide an extensive discussion of the welfare effects of price discrimination, but rather to show that such effects cannot be determined *a priori*. Their determination requires a case-by-case analysis.

[4] See D. Carlton and J. Perloff, supra note 1 at 277-80.
[5] Id. at 280.
[6] See Massimo Motta, *Competition Policy – Theory and Practice*, Cambridge University Press, 2004, at 493-94.

The welfare effects of first degree price discrimination do not deserve an extensive discussion since, as noted above, this form of discrimination is unlikely to occur in practice. Let us just say that these effects essentially depend on the welfare standard selected.[7] Because the firm in question is able to charge the maximum each consumer is willing to pay for a given product or service, it will be in a position to extract all consumer surplus. Thus, first degree price discrimination enhances total welfare (i.e., the sum of producer and consumer welfare). On the other hand, it decreases consumer welfare as consumer surplus is totally absorbed by the producer.

The welfare effects of second and third degree price discrimination require a greater degree of attention. Second and third degree price discrimination particularly increase welfare when they allow a firm to supply a group of consumers, which would not be supplied in the absence of price discrimination. Third degree price discrimination taking the form of different tariffs for peak and off-peak train travel may, for instance, allow price sensitive consumers that would not be able to use the train service under a uniform price to gain access to that mode of transportation.[8] A similar result can also be achieved through second degree price discrimination taking the form of rebates as such rebates may allow new categories of consumers to buy a product which they could not have afforded under a uniform price.

It is widely admitted that the welfare effects of such forms of discrimination essentially depend on the question of whether price discrimination increases total output.[9] Rebates producing exclusionary effects do not necessarily increase demand, but rather reallocate market shares between producers. As in the case of predation, the exclusionary effects of such rebates may force the competitors of the dominant firm to exit the market and thus lead to a reduction of output. A similar outcome may result from selective price cuts. On the other hand, rebates that increase total output by serving consumers that would not be served under a uniform price enhance welfare. The welfare effects of rebates and other forms of price cuts thus depend on the facts at play in each individual case.

A key insight of economics is that price discrimination is most likely to expand output where the seller has declining average total costs.[10] Expanding output through price discrimination is an essential strategy for firms facing problems of fixed cost recovery.[11] Price discrimination allows firms facing large fixed costs (in practice all firms that make substantial investments) to expand their output and thus spread fixed costs over a large number of units. When marginal costs are low (such as, for instance, in network or information-based industries), any positive price allows the firm to contribute to its fixed

[7] See Simon Bishop and Mike Walker, *The Economics of EC Competition Law*, Sweet & Maxwell, Second Edition, 2002, at 196.
[8] Id. at 198.
[9] See Jonathan Faull and Ali Nikpay, *The EC Law of Competition*, Oxford University Press, 1999 at §3.235.
[10] For a good discussion of this, see D. Ridyard, supra note 1 at 286.
[11] Id.

costs. Prohibiting price discrimination would thus prevent efficient recovery of fixed costs and would, in the long run, have a negative impact on investments.[12]

Another interesting issue is whether economic theory has something to say about geographic price discrimination.[13] Let's assume, for instance, that a firm sells widgets for 5 cents in Member State A and for 7 cents in Member State B, the intensity of demand being higher in B than in A. Let's also assume that the firm in question is able to prevent arbitrage or that arbitrage is not possible to due to transaction costs. Preventing price discrimination would produce ambiguous effects as the imposition of a uniform price (e.g., 6 cents) would make consumers of Member State B better off and those of Member State A worse off. Aggregating gains and losses may suggest overall welfare gains provided of course that the firm continues to serve both markets. But this condition might not be met in practice. If consumer demand in B is indeed larger than consumer demand in A, the firm may simply decide to stop serving A in order to focus on B. Such a scenario would lead to welfare losses as consumers of Member State A would no longer be served. Thus, an overall prohibition of price discrimination across Member States would not be justified as it might lead to welfare losses.

A different issue is whether measures seeking to prevent resale in high price Member States of products or services bought in low price Member States should be banned. Such measures have been subject to a *per se* prohibition by the ECJ on the ground that they would affect market integration.[14] On the other hand, there may be good reasons to allow restrictions on the cross-border resale of goods. Such restrictions may, for instance, be part of a package of measures designed to induce distributors to distribute a new brand and thus take a commercial risk.[15] Moreover, prohibiting such restrictions may encourage producers to integrate vertically, thereby reducing to an even greater extent intra-brand competition.

In sum, a *per se* prohibition on price discrimination cannot be justified on the basis of economic theory as price discrimination may, depending on the facts of each case, enhance welfare.

IV. **The scope of Article 82(c) of the EC Treaty**

[12] Id. at 287 ("Marginal cost pricing […] retains some desirable efficiency properties in [industries facing problems of cost recovery], but simple short-run marginal cost pricing fails to remunerate the firm's fixed costs. In a dynamic context, it will also fail to provide incentives for firms to make such investments in the future. As a consequence, firms in fixed cost recovery industries charge prices in excess, often will in excess, of short-run marginal costs. The likelihood that such pricing will entail some less of static efficiency (i.e.: certain consumers will be dissuaded from consuming the product even though they value it higher than the marginal cost of supply) must be traded-off against the risk that the product would not exist at all if investors were not offered the prospect of fixed cost recovery – and even some profit on top – at the time were the necessary investments were made.)

[13] See M. Motta, supra note 6 at 495-96.

[14] See ECJ, *United Brands Company v. Commission*, 27/76, 14 February 1978, ECR [1978]-207.

[15] See generally on this Valentine Korah ad Denis O'Sullivan, *Distribution Agreements under the EC Competition Rules*, Hart Publishing, 2002, at 27-36.

Article 82(c) considers the fact for one or several firms holding a dominant position of "applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage" an abuse of a dominant position. As noted above, the ECJ also considers as an abuse the application of similar conditions to unequal transactions. The ECJ case-law indicates that "dissimilar conditions" also include "dissimilar prices". Price discrimination thus clearly falls within the scope of Article 82(c).

The language of this provision triggers the following remarks. First, among the conditions which need to be met for applying Article 82(c) is a requirement that the measure under investigation applies dissimilar prices to "equivalent transactions". The evaluation of the equivalence of two transactions is not an easy matter as there are a myriad of factors that can be invoked to justify the lack of equivalence between two transactions. The most obvious reason for stating that two transactions are not equivalent is that the sales involve different costs for the seller.[16] The problem is of course to determine how significant cost differences should be for two transactions to be considered non-equivalent. Indeed, if all cost differences, however small, were to be taken into consideration very few transactions should be considered as equivalent. It could also be argued that differences regarding the moment at which sales are made render two transactions non-equivalent. For many products or services (airline tickets, package holidays, etc.), the moment at which a sale is made has a major impact on the price imposed by the sellers. When the cost of providing the product or service in question does not differ depending on the time of sale, it is subject to question whether a time of sale difference could justify a finding that two transactions are not equivalent. Finally, there is some uncertainty as to whether differences relating to the situation of the buyers can be taken into consideration when assessing the equivalence or lack of equivalence of two transactions.[17] For instance, applying prices inversely related to the elasticity of buyers is a strategy frequently used by firms to expand output. But when the cost of supplying consumers sorted on the basis of their elasticity does not differ, it is not clear whether differences in elasticity of demand can render transactions non equivalent under the terms of Article 82(c). Unfortunately, the decisional practice of the Commission and the case-law of the Community courts fail to provide any clear guidance on the above issues. In fact, the Commission and the courts generally assume that two transactions are equivalent without much analysis.[18]

The application of Article 82(c) also requires that dissimilarly treated equivalent transactions should place some of the dominant firm's trading parties at a competitive disadvantage against others. This condition clearly indicates that Article 82(c) essentially

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[16] See J. Faull and A. Nikpay, supra note 9 at §3.237.

[17] See, however, in *United Brands*, supra note 14 where the ECJ indicated at §228 that: "[...] Differences in transport costs, taxation, customs duties, the wages of the labour force, the conditions of marketing, the differences in the parity of currencies, the density of competition may eventually culminate in different retail selling price [...]".

[18] See Van Bael&Bellis, *Competition Law of the European Community*, Kluwer Law International, 2005 at 915.

seeks to prevent "secondary line" injury.[19] Scholarly discussions regarding price discrimination often draw a distinction between "primary line" injury, which is occasioned by the dominant firm to its competitors by applying different prices to its own customers, and "secondary line" injury, which is imposed on one of several customers of the dominant firm as against one or several other customers.[20] The reference to the placing of the dominant firm's "trading parties at a competitive disadvantage" clearly indicates that the parties Article 82(c) seeks to protect are the customers of the dominant player and not its competitors. Literally all legal scholars seem to agree on this point.[21] The need for a competitive disadvantage to occur also suggests that for Article 82(c) to apply, the dominant firm's customers should be in competition with each other.[22] This requirement makes the finding of a discriminatory abuse dependent on the finding a downstream market on which these firms compete.

The Commission and the Community courts have largely ignored the above condition with the result that they have applied Article 82(c) to dominant firms' pricing practices, which have little to do with putting their trading parties at a competitive disadvantage.[23] For instance, Article 82(c) has been applied to pricing practices, such as fidelity rebates or selective price cuts, which were allegedly designed to harm the dominant firms' competitors.[24] These practices are classic examples of primary line discrimination which should not be covered by Article 82(c). As pointed out by several authors, they should instead be treated under Article 82(b), which is the proper legal basis for dominant firms' practices which produce exclusionary effects. Similarly, Article 82(c) has been used to condemn practices which essentially sought to partition markets along national lines.[25] Here again, such practices have little to do with the secondary line injury scenarios which Article 82(c) is designed to prevent.

One could, however, argue that the selection of the proper legal basis (Article 82(b) v. Article 82(c)) is essentially an academic issue with limited practical implications. Such a

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[19] In fact, the rationale of Article 82(c) might have been quite close to the primary rationale behind the US Robinson-Patman Act, which was to protect competition on the downstream market and, more specifically, small purchasers against large purchasers. See *Federal Trade Commission v. Morton Salt*, 334 U.S. 37 ("The legislative history of the Robinson-Patman Act makes it abundantly clear that Congress it to be an evil that a large buyer could secure a competitive advantage over a small buyer solely because of the larger buyer's quantity purchasing ability"). See also Dominick T. Armentano, *Antitrust and Monopoly – Anatomy of a Policy Failure*, Second Edition, The Independent Institute, 1999, at 167 ("[I]s is readily admitted that Section 2 of the Clayton Act and its important Robinson-Patman amendments, were passed in order to protect small, independent business firms from the buying and selling practices of larger corporations, particularly large chain stores").

[20] See e.g. Alison Jones and Brenda Sufrin, *EC Competition Law*, 2nd Ed., Oxford University Press, 2004 at 411; J. Faull and A. Nikpay, supra note 9 at §3.235.

[21] See Santiago Martinez Lage and Rafael Allendesalazar, "Community Policy on Discriminatory Pricing: A Practitioner's Perspective", *Paper presented at the 2003 Annual EU Competition Law and Policy Workshops - What is an Abuse of a Dominant Position?*, Florence at 14; Van Bael&Bellis, supra note 18 at 915; Richard Whish, *Competition Law*, 5th ed., LexisNexis Butterworths, 2003, at 716 and 710.

[22] See John Temple Lang and Robert O'Donoghue, "Defining Legitimate Competition: How to Clarify Pricing Abuses under Article 82 EC", (2002) 26 *Fordham International Law Journal*, 83 at 115.

[23] See S. Martinez Lage and R. Allendesalazar, supra note 21 at 15.

[24] See infra at V(A).

[25] See infra at V(C).

view would be too simple, however, as the choice of the proper legal basis under Article 82 EC may have serious implications. As will be seen below, the problem with Article 82(c) is that, as interpreted in the current case-law, the evidentiary level it requires to reach a finding of abuse of a dominant position is quite low. After all, Article 82(c) only requires the application of dissimilar prices to equivalent transactions with the effect of placing some trading parties at a competitive disadvantage.[26] The requirement that trading parties be placed at a "competitive disadvantage" is not very demanding. It falls short, for instance, from asking the demonstration that such parties would be forced to exit the market should the discriminatory practice continue. Moreover, in most instances, the Commission and the Community Courts have simply ignored this condition for finding a violation of Article 82(c).[27] In contrast, Article 82(b) has been interpreted as requiring a showing of exclusionary effects. The language of this provision also conditions the finding of an abuse to the showing of a prejudice to the consumers. As price discrimination measures taking the form of rebates generally benefit consumers, the evidentiary burden imposed by Article 82(b) seems thus higher.

This low evidentiary threshold is not of major concern when dealing with cases of secondary line discrimination which do not produce exclusionary effects. After all, this form of discrimination is quite rare and hardly justifiable when it occurs. In contrast, when the matter in question involves primary line discrimination, a simple finding of price discrimination is clearly insufficient to reach a finding of abuse of a dominant position. Such cases, which, for instance, concern rebates and selective price cuts, require at the minimum the showing that the measure in question produces exclusionary effects, which may drive rivals out of the market. In fact, not unlike essential facilities cases, secondary line price discrimination cases involve a strategy whereby a dominant firm restricts the output of its rivals by excluding them from the market. The right legal basis to deal with such cases is Article 82(b).

V. Proposed analytical framework for examining price discrimination measures

The objective of this Part is to provide an analytical framework for examining the various forms of price discrimination imposed by dominant firms. As we have seen above, price discrimination can take the form of many different practices whose objectives and effects can substantially differ. Because of such differences, we propose to divide these practices in three categories depending on whether they create primary line injury, secondary line injury, or whether they involve geographic price discrimination. The various kinds of measures falling within these categories are summarized in Table I (see end of this paper).

A. Price discrimination in primary line injury settings

This section first seeks to demonstrate that while the wording of Article 82(c) clearly indicates that this provision was designed to prevent price discrimination practices

[26] See J. Temple Lang and R. O'Donoghue, supra note 22, who consider it is a strict test which is however not applied in practice.
[27] See J. Faull and A. Nikpay at p.176.

placing a dominant firm's customers at a competitive disadvantage vis-à-vis other customers (secondary line price discrimination), a significant number of Commission decisions and Community courts' judgments rely on Article 82(c) to condemn primary line price discrimination measures. We also explore why the Commission and the Community courts relied on Article 82(c) while other provisions might have been better suited to the cases at hand (1). This section also seeks to show that the Commission and the Community courts have generally been too stringent with the price discrimination measures they have been called to examine under Article 82. As primary line price discrimination may increase welfare, a more balanced approach would be preferable (2).

1. Price discrimination in primary line injury settings: A legal analysis

This sub-section first outlines the main categories of primary line price discrimination, which have been found as constituting abuses of a dominant position in the Commission's decisional practice and in the Community courts' case-law (1.1). It then shows that these practices have little to do with the types of behaviour that Article 82(c) initially sought to prevent and also tries to explain why the Commission and the Community courts examined, mistakenly in our opinion, these practices under Article 82(c) (1.2).

1.1. Main forms of primary line price discrimination measures examined under Article 82(c)

Hereafter, we successively review cases involving rebates, selective price cuts and tied and bundled prices.

1.1.1 Price Discrimination in the form of rebates

A first form of price discrimination consists in rebates, i.e. discounts paid retrospectively by a seller to a purchaser in respect of past purchases.[28] Rebates generally entail price discrimination because the customer who receives a rebate pays a lower price than other customers purchasing a similar good or service.[29]

There exist several categories of rebates. A first category relates to "quantity rebates", i.e. discounts granted on the basis of the volume purchased. The Commission and the Community courts have generally considered that quantity rebates reflecting cost efficiencies resulting from the larger amount of products sold are not discriminatory.[30] In

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[28] This definition is taken from Lennart Ritter and David Braun, *European Competition Law: A Practictioner's Guide*, Kluwer Law International, 2004, at 465.

[29] See ECJ, *Suiker Unie and others v. Commission*, 16 December 1975, 40/73, ECR [1975]-1663 at §122: " As the commission has emphasized the effect of the system complained of was that different net prices were charged to two economic operators who bought the same amount of sugar from SZV if one of them purchased from another producer as well. By acting in this way SZV applied dissimilar conditions to equivalent transactions with other trading parties' within the meaning of article 86 (c) of the Treaty".

[30] To the contrary, uniform pricing of different volumes can be seen as discriminatory. This is why the Commission considers that quantity rebates are normally unobjectionable. See Commission Decision 97/624 of 14 May 1997, *Irish Sugar plc.*, OJ L 258 of 22 September 1997, pp.1-34 at §153.

contrast, the judgment of the CFI in *Michelin II* suggests that quantity rebates not based on such efficiencies are not economically justified and thus should be found discriminatory within the meaning of Article 82(c).[31] So far, there has, however, been no case where pure quantity rebates have been found discriminatory under Article 82(c).

A second form of rebates relates to "fidelity rebates", i.e. discounts offered as a counterpart of a commitment from the purchaser to place all or most of its orders to the seller granting the rebate, be they large or small. Fidelity rebates are generally seen as a horizontal exclusionary devices aiming at foreclosing competitors or impeding their expansion. Nevertheless, Commission decisions and ECJ judgments involving fidelity rebates have condemned them on the basis of Article 82(c), omitting in their analysis the "competitive disadvantage" condition built in this provision.

This can, for instance, be observed in *Hoffmann-La Roche*, a case where the dominant company had granted rebates to a number of purchasers, as a counterpart to the commitment from the purchasers to acquire all or most of their vitamins or certain vitamins from Hoffmann-La Roche.[32] The Commission held that these contracts, on the one hand, had a horizontal effect by distorting competition between vitamins producers and, on the other hand, had a discriminatory effect in that they applied dissimilar conditions to equivalent transactions. The ECJ ruled on the question of discrimination by holding that:

> "the effect of a fidelity rebate is to apply dissimilar conditions to equivalent transactions with other trading parties in that two purchasers pay a different price for the same quantity of the same product depending on whether they obtain their supplies exclusively from the undertaking in a dominant position or have several sources of supplies".

The Court sanctioned the discrimination on face value and did not engage in an analysis of the competitive situation downstream as required under Article 82(c).[33] Hoffmann La Roche, however, argued that the rebates were not of such a kind as to place its customers at a competitive disadvantage. The Court eluded the question declaring:

> "[...] since the course of conduct under consideration is that of an undertaking occupying a dominant position on a market where for this reason the structure of competition has already been weakened, within the field of application of article [82] any further weakening of the structure of competition may constitute an abuse of a dominant position.".[34]

The ECJ's reference to the weakening of the structure of competition on the producer's market confirms that the discrimination was sanctioned for its primary line injury effect rather than for the secondary line injury required by Article 82(c). The Court did not deal

[31] See CFI, *Manufacture française des pneumatiques Michelin v Commission*, (*Michelin II*), 30 September 2003, T-203/01 at §§98 and 100. See also, Denis Waelbroeck, "Michelin II: A per se rule against rebates by dominant companies?" (2005) 1(1) *Journal of Competition Law and Economics*, 149-171 at p.151.

[32] See ECJ, *Hoffmann-La Roche v. Commission*, 13 February 1979, 85/76, ECR[1979]-461.

[33] Id. at §35. The trading parties were 22 large firms of different industries.

[34] Id. at §122 and following.

with the question of the competitive disadvantage. Instead, it relied on abstract arguments to establish a violation of Article 82(c).[35]

In some cases, however, the Commission and the Community courts examined both primary and secondary line effects of fidelity rebate schemes. In *British Plasterboard Industries*, for instance, BPB, the dominant plasterboard producer in Great Britain and Ireland (through its subsidiary BG) was faced with increasing competition from imports from France and Spain.[36] In Northern Ireland, BPB withdrew a rebate from its customers who intended to import Spanish plasterboard. Moreover, it offered an additional rebate to all customers who agreed to purchase exclusively from BG and not deal with imported products.[37] The CFI held that such a practice "by virtue of its discriminatory nature was clearly intended to penalize those merchants who intended to import plasterboard and to dissuade them from doing so, thus further supporting BG's position in the plasterboard market".[38] Although it did not elaborate on the issue and made no reference to Article 82(c), the CFI's statement seemed to point in the direction of two effects, i.e. a secondary line injury for those merchants not committing to loyalty and a primary line one with the maintenance of BG's dominant position. As far as the secondary line injury was concerned, the Commission's decision indicated that imports had prompted increased price competition at the merchants' level.[39]

British Airways is another case were both primary and secondary effects were identified. In this case, the Commission and the CFI considered that the loyalty (or growth) rebate schemes relied upon by BA had a discriminatory nature contrary to Article 82(c).[40] Two customers (i.e. travel agents) purchasing the same level of British Airways tickets could indeed receive a different rebate if their sales of British Airways tickets were different in the previous year.[41] The practice had, as the Commission rightly held in its decision, the effect of distorting competition between BA and other airlines on the market for transport services.[42] Yet, unlike *Hoffman-La Roche*, British Airways did not only create a primary line injury discrimination. In their reasoning, both the Commission and the ECJ also referred to the distortion of competition existing downstream between travel agents. The

[35] A similar approach can be observed in *Suiker Unie*, ECJ, supra note 29. In that case, the Commission had considered that the fidelity rebates granted by SZV, a dominant sugar producer in Southern Germany to its customers, amounted to an "unjustifiable discrimination against buyers who also buy sugar from other sources than SZV". The Commission, in particular, seemed concerned by the fact that the rebate policy had been adopted so as to "limit possibilities for imports" and "to strengthen the dominant position of the producer". The Commission thus examined the horizontal effects of the rebates scheme. The Court followed the Commission's reasoning as it essentially disregarded the “competitive disadvantage” requirement contained in Article 82(c) and preferred linking the discrimination to foreclosure effects generated by the rebates.
[36] See Commission Decision 89/22 of 5 December 1988, IV/31.900, *BPB Industries plc.*, OJ L 10 of 13 January 1989 pp.50-72.
[37] Id. at §148.
[38] See CFI, *BPB Industries plc and British Gypsum Ltd. v. Commission*, T-65/89, ECR 1993 II-389 at §119.
[39] See Commission decision at §49.
[40] See Commission Decision 2000/74 of 14 July 1999, *Virgin/British Airways*, JOCE L 30 of 4 February 2000, pp.1-24.
[41] Id at §§108-111. The travel agents were thus given incentives to remain loyal to British Airways through increasing their sales of BA's tickets.
[42] Id at §111.

market for supplying air travel agency services was intensely competitive and the ability of agents to compete in supplying such services was affected by the discriminatory conditions of remunerations resulting from BA's schemes.[43]

A third form of rebates that can be discriminatory are "target rebates", i.e. those conditional on a company meeting a sales target that is higher than previous purchases. The Community courts' case-law provides several illustrations of target rebates being found discriminatory pursuant to Article 82(c). In *Michelin I*, the dominant tyre producer on the Dutch market for new replacement tyres for trucks, buses and similar vehicles paid an annual bonus to its dealers depending on their reaching of a sales target, which was set at a level higher than the purchases made in the previous years.[44] The bonus was determined individually and selectively for each dealer. In addition to showing that this practice had the effect of tying independent dealers to Michelin (thereby foreclosing competitors), the Commission identified a discrimination contrary to Article 82(c). Different bonuses were indeed granted to dealers whose situations were comparable. These bonuses were not linked to cost efficiencies, but to the loyalty that had been shown to Michelin. The Commission, however, paid no attention at all to the conditions mentioned in Article 82(c). In its assessment of the effects of the discount, the Commission only relied on the horizontal effect of the practice, namely that it "distorts the competition between tyre producers" and impedes "access to the Netherlands market for [Michelin's] competitors".[45] The Commission's findings were annulled by the ECJ, which considered that the differences in the treatment of dealers could be explained by a number of commercial reasons. It could thus not be inferred from these differences that Michelin had engaged in discrimination.[46]

In *Irish Sugar*, the Commission found that target rebates offered by Irish Sugar to major food wholesalers in Ireland were discriminatory because they were dependent on percentage increases in purchases rather than absolute purchase volumes.[47] Thus, companies ordering small volumes but having improved their sales compared to the previous year were treated similarly to companies ordering large volumes but having not increased their sales. In its reasoning, the Commission was, however, less concerned by the discrimination the rebate system introduced between distributors, than by the fact the rebates were "making it difficult for competitors to gain a foothold in the market" and "part of a policy of restricting the growth of competition from domestic sugar packers".[48] Once again, the Commission focused on the primary line effects of the measure in question rather than on its secondary line effects.

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[43] See Commission Decision, supra note 40 at §111 and CFI, *British Airways plc v Commission*, 17 December 2003, Case T-219/99, not yet published at §238.

[44] See Commission Decision 81/969 of 7 October 1981, *Bandengroothandel Frieschebrug BV/NV Nederlandsche Banden-Industrie Michelin*, OJ L 353 of 9 December 1981 pp.33-47 at §38.

[45] Id. at §49.

[46] See ECJ, *NV Nederlandsche Banden Industrie Michelin v. Commission*, 9 November 1983, 322/81, ECR [1983]-3461 at §90.

[47] See Commission Decision, supra note 30 at §154.

[48] Id at §152 and §154.

1.1.2. Price discrimination in the form of selective price cuts

A second form of price discrimination can be found in selective price cuts strategies whereby an operator cuts its prices selectively, but not below costs, to customers that might switch to a competitor, while leaving prices to other customers at a higher level.[49] The Commission has originally been quite cautious in equating these practices with price discrimination pursuant to Article 82(c). In *ECS/AKZO*, the Commission sanctioned as an abuse of a dominant position the predatory prices selectively offered and charged by AKZO to ECS's customers with a view to excluding the latter from the market.[50] Although the decision was largely based on the predatory nature of the prices, the Commission also referred to the discriminatory nature of the conduct. However, the Commission decided not to apply Article 82(c) to the matter at hand:

> "Discrimination between similarly-placed customers is expressly prohibited by Article [82](c) when it places certain firms at a competitive disadvantage. In the present case however the anticompetitive effect of AKZO's differential pricing involved not so much direct injury to customers but rather a serious impact on the structure of competition at the level of supply by reason of its exclusionary effect".[51]

The Commission prohibited AKZO from offering or applying prices which would result in customers of ECS paying AKZO prices dissimilar to those being offered by AKZO to comparable customers.[52]

In *Eurofix-Bauco v. Hilti* the Commission did not apply Article 82(c) either. Hilti had implemented a discriminatory strategy taking the form of selective price cuts and other advantageous terms in favour its competitors' main customers. Hilti's other customers did not benefit from these special conditions. The Commission considered that these practices were part of a strategy to limit the entry of competitors in the market for Hilti-compatible nails and thus relied essentially on a primary line injury reasoning.[53] The Commission held:

> "An aggressive price rivalry is an essential competitive instrument. However, a selectively discriminatory pricing policy by a dominant firm designed purely to damage

[49] See, on this, Einer Elhauge, "Why Above-Cost Price Cuts To Drive Out Entrants Are Not Predatory--and the Implications for Defining Costs and Market Power" (2003) 112 *Yale Law Journal*, 681; Aaron S. Edlin, "Stopping Above-Cost Predatory Pricing" (2002) 111 *Yale Law Journal*, 941; R. Whish, supra note 21 at 653.

[50] Commission Decision 85/609 of 14 December 1985, *ECS/AKZO*, OJ L 374 of 31 December 1985, pp.1-27.

[51] Id. at §83.

[52] Id. at Article 3(3). Article 3(5) was however annulled by the Court of Justice. See ECJ, *AKZO Chemie BV v Commission*, 3 July 1991, C-62/86, ECR[1991],I-3359.

[53] See Commission Decision 88/138 of 22 December 1987, *Eurofix-Bauco v. Hilti* OJ L 65 of 11 March 1988 pp.19-44. At §§80-81 of the Decision the Commission considered that the practice was deemed to be "designed to damage the business of, or deter market entry by, its competitors". Some have seen in the Commission's qualification of the practice a reference to both primary and secondary line injuries, see Van Bael&Bellis, supra note 18 at p.915.

the business of, or deter market entry by, its competitors, whilst maintaining higher prices for the bulk of its other customers, is both exploitative of these other customers and destructive of competition".

In more recent cases, however, the Commission and the Court held that selective price cuts could amount to price discrimination incompatible with Article 82(c) EC. In *Irish Sugar,* the target rebates scheme that was described above had an additional feature that rendered it similar to a selective price cut. The size of the target rebate varied depending on the customer at stake, i.e. being more favourable to particular customers of competing sugar packers. The Commission held that this was constitutive of "selective and discriminatory pricing". However, in analysing its effects, the Commission relied on a primary line injury analysis by stating that this practice was part of a policy of restricting the growth of competition from domestic sugar packers.[54]

A more explicit finding of price discrimination incompatible with Article 82(c) appeared in *Compagnie Maritime Belge*. The members of CEWAL, a liner conference holding a joint dominant position on shipping routes between northern Europe and Zaire had operated a "fighting ships" schemes pursuant to which they offered (i) liner services at the closest dates of sailing possible to the sailings of its main competitor, G&C, (ii) at special rates different from the rates normally charged by CEWAL and that were the same or lower than the prices of G&C. In its decision, the Commission showed that the practice amounted to a primary line injury abuse because the members of CEWAL were seeking to eliminate their principal competitor through the use of fighting ships. In addition to this finding, however, the Commission added that the practice constituted "a clear abuse of a dominant position in breach of Article [82](c)" in that it had:

> "[...] a discriminatory effect against shippers who, having to load on dates some time from the sailing dates of G&C ships, must therefore pay the higher regular conference tariff for the carriage of the same goods […]. This is because shippers have dissimilar conditions imposed on them for equivalent transactions, which places those who are forced to pay higher rates at a competitive disadvantage".[55]

The decision was appealed by the parties which argued *inter alia* that there was no discrimination because at any given time, all shippers were treated in the same way.[56] In fact, the parties were merely applying a uniform price differentiation scheme with respect to timing. The CFI and the ECJ eluded the question of price discrimination and relied on the exclusionary nature of the practice to consider it an abuse of a dominant position.[57]

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[54] See Commission Decision**,** supra note 30 at §154. This was upheld by the CFI, *Irish Sugar plc v. Commission*, 7 October 1999, T-228/97, ECR [1999] II-2969 at §§215-225.

[55] See Commission Decision 93/82 of 23 December 1992, *Cewal*, OJ L 34 of 10 February 1993 pp.20-43 at §83.

[56] See CFI, *Compagnie Maritime Belge Transports SA and Others v. Commission*, 8 October 1996, Official Journal C 336, 9 November 1996, T-24/93, T-25/93, T-26/93 and T-28/93, ECR[1996] II-1211 at §124.

[57] It is of note, however, that AG Fennelly stated: "normally, non-discriminatory price cuts by a dominant undertaking which do not entail below-cost sales should not be regarded as being anti-competitive". A contrario, this seems to imply that discrimatory selective price cuts above costs could be held abusive under Article 82 EC. See Opinion of AG Fennelly of 29 October 1998, ECR [2000] I-1365, at §132.

The question nevertheless arises as to whether a different price structure between traditional customers and competitors' customers or those contemplating shifting to a competitor should be always deemed discriminatory. As we have seen in Part II above, pricing selectively according to the elasticity of customers is widely admitted as efficiency-enhancing conduct by economists. The Commission and the Community courts have not, however, resolved the issue of whether customers with different price elasticity could be considered as being in a different situation, thereby rendering Article 82(c) inapplicable.

1.1.3 Tied and bundled pricing

Tied and bundled pricing practices represent a third form of primary line injury price discrimination. In some instances, firms subordinate the granting of a discount to the acquisition by the purchasers of two distinct products. In *Eurofix-Bauco v. Hilti*, the Commission sanctioned Hilti on the ground that it had granted special discounts for the combined purchase of cartridge strips and nails and/or that it refused or reduced normal discounts for customers buying cartridge strips only.[58] In spite of the reference to the discriminatory character of this policy, the Commission did not rely on Article 82(c). It merely held that the practice had the effect of both exploiting the customers, as well as producing a horizontal effect by "excluding independent nail makers who may threaten the dominant position Hilti holds".

The lack of attention given to the discriminatory effects of tied or bundled pricing appeared even more clearly in *Napier Brown*. In that case, a dominant sugar supplier, British Sugar, had refused to grant an option to its customers between purchasing sugar on an ex factory (i.e., without delivery) or delivered price basis. The Commission considered that British Sugar's conduct whereby it only sold sugar provided that it also delivered it was contrary to Article 82 EC. The Commission did not make any reference to Article 82(c) and relied on the fact that the practice produced an exclusionary effect on the neighbouring market for the delivery of sugar. The Commission could, however, have identified a discriminatory effect because a price including the cost of delivery was charged even when the purchasers did not wish to have the sugar delivered by British Sugar.

The discriminatory effects of tied or bundled pricing have received more attention from the Commission in recent years. In the *Digital* case, the Commission considered that Digital, a dominant operator in the field of software maintenance services and other hardware services had abused its dominant position by engaging in discriminatory practices and tied sales.[59] Digital was charging discriminatory prices depending on whether the customer bought computer hardware from the same supplier. The Commission relied on a primary line injury argumentation. It stated that this policy "revealed a clear desire to obstruct the ability of independent service suppliers to compete

[58] See Commission Decision, supra note 53 at §§ 34(5) and 75.
[59] See XXVIIth Report on Competition Policy – 1997, at §69. See also, L. Ritter and D. Braun, supra note 28 at p.452.

with Digital on the markets for maintenance services and other, hardware services for Digital computers".

Further, in *Van den Bergh Foods*, the Commission relied on the wording of article 82(c), although this provision was not explicitly mentioned.[60] A dominant ice cream manufacturer in Ireland had adopted a pricing policy towards its retailers whereby it supplied its ice cream products and freezer cabinets at an "inclusive price", i.e. the freezer cabinets and the ice cream were bundled together in a single price. This produced discriminatory effects as retailers that already had their own freezer cabinet paid the same price as those that acquired a freezer cabinet from Van den Bergh foods. In its statement of objections, the Commission considered that this policy breached article 82 EC in that it:

> "[...] gave rise to discrimination between trading partners, by treating dissimilar situations in a similar fashion. Retailers with their own freezer cabinets effectively paid for a service which they did not receive and, in so doing, were forced to subsidise cabinet provision to those taking HB cabinets; the former retailers thereby placed themselves at a competitive disadvantage *vis-à-vis* the latter ones".[61]

The issue was subsequently resolved, with Van den Bergh foods abandoning the inclusive pricing policy and replacing it by a "differential" pricing scheme, whereby retailers that would not purchase the freezers would receive from Van den Bergh foods a lump sum reflecting the purchase and maintenance cost savings of the latter in not supplying and servicing a freezer cabinet to the retailer.[62]

1.2 Why have the Commission and the Community courts mistakenly relied on Article 82(c) to address primary line cases?

As we have seen in Part IV, it is clear from the wording of Article 82(c) that this provision was designed to prevent price discrimination practices which placed a dominant firm's customers at a competitive disadvantage vis-à-vis other customers. Article 82(c) thus seeks to prevent secondary line price discrimination. Interestingly, the majority of the cases in which the Commission and the Community courts evoked Article 82(c) essentially deal with primary line injury. The mechanisms put in place by the dominant firms in question typically sought to produce exclusionary effects designed to encourage competitors to exit the market and to prevent entry.[63] The question why the Commission nonetheless relied (explicitly or implicitly) on Article 82(c) thus arises. Several reasons may have prompted the Commission and the Court to use this provision in an extensive fashion.

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[60] See Commission Decision 98/531 of 11 March 1998, *Van den Bergh Foods Limited*, OJ L 246 of 4 September 1998, p.1.
[61] Id. at §76.
[62] Id. at §77.
[63] In most of these cases, complainants were not the trading parties, but the competitors, suffering the exclusionary effect of the practice. This probably reveals that the trading parties did not consider having themselves been put at a competitive disadvantage.

A first reason for the Commission's extensive interpretation of the concept of price discrimination lies in the early history of the application of Article 82 EC. Besides the fact that the ESCC Treaty's provision on price discrimination did not draw any distinction between primary line and secondary line injuries,[64] the possibility to apply Article 82 to primary line discrimination settings was supported early by a group of scholars appointed in the 1960s by the Commission to advise it on the application of Article 82 EC.[65] More importantly, the ECJ delivered several rulings under Article 82 EC where it imposed fairly limited constraints on the Commission to prove an abuse of a dominant position. In particular, the ECJ ruling in *Continental Can*, indicated to the Commission that the list of abusive practices mentioned in the Treaty was not exhaustive.[66] This opened the way to subsequent broad pronouncements on the issue of price discrimination. An important step was made in 1979 with the seminal *Hoffmann-La Roche* ruling where the Court delivered a signal whereby to reach a finding of price discrimination under Article 82(c), it was not necessary to apply strictly the conditions imposed by that provision. As Advocate General Van Gerven rightly observed in his Opinion under *Corsica Ferries*:

> "It appears implicitly from the Community case-law, [...] that the Court does not interpret that phrase [i.e. "applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage"] restrictively, with the result that it is not necessary, in order to apply it, that the trading partners of the undertaking responsible for the abuse should suffer a competitive disadvantage against each other or against the undertaking in the dominant position.[67]

The requirement of a secondary line injury for evidencing an abuse of a dominant position having been largely removed from Article 82(c), the Commission enjoyed a large scope for developing a *praeter legem* policy against price discrimination.[68] This

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[64] It merely prohibited "[...] discriminatory practices involving, within the common market, the application by a seller of dissimilar conditions to comparable transactions [...]". See Article 60(1) of the ECSC Treaty.

[65] See David Gerber, *Law and Competition in Twentieth Century Europe – Protecting Prometheus*, Clarendon Press Oxford, 1998, at 356-357. In the early 1960s, the Commission sought to establish a theoretical framework for interpreting the abuse concept enclosed in Article 82 EC through the appointment of a group of professors charged with the duty to work out the basic enforcement principles of this provision. The group of Professors released a Memorandum on Concentration in the Common Market in 1966 which seemed to suggest that the concept of price discrimination enclosed in Article 86(c) could encompass the eviction of competing companies. See, contra, René Joliet, *Monopolization and Abuse of a Dominant Position*, Collection scientifique de la Faculté de droit de l'Université de Liège, 1970 at 477. Professor Joliet argued that Article 82(c) merely applied to secondary line discriminations and did not apply to "discriminatory price cutting having adverse effects upon primary-line competition".

[66] ECJ, *Europemballage Corporation and Continental Can Company Inc. v Commission*, 21 February 1973, 6-72, ECR [1973]-215**.**

[67] In its ruling on the case, the Court of justice did not even mention the condition of competitive disadvantage in its judgment. See Van Bael&Bellis, supra note 18 at 917.

[68] As it seems it has been read out from Article 81(1) (d) EC. The extensive reliance on Article 82(c) for sanctioning primary line injuries price discrimination merely mirrors the evolution of case law and decisional practice of the Commission under Article 81(d), which forbids collusive discriminatory action in the same terms as Article 82 EC. In its decision *Industrieverband*, the Commission implicitly envisaged the application of the concept of discrimination in a primary line injury setting by holding that a collective aggregated sales bonus (i.e. a concerted bonus granted to all customers purchasing from the members of the association of undertakings) was placing "other suppliers at a competitive disadvantage, since they [had] to

explains why the Commission has been able in a number of cases to rely on a primary line injury reasoning to sanction discriminatory business conduct. The Commission was further comforted in its approach by subsequent judgments of the Community Courts (e.g., *Tetra Pak II*) holding that the proof of an abuse did not require bringing evidence of the anticompetitive effects of the conduct at stake.[69]

Second, in a number of cases, the Commission seized the opportunity that was given to it to apply Article 82(c) beyond the limited scope of secondary line price discrimination in support of a finding of abuse of dominance in a primary line setting. Indeed, in most cases involving primary line price discrimination, the question arises whether the practice at stake is a normal competitive strategy that should not be condemned (the so-called "meeting competition" strategy) or whether it is an exclusionary behaviour that seeks to exclude competitors from the market. This is, in particular, important in the context of above costs selective price cuts, where the case-law requires, for a finding of an abuse of a dominant position, to show that the firm under scrutiny has the intent to eliminate its competitors.[70] In these cases, a finding of discrimination may have helped reaching the legal evidentiary level required to identify a finding of abuse under Article 82 EC. This is apparent in the *Irish Sugar* case where the imposition of discriminatory prices was interpreted as one of the elements showing a policy of restricting the growth of competition from domestic sugar packers.[71]

Third, linked to the prior observation may also be the fact that most forms of pricing abuses involve some aspect of discrimination. A finding of discrimination may thus not only lower the evidentiary threshold for the finding of an abuse, but also allow the Commission to impose a higher fine, considering it has established two separate infractions. In *Irish Sugar* and in *British Airways*, for instance, the Commission combined a finding of exclusionary abuse (under Article 82(b)) with a price discrimination abuse (under Article 82(c)).

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surmount an artificial, collectively erected barrier when supplying members' customers and this generates business for the members". On appeal before the Court, the Commission confirmed that it interpreted the discount at stake as a discriminatory practice. See Commission Decision 80/1074 of 16 October 1980, *Industrieverband Solnhofener Natursteinplatten eV*, OJ L 318 of 26 November 1980 pp.32-39. In a number of other decisions, the Commission applied similar principles. In *Roofing Felt*, for instance, the Commission sanctioned a concerted campaign against another manufacturer, IKO, to induce it to abandon a price-cutting policy, through application of discriminatory rebates. See Commission Decision 86/399 of 10 July 1986, *Roofing felt*, OJ L 232 of 19 August 1986, pp.15-33. In *Meldoc*, the Commission sanctioned the concerted implementation of dumping prices to prevent imports from Belgium suppliers on the Dutch market for fresh milk. See Commission Decision 86/596 of 26 November 1986, *Meldoc* OJ L 348 of 10 December 1986 pp.50-65.

[69] For instance, in the recent *Deutsche Post AG* case, the Commission justified its superficial assessment of the discriminatory conduct at stake by recalling the *Tetra Pak II* ruling pursuant to which "Article 82 may be applied even in the absence of a direct effect on competition". See Commission Decision, infra note 112 at §133. See CFI, *Tetra Pak International SA v. Commission* (*Tetra Pak II*), 6 October 1994, T-83/91, ECR [1994] II-755.

[70] See ECJ, *Compagnie Maritime Belge Transports SA* (C-395/96 P), *Compagnie Maritime Belge SA* (C-395/96 P) *and Dafra-Lines A/S* (C-396/96 P) *v. Commission*, 16 March 2000, ECR [2000] I-1365 at §119.

[71] See Commission Decision, supra note 30 at §§145 and following.

Finally, if it had not been extended by the Commission, Article 82(c) would have remained "dead letter". Indeed, from an economic viewpoint, a seller that is not vertically-integrated often would seem to have little incentive to want to distort downstream competition since it benefits from a competitive downstream market for distributing its goods.[72] A pricing practice that removes distributors from the market may produce two kinds of adverse effects on the seller. First, the distributors may compete less aggressively for the distribution of the goods at stake. Second, a risk of consolidation of the market structure downstream may reduce the bargaining power of the upstream firm and consequently negatively affect its revenues. This may explain why the Commission has only shown little interest towards secondary line price discrimination and has preferred curbing the provision towards an active policy against primary line discrimination.

These reasons explain to one degree or another why Article 82(c) has been extended by the Commission and the Community courts to primary line price discrimination.[73] As noted in Part IV above, we believe this extension is unfortunate as it applies the wrong legal test to primary line abuses. Since such abuses involve exclusionary effects, they would be better dealt with under Article 82(b).

2. Price discrimination in a primary line setting: An economic analysis

In the preceding section, we have shown that the Commission and the Community courts have wrongly relied on Article 82(c) for condemning price discrimination strategies that produce primary line effects. In this section, we argue that, independently of the problem of the legal basis on which they based their decision, the position taken by the Commission and the Community courts when dealing with primary line schemes has generally been over-restrictive. We thus suggest that these authorities should take a more cautious approach to price discrimination. The discussion which follows focuses on the most contentious form of price discrimination, i.e. rebates. It does not propose to offer responses to all the issues raised by rebate schemes, but instead to give a few guidelines on how to deal with them in a more coherent and analytically correct fashion than under the current case-law.

The Commission and the Community courts’ position that only rebates that correspond to cost efficiencies should be compatible with Article 82 EC is plainly wrong. First, the circumstances in which cost savings can be achieved by selling greater volumes are limited and clearly do not apply to a series of industries, such as network industries and industries based on information goods. Selling 1000 software licences to a customer instead of 500 will not trigger significant cost savings as additional sales generate small transaction costs. Taken literally, the Commission and the Community courts’case-law

[72] See infra at V(B)2.

[73] Interestingly, the US Robinson Patman Act, which was historically adopted with the main aim to prevent price discrimination from damaging competition between downstream customers (secondary line effects) has also been applied from the start to primary line effects. The main difference between EC law and US law, however, is that price discrimination has hardly been subject to enforcement since the 1980s.

would mean that rebates on such additional sales could never be justified. Second, economies of scale are rarely linear. Thus, even if some cost savings could result from selling larger amounts to customers, it would be highly unlikely for such savings to be mirrored exactly by a linear discount structure such as the one postulated by the Court.[74] Finally, the application of such a test may run into practical difficulties. Verifying whether a given discount corresponds to cost savings may prove particularly challenging as it requires the gathering of information over the dominant firm's costs structure, as well as the cost efficiencies it can realize through an increase of its output.[75]

Second, the restrictive position of the Commission and the Community courts largely ignores the necessity for industries facing high fixed costs to recover such costs through price discrimination. As we have seen above, firms that engage in substantial investments need to recover their fixed costs by pricing their products or services above marginal costs. For such firms, it makes a great deal of sense to price discriminate between customers whose willingness to pay for the product or service in question is high and those whose willingness to pay is low. While the prices charged to the former will be well in excess of marginal costs, the prices charged to the latter will be near marginal costs, but nevertheless contribute to the firm's fixed costs.[76] This approach enhances welfare in at least two different ways. First, it allows the price discriminating firm to efficiently recover its fixed costs and thus protects its ex ante incentives to make investments.[77] Moreover, customers with a low willingness to pay might be able to acquire a product or service, they may not necessarily be able to afford under a uniform price.

Third, the decisional practice of the Commission and the Community courts' case-law tend to ignore the fact that a ban on price discrimination may facilitate tacit collusion at both retail and supply levels, in a similar way as "Most Favoured Nation Clauses" notoriously do.[78] As far as the retail level is concerned, distributors operating in a same market may (provided certain conditions are met, such as transparency, concentration at the retail level, etc.) understand each other's pricing policies and thus be able to tacitly collude on similar retail prices.[79] In such a context, a rule forbidding suppliers to price discriminate may help sustain a tacitly coordinated equilibrium at the retail level. Indeed, uniform pricing most likely tends to harmonize costs for distributors. This is problematic

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[74] See D. Ridyard, supra note 1 at 289 and D. Waelbroeck, 31 at 152.

[75] See D. Waelbroeck, supra note 31 at 158 who specifies as: "(i) defining a proper methodology for measuring costs in each industry [...]; (ii) deciding how the costs savings can be attributed to each customer [...]; and (iii) laying down what the appropriate time period for recovery of fixed costs shall be [...]".

[76] See D. Ridyard, supra note 1.

[77] By contrast, if a firm with market power is forced to charge uniform prices, any price reduction it makes to get a marginal customer will make it lose some profits from the inframarginal customers who are prepared to pay a higher price. Thus, a firm with market power which can only impose a uniform price will select a price that many marginal customers will not be willing to pay even though they value the product more that the marginal cost of producing it. This clearly leads to allocative inefficiency.

[78] See R. Posner, supra note 3 at 81. A Most Favoured Nation clause is a clause pursuant to which a contracting party commits itself to treating all its customers the same way that is to extend the benefit of any advantage offered to a customer to its other customers.

[79] See Alan J. Cox, "The Frequently Forgotten Benefits of Price Discrimination" in the *Economics of Antitrust – New Issues, Questions and Insights*, Lawrence Wu Ed., NERA Economic Consulting, 2004 at 106.

for two reasons. First, it gives retailers a focal point for approximating their pricing policies around a similar benchmark. Second, it reduces the scope for the retailers to deviate from the coordinated retail price provided the input represents a large fraction of the costs incurred by the retailers. In contrast, charging different prices to distributors in a manner that does not necessarily reflect cost differences may jeopardize the viability of a downstream collusive course of conduct. Safeguarding the possibility to grant a competitive advantage to a customer may thus be good policy where downstream markets demonstrate oligopolistic features.

As far as the supplier level is concerned, an outright prohibition of price discrimination may also contribute to stabilising a situation of tacit collusion in industries where, for a number of reasons (e.g., high sunk costs, increasing returns on scale, natural capacity constraints, etc.), the market structure has oligopolistic features. This is so because a requirement of pricing uniformly for all customers may offer a convenient device for monitoring adherence to an explicit or tacit collusive scheme upstream.[80] Indeed, a deviating operator would have to extend the benefit of a price cut to all its customers on the market, and accordingly reopen negotiations with all of them, an event likely to be noticed by its competitors. In addition, the cost of monitoring adherence to the coordinated scheme decreases, because instead of monitoring all the transactions entered into by each customer on the market, the monitoring of the prices offered to only one distributor is sufficient to identify the initiation of a cheating strategy by one of the suppliers.

Fourth, suppliers often try to induce their distributors to invest in distribution facilities or to introduce innovative systems of distribution through pricing policies that are not strictly justified by cost savings.[81] On this issue, the current state of the case-law of the Community courts seems again overly restrictive. In *Michelin II*, the service bonus (an additional financial reward offered by Michelin to improve the service by the dealers) was condemned by the CFI because it was held to be subjective and thus inevitably led to discrimination. In addition to the fact that most of the criteria for granting the bonus were strictly objective, neither the Court nor the Commission assessed the potential for discrimination stemming from the alleged subjectivity. Unlike non dominant firms, companies enjoying substantial market power may thus be deprived of the possibility to reward the increased quality of the service of their distributors.[82]

Against this background, let us now critically examine the position taken by the Commission and the Community courts with respect to the various forms of rebates examined above. First, we have seen that the quantity rebates are unobjectionable under

[80] The CFI has held that a detection mechanism is a necessary condition for coordinated effects to occur in an oligopolistic market. See CFI, *Airtours plc v Commission*, 6 June 2002, T–342/99, [2002] E.C.R. II–2585 at §62 and CFI, *Laurent Piau v. Commission*, 18 March 2005, T-193/02, not yet published at §111.

[81] See A. Cox, supra note 79 at 103-104.

[82] See CFI, supra note 31 at §140: "The granting of a discount by an undertaking in a dominant position to a dealer must be based on an objective economic justification [...]. It cannot depend on a subjective assessment by the undertaking in a dominant position of the extent to which the dealer has met his commitments and is thus entitled to a discount".

EC competition rules when they correspond to cost efficiencies.[83] For reasons explained above, this position is excessively restrictive and fails to take into account the reasons why dominant, as well as non-dominant firms, engage in price discrimination. This is not to say that all quantity rebates should be declared compatible with EC competition rules. Indeed, quantity rebates can create serious secondary line injuries, notably when they are a reflection of buyer market power.[84] One or several large buyers might indeed be able to extract such rebates from a (dominant) supplier, thereby creating the risk of harming the competitive position of smaller competitors.[85] In such cases, the quantity rebates would in fact fulfil the conditions of Article 82(c) and should thus be prohibited under this provision.

While the Commission and the Community courts accept some forms of quantity rebates (those related to cost efficiencies), they apply a *per se* rule to fidelity and target rebates on the ground that such rebates produce exclusionary effects. Here again, this position seems over-restrictive. While such rebates may have some anti-competitive effects, this is not necessarily the case. As noted in the OECD Report on fidelity and discount rebates "because fidelity discounts have potentially pro- and anti-competitive effects, and both are highly dependent on specific features of the discounts and the markets they are found in, a case by case approach to fidelity discounts seems warranted".[86] Prohibiting fidelity and target rebates as a matter of principle thus leads to Type I errors (false convictions). The difficulty is, however, to find a test, which allows distinguishing pro-competitive rebates from anti-competitive ones.

A simple test would be to say that rebates are pro-competitive when they increase total output and anti-competitive when they fail to do so. A modified version of such a test was, for instance, suggested by John Vickers in a speech delivered in 2001 where he stated that: "[i]ncreased supply … is *necessary but not sufficient* for price discrimination not to have an adverse effect on economic efficiency and on consumers".[87] This statement raises, however, two problems. The first one is that it does not say why an increase in output is not sufficient for a rebate to benefit from a presumption of legality. It does not explain either which additional test should be applied to output enhancing rebates to be considered pro-competitive. The second is that, applied at face value, this test would be excessively severe as it would amount to a *per se* rule against rebates,

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[83] See Commission Decision in *Michelin I*, 81/969 of 7 October 1981 supra note 44.

[84] The strictness of this position can be clearly observed from the following passage of the Commission Decision in *Michelin I* at §54: "with the exception of short-term measures, no discount should be granted unless directly linked to a genuine reduction in the manufacturer's costs".

[85] See OECD report on loyalty and fidelity discounts and rebates, DAFFE/COMP(2002)21 at p. 7 ("Standard volume rebates tend to be a comparatively blunt instrument for encouraging customers to increase their purchases. Their existence is as much a reflection of large buyer power rather than any seller objective or initiative. Large buyers expect to obtain better terms than smaller buyers and they can often recognise that the seller's fixed cost recovery problem translates to a negotiating weakness when it comes to large buyers. For suppliers, even those who enjoy significant market power, who have low marginal costs of supply and high fixed costs, any threat of withdrawal of purchases or goodwill by a large buyer carries a significant business risk. Volume discounts are often a reaction to this risk.").

[86] Id.

[87] See John Vickers, "Competition Policy and Innovation", *Speech to the International Competition Policy Conference*, Oxford, 27 June 2001.

which do not increase output. While economic theory teaches that rebates increasing total output are generally pro-competitive, there is little basis to say that rebates that increase the sales of a dominant firm while not necessarily increasing total output (increased sales being taken away from competitors) should necessarily be considered as being anti-competitive.

A preferable approach can be found in the OFT Guideline 402 on The Chapter II Prohibition:

> "In general, price discrimination will not be an abuse in such industries [i.e. those with high fixed costs in relation to marginal costs] if it leads to higher levels of output than an undertaking could achieve by charging every customer the same price."[88]

This guideline thus suggests that, in industries facing fixed-cost recoveries issues, rebates (or other forms of price discrimination) enhancing total output would not amount to an abuse of a dominant position. This approach, to which we subscribe, presents the advantage of creating a safe harbour for output enhancing rebates motivated by fixed-costs recovery. In addition, it does not automatically prohibit rebates that do not increase total output. Such rebates should thus be assessed on a case-by-case basis.

The question remains, of course, to determine the test(s) on the basis of which the pro- or anti-competitive nature of fidelity or target rebates that do not increase total output should be assessed. A wide range of criterions have been proposed by authors, which the scope of this paper does not allow to exhaustively review. The discussion that follows offer a few guidelines on the steps the Commission and the Community courts should take before declaring such rebates in violation of Article 82 EC.

A first logical step in the analysis would be to demonstrate that the rebates in question generated concrete anti-competitive effects. To the extent that the goal of investigating such rebates is to prevent exclusionary effects, the most elementary obligation for the enforcement authorities should be to show that such effects have occurred in the case at hand.[89] Unfortunately, in *British Airways*,[90] the CFI held that "for the purposes of establishing an infringement of Article 82 EC, it is not necessary to demonstrate that the abuse in question had a concrete effect on the markets concerned. It is sufficient in that respect to demonstrate that the abusive conduct [...] tends to restrict competition, or in other words, that the conduct is capable of having, or likely to have such an effect". This position, which the CFI repeated in *Michelin II*,[91] is regrettable as it dispenses the Commission from showing that the rebate scheme in question has negatively affected the structure of the market. For instance, in *Michelin II*, the CFI upheld a finding of abuse while the market shares and the prices of the dominant firm had been steadily falling over

[88] See OFT Guideline 402, The Chapter II Prohibition at §4.15.
[89] Unlike *ex ante* control such in merger cases, *ex post* control under Article 82 EC involves matters where the effects of the allegedly anti-competitive conduct can generally be observed.
[90] See CFI, *British Airways plc v Commission*, supra note 43.
[91] See CFI, *Michelin II*, supra note 31.

a 10-year period. In addition, Michelin's competitors had reinforced their position on the market and new manufacturers had entered the market.[92]

Second, when some negative effects on the market can be identified, the enforcement authority should also determine that such effects result from the rebates adopted by the dominant firm. Any loss of market share by rivals should not necessarily lead to the banning of such rebates. First, rebates (and, more generally, prices) are not the only parameters of the competitive process. Rivals' market share losses may thus be explained by a variety of factors, such as the quality of the products offered, the service provided to the customers, etc. Moreover, Article 82 EC should not be used to protect inefficient competitors, but competitors that are as or more efficient than the dominant firm but whose survival on the market would be threatened by exclusionary strategies. The application of the equally-efficient competitor test may, however, raise difficulties in industries with declining total average costs due to the presence of economies of scale. In such industries, a new entrant that would be overall as efficient as the dominant firm might nevertheless be unable to compete with the dominant firm's prices unless it could start its operations on a sufficient scale. The problem with fidelity and target rebates is that, by locking in customers, they may prevent equally efficient competitors from reaching or maintaining a scale to operate profitably on the market. This may lead enforcement authorities to adopt measures designed to limit the customer lock-in effects of some rebate schemes.

In sum, common sense pleads for a case-by-case approach to the assessment of rebates. While a form of rebate may create serious foreclosure effects on a given market, the same measure will have benign effects on another. As seen above, a variety of factors should be taken into account when assessing rebates, such as whether such rebates enhance total output, whether the affectation of the structure of competition following the adoption of rebates is linked to exclusionary effects that would be produced by such rebates or other factors, such as the lower efficiency of competitors, etc.

B. Price discrimination in secondary line injury settings

This sub-section first seeks to determine the circumstances in which Article 82(c) has been used to condemn secondary line injury price discrimination practices and then analyses whether this provision was the right legal basis for assessing these practices (1). It then explores whether the decisions of the Commission and the Community courts' case-law dealing with secondary line discrimination is well in line with economic theory (2).

1. Price discrimination in secondary line injury settings: A legal analysis

The purpose of this section is first to identify the different scenarios of secondary line price discrimination, i.e. discrimination affecting the conditions of competition at the downstream level. The decisional practice of the Commission and case-law of the ECJ has applied Article 82(c) to secondary line injury settings in two main situations, which

[92] See CFI, *Michelin II*, supra note 31 at §236 and D. Waelbroeck, supra note 31 at 159.

will be discussed below (1.1). This section then discusses whether Article 82(c) is the right legal basis for sanctioning these practices of secondary line price discrimination (1.2).

1.1. Main forms of secondary line price discrimination measures examined under Article 82(c)

A first scenario can be found when non vertically-integrated operators apply discriminatory prices to their customers (1.1.1). A second scenario involves discriminatory pricing by vertically-integrated operators (1.1.2).

1.1.1. Secondary line injury price discrimination by non vertically-integrated operators

The decisional practice of the Commission and the case-law of the Community courts provide various examples of secondary line injury price discrimination by non vertically-integrated operators, in particular in the transport sector where an undertaking (often a public one) has been granted an exclusive right to operate an essential facility without, however, being active on the downstream market. Most of the cases dealt with by the Commission and the courts involved discriminations on the ground of nationality, or measures trying to favour domestic activities over international and/or non domestic ones.

In *Corsica Ferries II*, the corporation of pilots of the port of Genoa had received from the public authorities the exclusive right to provide compulsory piloting services in the port of Genoa.[93] The piloting tariffs had been fixed by the corporation of pilots and approved by the Minister. Various reductions of the basic tariff applied for vessels permitted to carry out maritime cabotage, i.e. traffic between two Italian ports. Only vessels flying the Italian flag could obtain permission to engage in maritime cabotage and, thus, benefit from the tariff reductions. Corsica Ferries, a maritime transport operator which operated a liner service between the port of Genoa and various Corsican ports complained of the discriminatory nature of the tariffs. The ECJ held that:

> "Article [82](1) and Article [86] of the Treaty prohibit a national authority from enabling an undertaking which has the exclusive right of providing compulsory piloting services in a substantial part of the common market to apply different tariffs to maritime transport undertakings, depending on whether they operate transport services between Member States or between ports situated on national territory".[94]

Indeed, as Advocate General Van Gerven had explained in his Opinion, the compulsory piloting services carried out by the corporation of pilots were "strictly the same", for both

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[93] See ECJ, 17 May 1994, *Corsica Ferries Italia Srl v Corpo dei Piloti del Porto di Genova*, C-18/93, ECR [1994] I-1783.

[94] Id. at §45. This ruling was subsequently confirmed by the Commission in a decision which condemned the Italian Republic for not complying with the ruling. See Commission Decision 97/745 of 21 October 1997, OJ L 301 of 5 November 1997 pp.27-35.

the company that was active on the cabotage market or on an international line.[95] The measure was in fact a subtle and indirect way to confer an advantage on national economic operators.

Similar examples of sellers conferring a preferential treatment on specific undertakings can also be observed in a number of cases involving airport facilities. For instance, in the *Brussels National Airport* case, the Belgian legislation provided for a system of stepped discounts on landing fees, which favoured airlines that had a large volume of traffic at Brussels airport over airlines having a lower traffic.[96] The thresholds established by the Belgian legislation were such that only a carrier based at the airport could benefit from the discounts to the detriment of other Community carriers. This had the effect of favouring the Belgian public carrier over its competitors. The Commission considered that Article 82(c) could be applied to cases where:

> "an undertaking in a dominant position [gives] preference to another undertaking from the same State or another undertaking which is pursuing the same general policy".[97]

In this case, the State, acting through its intermediary, i.e. the Belgian Airways authority enjoying an exclusive right on the market for aircraft landing and take off services, was giving "preferential treatment" to a specific undertaking, i.e. the national public airline Sabena. The Commission hence applied Article 86 in combination with Article 82(c).

A similar line of reasoning was followed by the Commission in the *Portuguese Airports* case, where discounts on landing fees *de facto* created an advantage in favour of national airlines.[98] Furthermore, this case also concerned the application of different landing charges to domestic and international flights (and in particular intra-EEA flights). These measures were also held to be discriminatory within the meaning of Article 82(c) because the landing and take off services provided by the airports were the same, irrespective of the fact whether the airline had an international or domestic activity.[99]

In *Alpha Flight/Aéroports de Paris*, ADP, the manager of the Paris airports had charged commercial fees to Alpha Flight and OAT, two suppliers of ground-handling services in return for the granting of a licence to operate in one of the airports (i.e., a form of access fee remunerating the services provided by the airport manager, i.e. supervision and organisation of ground-handling activities).[100] The commercial fee paid by each of the

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[95] See Opinion of Advocate General Van Gerven delivered on 9 February 1994 under C-18/93, ECR [1994] I-1783 at §19.
[96] See Commission Decision 95/364 of 28 June 1995 OJ, L 216 of 12 September 1995 pp.8-14.
[97] Id at §17.
[98] See Commission Decision 1999/199 of 10 February 1999, *Portuguese Airports*, OJ L 69 of 16 March 1999, pp.31-39 at §26. A similar line of reasoning was followed in a decision concerning the landing charges applied by the Spanish Airport Authorities, see Commission Decision 2000/521 of 26 July 2000, OJ L 208 of 18 August 2000 at pp.36-46 at §§48-53.
[99] See Commission Decision 1999/98 of 10 February 1999, *Ilmailulaitos/Luftfarsverket*, OJ L 69 of 16 March 1999, pp.24-30 and Commission Decision 1999/199, *Portuguese Airports*, supra note 98.
[100] See Commission Decision, 98/153 of 11 June 1998, *Alpha Flight Services/Aéroports de Paris*, OJ L 230 of 18 August 1998, pp.10-27.

suppliers was calculated on the basis of their respective turnover.[101] Following a complaint filed by Alpha Flight, the Commission's investigation revealed that the fees were applied in a discriminatory manner. It appeared indeed that on the basis of equivalent turnovers, the fees paid by OAT were substantially different. In addition, self handling airlines were charged much lower fees than the companies providing ground-handling activities to airlines, although the management services supplied by ADP to both kinds of operators were strictly similar.[102] The Commission thus considered that the variation of the fee from one supplier to another within a same airport distorted competition between suppliers or users of ground-handling services and thus was a discrimination contrary to Article 82(c).[103] The hypothesis of a discrimination on the ground of nationality, although not explicitly referred to in the decision, could not be ruled out, given that at the time of the case, ADP and OAT (a subsidiary of Air France) were both national public companies, whereas Alpha Flight was a subsidiary of a UK company.

1.1.2. Secondary Line Injury Price Discrimination by Vertically-Integrated Operators

Markets structures where vertically-integrated firms control essential inputs are often prone to secondary line injury price discrimination. Indeed, vertically-integrated operators have generally a strong incentive to charge a lower price to their downstream subsidiary than to the latter's competitors. The decisional practice of the Commission and the case-law of the Community courts contain several examples of this.

A first illustration can be found in the *Deutsche Bahn* case. Transfracht, a subsidiary of the German Railway operator was active in the carriage of maritime containers to or from Germany passing through German ports. Intercontainer was active in the carriage of maritime containers to or from Germany, passing through western ports (Belgium and Netherlands ports). Although providing a similar service (i.e., the carriage of maritime containers to and from Germany), both firms had been charged different prices by Deutsche Bahn for access to the rail infrastructure. The facts revealed, for instance, that the price differences ranged from 2 to 77% in respect of the carriage of empty containers in favour of Transfracht. The Commission and the CFI thus considered that Deutsche Bahn had infringed article 82(c) EC in applying dissimilar conditions to equivalent services. The discrimination had the effect of placing the parties operating from western ports at a competitive disadvantage vis-à-vis Deutsche Bahn and its subsidiary.[104] In support of this, the Commission had gathered evidence that Deutsche Bahn's price discrimination had substantially limited the carriage of containers between the western ports and Germany in favour of imports and exports to and from Germany through the port of Hamburg.[105]

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[101] OAT global fee's structure was, however, slightly different.

[102] Id at §§119 and 121.

[103] Id. at §126 of Commission Decision. Confirmed by CFI, *Aéroports de Paris v. Commission*, 12 December 2000, T-128/98 [2000] ECR II-3929 and ECJ, *Aéroports de Paris v. Commission*, 24 October 2002, C-82/01, ECR [2002] I-9297.

[104] See CFI, *Deutsche Bahn AG v. Commission*, T-229/94, ECR [1997] II-1689 at §93.

[105] See Commission Decision 94/210 of 29 March 1994, *HOV-SVZ/MCN*, OJ L 104 of 23 April 1994 pp.34-57 at §254.

The CFI dismissed the two justifications raised by Deutsche Bahn for discriminating between Transfracht and Intercontainer. First, it rejected the alleged cost reductions achieved in German ports by Deutsche Bahn through rationalization strategies because there was no reason why these rationalization strategies had not been implemented with respect to carriage of containers coming from western ports.[106] Second, the greater competition from other carriage methods on routes originating from western ports could not justify higher tariffs. To the contrary, this greater competition should have given rise to a reduction of Deutsche Bahn tariffs applied on the western journeys.[107]

A similar scenario took place in the famous *ITT Promedia* saga. Belgacom, the Belgian national telecommunications operator was active on the market for the publishing of telephone directories through its subsidiary, Belgacom Directory Services (BDS).[108] ITT Promedia N.V., a directory-publishing company that wanted to have access to data regarding Belgacom's subscribers, complained to the Commission that the latter had applied, inter alia, discriminatory prices for access to the data on its subscribers for voice telephony services. In particular, ITT had been charged a price representing 34% of its turnover. The Commission considered that there was no justification for this, except the market power associated with Belgacom's dominant position. In the course of the proceedings, Belgacom, however, agreed to abolish the turnover price component and to adopt a calculation based on the ratio of total annual costs to the number of publishers. Absent any published decision on this element of the case, it would be speculative to guess whether the Commission relied on Article 82(c) during the proceedings. At any rate, however, the facts of the case are a blatant illustration of secondary line price discrimination by a vertically-integrated operator.

In *Deutsche Post*, the Commission decided that Deutsche Post had infringed Article 82 EC by *inter alia* surcharging incoming cross-border letter mailings from the UK sent by senders outside Germany but containing a reference in its contents to an entity residing in Germany.[109] By surcharging such mailings, Deutsche Post tried to put an end to ABA remailing, a practice whereby German customers would mail from the UK letters to be sent to German addresses. The Commission found that Deutsche Post committed an abuse of a dominant position on the market for the forwarding and delivery of incoming cross-border letter mail in Germany by price discriminating between incoming cross-border letter mail which it considered to be genuine international mail and incoming cross-border letter mail which it considered to be virtual ABA remail. The Commission found that this conduct could fall under Article 82(c) as Deutsche Post imposed dissimilar prices to equivalent transactions, a situation that placed some of its trading parties (e.g., mail order companies operating from the UK indicating in the contents of their mailings a reference to an entity residing in Germany) at a competitive disadvantage vis-à-vis other

[106] See CFI, supra note 104 at §90.
[107] Id. at §91.
[108] See XXVIIth report on Competition Policy, 1997 at §67 and Commission press release, IP/97/292 of 11 April 1997, "Settlement reached with Belgacom on the publication of telephone directories - ITT withdraws complaint".
[109] See Commission Decision 2001/892 of 25 July 2001, *Deutsche Post AG - Interception of cross-border mail*, OJ L 331 of 15 December 2001, pp.40-78.

trading parties (e.g., mail order companies operating from the UK not indicating such a reference). This was a clear example of secondary line price discrimination.

Incidentally, the Commission noted that the price discrimination in question could also place the British Post Office (BPO) at a competitive disadvantage against Deutsche Post not in the relevant market but in the UK market for outgoing cross-border letter mail. The additional costs incurred by the BPO as a consequence of the surcharge claimed by Deutsche Post, combined with the frequent disruptions of the mail traffic carried out by Deutsche Post, could indeed induce UK customers to use the service of the latter in the UK for the conveyance of their mail addressed to Germany. Thus, Deutsche Post's control of the mail delivery segment of postal items in Germany could be used to gain a competitive advantage on the market for outgoing cross-border letter mail in the UK by discriminating against the BPO with which it was in competition on that market. Deutsche Post's conduct amounted to secondary line price discrimination on the UK market for outgoing cross-border mail. It also qualifies as an exclusionary abuse as Deutsche Post used its dominant position on the market for the forwarding and delivery of cross-border mail in Germany to extend it to the market for outgoing cross-border mail in the UK.

In 2004, the Commission adopted a decision finding that Clearstream Banking AG and its parent company Clearstream International SA had violated Article 82 EC inter alia by applying discriminatory prices to its customers.[110] This case concerned the provision of clearing and settlement services for securities issued according to German Law. Such services are provided by Central Securities Depositories (CSDs) entities which hold and administer securities and enable securities transactions to be processed. Clearstream AG, a CSD, had a monopoly for the provision of such services for German securities. It was providing clearing and settlement services to other CSDs but also to International Central Securities Depositories (ICSDs).[111] There are two ICSDs in the EU: Euroclear Bank (EB) and Cleastream Banking Luxembourg (CBL), a subsidiary of Clearstream International SA and a sister company to Clearstream Banking AG. The discrimination issue in this case was that, from 1997 to 2002, Clearstream had charged higher fees to Euroclear Bank than to CSDs outside Germany. The Commission established that these fees were discriminatory because the service provided by Clearstream to CSDs and to Euroclear Bank was equivalent, and because there was no objective justification (cost differences) for the difference in fees.

This case is interesting because the discriminatory effects seem to have taken place at two different levels. First, Euroclear Bank was discriminated vis-à-vis CSDs entities with which it is competing on several different markets. This was thus a clear case of secondary line discrimination. At the same time, it seems that the primary rationale for the price discrimination put in place by Clearstream AG was to penalize Euroclear Bank, which was a direct competitor of its sister company CBL on the market for secondary clearing and settlement of securities in cross-border trades. The reason why this

[110] See Commission Decision of 2 June 2004, *Clearstream*, COMP/38.096, not yet published.
[111] ICSDs are organizations whose core business are clearing and settling securities (traditionally Eurobonds) in an international (non-domestic) environment.

discrimination on a second level was possible was that Clearstream AG and CBL were part of the same group. This is where the presence of a degree of vertical integration could be found.

Finally, in the recent *BdKEP* case, the Commission considered that some provisions of the German Postal Law were inducing Deutsche Post AG (DPAG) to engage in price discrimination contrary to Article 82(c).[112] The disputed provisions had the effect of allowing large senders (in general corporations) to feed self-prepared mail directly into sorting centres and enjoy discounts for doing so, while commercial mail preparation firms were denied the right to enjoy similar discounts. The Commission considered that DPAG was applying dissimilar conditions to equivalent transactions because large senders and commercial firms handing over similar volumes of prepared mail at sorting centres (thus leading to the same savings in handling operations and efficiency gains for DPAG) paid different tariffs.

Yet, the secondary line competitive injury resulting from this practice was not manifest because commercial mail preparation firms and large senders were not competing on a relevant market. The Commission considered nonetheless that there was a secondary line injury element in DPAG's conduct. Indeed, the investigation had revealed DPAG had launched two mail preparation services to large senders. It was thus active at the same level as commercial preparation firms.[113] By virtue of the discriminatory discounts conditions, the failure of mail preparation firms to qualify for quantity-based discounts put those firms at a competitive disadvantage vis-à-vis DPAG because they did not have the possibility to procure their clients savings on postage whereas DPAG was able to allow for a consolidation of its clients mail items in order to procure them savings on postage.[114] The discrimination thus additionally constituted an exclusionary abuse because DPAG could extend its dominant position on the market for basic postal services into the market for mail preparation services.

1.2. The choice of article 82(c) as the legal basis for the secondary line injury cases

As far as secondary line injury price discrimination is concerned, Article 82(c) seems to be the appropriate legal basis. Indeed, unlike in the case of primary line discrimination examined in the preceding section, most of these cases do not contain an element of leveraging/extension of a dominant position. They represent clear examples of situations where price discrimination by a supplier distorts competition between its trading parties. However, the cases of secondary line discrimination by non vertically-integrated firms examined above are not "genuine" cases of secondary line discrimination because they all involved an element of discrimination on the ground of nationality. Indeed, in most of these cases the dominant suppliers' conduct must have been motivated by the willingness to favour domestic operators. The practices in question in these cases nonetheless fit well in the concept of secondary line discrimination irrespective of the aims pursued by the

[112] As well as Article 86(1). See Commission Decision of 20 October 2004, COMP/38.745, *BdKEP/Deutsche Post AG and Bundesrepublik Deutschland*, not yet published.
[113] Id at §60.
[114] Id at §94.

dominant firms involved. This is probably why both the Commission and the Community courts have proceeded on the basis of Article 82(c).[115] In addition, it is not sure that the other legal basis provided for by the EC Treaty to condemn discrimination (i.e., Article 12 EC) could have been applied to sanction such practices.

The choice of the proper legal basis for secondary line price discrimination by vertically-integrated firms raises more complex questions. Unlike cases of primary line discriminations, the pricing schemes in question did not aim at excluding rivals operating at the same level of the firm engaging in price discrimination. These cases typically involved a strategy of leveraging by the dominant firm designed to exclude rivals of its downstream (or upstream) operations. For reasons already explained above, Article 82(b) is the proper legal basis for assessing this type of price discrimination.

2. Price discrimination in secondary line injury settings: An economic analysis

The purpose of this section is to provide a brief overview of whether producers have an incentive to practice price discrimination to inflict a competitive disadvantage on certain customers active at the downstream level. Where it seems that there are not clear incentives to discriminate for non vertically-integrated firms (2.1), it appears, on the contrary, that vertically-integrated firms have stronger incentives to price discriminate so as to place its downstream subsidiary's rivals at a competitive disadvantage (2.2).

2.1. Absence of clear economic incentives to discriminate for non-vertically integrated firms

[115] In fact, in many of the cases, the reference to the national discrimination was not mentioned in the review of Article 82(c). This is particularly manifest in the appeal of the Commission's decision in *Portuguese Airports* before the ECJ. The appellant observed that the various measures at stake did not discriminate on the grounds of nationality because they were not dependent on the nationality of the airlines. The Court conceded that Article 82(c) applied to the application of dissimilar conditions to equivalent transactions irrespective of the existence of discrimination on the ground of nationality. See ECJ, *Portuguese Republic v. Commission*, C-163/99, 29 March 2001, ECR [2001] I-2613 at §46. The Court preferred to rely on an objective economic assessment of the forbidden measures. The Court only mentioned in passing that the discount system favoured the national airlines (see §56). As far as the discounts were concerned, it referred to *Michelin* and observed that the mere fact that the system was correlated to the volume of purchases could not lead to the conclusion that there was discrimination. The Court, however, observed that the non linear progression of the discount only allowed two large companies to obtain it and that there was no objective justification for it (the Court did not make any explicit pronouncement as to the value of economies of scale in terms of justification). As far as the differentiation between domestic and international fees were concerned, the Court held that it led to applying dissimilar conditions to equivalent transactions because different tariffs were charged for the same number of landings of similar aircrafts (see §66). A similar approach had been followed by the Court in *Corsica Ferries II*, where the question of the discrimination on the ground of nationality had not been evoked under Article 82c), but with respect to the issue of the freedom to provide services where the Court had held that: "The system gives preferential treatment to vessels permitted to engage in maritime cabotage, in other words, those flying the Italian flag. […] Such a system indirectly discriminates between economic operators according to their nationality, since vessels flying the national flag are generally operated by national economic operators, whereas transport undertakings from other Member States as a rule do not operate ships registered in the State applying that system". ECJ, *Corsica Ferries Italia Srl v. Corpo dei Piloti del Porto di Genova*, 17 May 1994, C-18/93ECR [1994] I-1783 at §§32-33.

The analysis under Part III showed that, under certain circumstances, there is an incentive for firms to discriminate between their customers. This might be, for instance, the case for firms facing fixed-costs recovery problems or producing a range of differentiated products, firms engaging in product versioning, deriving costs savings from discriminating, etc.[116] However, Article 82(c) deals with price discrimination placing trading partners at a competitive disadvantage. The question thus turns on whether rational non vertically-integrated operators have an incentive to price discriminate so as to place one of their trading parties at a competitive disadvantage. This is unlikely to be the case for several reasons. First, upstream firms benefit from a competitive downstream market for distributing their goods. The possibility to grant a competitive price advantage to a distributor may certainly, in the short run, give the latter a strong incentive to distribute the goods efficiently. But in the long run, the insulation of the distributor from competitive pressures may affect its efficiency in distributing the product. Second, an upstream firm granting a competitive price advantage to a purchaser may send a risky signal to the market. Purchasers will be reluctant to order products from the seller in the future, if they face the risk of being discriminated against subsequently. Third, the grant of a competitive advantage may lead to the exclusion of the discriminated purchasers and in turn to increased concentration on the purchasing market. This would increase the countervailing buying power of the seller's downstream distributors and accordingly limits its own market power.

This is not to say, however, that no situation of secondary line injury price discrimination may arise. A first scenario could, for instance, take place in a situation (close to the one envisioned in the *Robinson Patman Act*) where a supplier facing two different kinds of customers according to their purchasing power (e.g., large supermarkets and small retail outlets), would discriminate in favour of the former and, as a result, give them a competitive advantage.[117] This would distort downstream competition as the powerful buyer would end up paying a sub-competitive price on its purchases whereas rival buyers would pay a supra-competitive price for their purchases. In addition, both sub-competitive and supra-competitive prices would lead to lower output than the competitive price. Indeed, the sub-competitive prices will lower output by making sellers less willing to produce for the powerful buyer; the supra-competitive prices will lower output by making rival buyers less willing to purchase the products or services covered. The question whether, as a matter of policy, competition rules should be solicited to sanction the seller for price discrimination calls a negative answer. Indeed, it would be nonsensical as, in a situation of this kind, it is the purchaser, not the seller, that exploits its market power to place its competitors at a competitive disadvantage.[118] The appropriate target for enforcement authorities should thus not be the price discriminator, but the firm benefiting from the price discrimination. So far, Commission and the Community courts have rightly refrained from using Article 82(c) in such settings.

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[116] See A. Cox, supra note 79 at p.105.

[117] A condition for this would be that the buyer enjoys market power downstream. A buyer with market power that wants to gain a competitive advantage downstream may be able to insist on a large discount compared to what the sellers charge other buyers who compete with the powerful buyer downstream.

[118] In a case of this kind, it can be safely assumed that the seller has no market power and takes the price of the big purchaser.

A second scenario where the upstream firm could have an incentive to grant a competitive advantage to a purchaser could appear where the downstream market is composed of purchasers forming a dominant oligopoly that tacitly colludes both upstream (so as to be charged uniform sub-competitive prices for the input) and downstream (charging supra-competitive prices to customers). In this situation, the upstream firm could have an interest in granting a competitive advantage to one of the oligopolists. A reduction of the input price to one of the oligopolists would indeed likely trigger a deviation from the collusive equilibrium downstream and hence induce the necessity for all operators to increase output at the retail level. As output would rise, the orders addressed to the seller would increase. In these cases, again, sanctioning the secondary line price discrimination would be nonsensical, but for different reasons. The price discrimination would most likely result in a rise of output at the retail level and thus enhance consumer welfare by reintroducing price competition downstream.

The two latter scenarios are, however, only likely to occur in very specific circumstances. Thus, it can be safely considered that non vertically-integrated firms would price discriminate to grant a competitive advantage to some buyers at the expense of others only in limited circumstances. This suffices to explain why the case-law contains no illustration of pure secondary line injury price discrimination by non vertically-integrated operators. However, the above analysis only envisioned secondary line price discrimination by non vertically-integrated firms from an economic viewpoint. Non economic considerations may also come into play and explain why the the Commission and the Community courts have rightly condemned secondary line injury price discrimination practices in the cases described at 1.1.1.

2.2. Economic incentives for vertically-integrated firms to price discriminate so as to inflict a competitive disadvantage to their rivals

In contrast to the above situation, vertically-integrated firms have strong incentives to price discriminate in favour of their downstream subsidiaries as such discrimination results in a competitive disadvantage for their subsidiaries' rivals.[119] In addition to the incentive to capture the efficiencies stemming from vertical integration, such firms may also strategically use their control of an essential input to prevent entry or induce the exit of downstream rivals. A monopolist in an input market has a strong incentive to increase the costs of the rivals to its downstream subsidiary as this "softens" downstream competition and increases its profits.[120]

[119] It is assumed here that the downstream rivals of the vertically integrated firm are active in the same product market. As M. Motta observes, in the case of a vertically integrated operator, if the downstream rivals are active in slightly different product markets from the downstream integrated business, supplying them at higher prices would entail foregoing profits because (i) the downstream firm's share remains unchanged and (ii) demand for the output diminishes with a consequent loss of profits. Thus, there would be no incentive to price discriminate in such a setting. See M. Motta, supra note 6 at 373.

[120] See Nicholas Economides, "The Incentive for non-price discrimination by an input monopolist", (1998) 16 *International Journal of Industrial Organization*, 271 at 283. A similar view has been expressed by Thomas Krattenmaker and Steven Salop who explained that a downstream firm may often try to raise its rivals' costs in order to foreclose rivals in asking a bottleneck monopolist to only deal with rivals on

One should not, however, jump too quickly to the conclusion that the incentive to discriminate will inevitably lead to substantial anticompetitive effects and should thus be condemned under competition law. A first reason for not jumping to this conclusion is that economists have shown that anticompetitive effects stemming from price discrimination by vertically-integrated firms are only likely to arise in a narrow set of circumstances. Foreclosure or exclusion are unlikely to arise if there are other substitutes inputs on the markets or low barriers to entry at the upstream level.[121] Indeed, in the presence of alternatives, the upstream firm would prefer to supply the downstream rivals itself rather than letting them be supplied by an upstream competitor or engage into a strategy of vertical integration. A careful assessment of the market power of the input firm upstream and of the barriers to entry should be conducted prior to condemning such forms of price discrimination.

In addition, the assessment of the anti-competitive effect of price discrimination favouring a dominant firm's downstream subsidiary critically rests on the proportion of the input cost within the overall total cost of actual or potential downstream competitors.[122] The case-law of the ECJ seems to take this element into account. For instance, in *Alpha Flight/Aéroport de Paris* (a case that does not, however, concern a vertically-integrated firm scenario), the Commission insisted on the fact that the discriminatory commercial fee was an important part of a suppliers' cost structure.[123]

Finally, it is necessary to assess *ex hypothesi* if, in case of successful foreclosure, the discriminating vertically-integrated firm would have the possibility to raise prices at the retail level. Indeed, if that was not the case, it would be doubtful that the price discrimination carried out was actually seeking to strategically drive its subsidiary's competitors out of business. In addition to its inability to raise prices downstream, the vertically-integrated firm would lose the source of revenues that was generated by the selling of inputs to downstream rivals. Other reasons could in contrast be found to justify the discrimination, such as, for instance, the efficiencies stemming from vertical integration.

A second economic reason why enforcement authorities should be cautious when enforcing Article 82(c) EC against vertically-integrated firms engaging in discriminatory pricing is that, from a policy standpoint, a number of adverse effects on firms' efficiency could arise from a strict prohibition of price discrimination in favour of one's own subsidiary. This could indeed lead to several kinds of Type I errors. First, forbidding price discrimination in favour of one's subsidiary may incidentally discourage firms from vertically-integrating their operations even when such integration could generate substantial efficiencies (limitation of transaction costs, prevention of double monopoly

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discriminatory terms (i.e. a practice referred to as the bottleneck method). This was the situation at stake in the famous *Terminal Railroad* case in the US. See Thomas G. Krattenmaker and Steven C. Salop, "Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price", (1986) 2 *Yale Law Journal*, 209 at 235.

[121] See, on this, M. Motta, supra note 6 at 341.

[122] See T. Krattenmaker and S. Salop, supra note 120 at 259.

[123] See Commission Decision, supra note 100 at §109.

pricing, etc.). Second, mandatory uniform pricing (combined with a duty to deal with the downstream operators) may, lead to harmonized access conditions for operators on the downstream market. This is certainly problematic in oligopolistic market structures as the symmetry of costs between operators is often cited as a critical factor for the likelihood of a collusive outcome.[124] Of course, the risk that harmonized access conditions limit the scope for price competition on downstream markets depends on the fraction represented by access costs within average total costs.[125] From an abstract perspective, it is impossible to determine whether the risk is high or low. But neither the Commission nor the Community courts seem so far to have paid attention to this question.[126] Third, absent any injunction regarding the methodology to be used to calculate the input price (LRIC, retail-minus, etc.), a requirement of uniform pricing imposed on a vertically-integrated operator may leave it with the choice of taking its profits upstream rather than downstream and set the uniform price for the input at the monopoly level for both its subsidiary and the latter's rivals. In such a scenario, competition authorities could initiate proceedings for abusive pricing. As is, however, well known, such authorities are generally not keen on launching such proceedings if only because of the difficulty to determine when a price is excessive.

Interestingly, the Commission and the Community courts have, so far, refrained from harshly sanctioning secondary line price discrimination by vertically-integrated firms. The examples in *Deutsche Bahn* and *BdKEP* showed that the Commission has only initiated actions on the basis of Article 82(c) in situations of blatant discrimination where the holder of a bottleneck was without any doubt trying to extend its dominant position into the downstream market and exclude its competitors.

C. Geographic price discrimination and measures facilitating this form of discrimination

In this section, we discuss geographic price discrimination schemes, as well as measures to facilitate such schemes. The case law of the Community courts and the decisional practice of the Commission are first analysed (1). The economics of geographic price discrimination and facilitating measures are then discussed (2).

1. Geographic price discrimination and facilitating measures: A legal analysis

The case law of the Community courts gives a number of illustrations where Article 82(c) has been used to sanction dominant firms engaged in geographic price discrimination (1.1). It is, however, doubtful that Article 82(c) was the appropriate legal basis for situations of this kind (1.2).

[124] See Commission Guidelines on the Assessment of Horizontal Mergers under the Council Regulation on the Control of Concentrations between Undertakings, OJ C 31 of 5 February 2004, pp.5-18 at §.48.
[125] This is likely to be a minimal concern where access costs are a limited share of the average total costs.
[126] In stark contrast with the US Supreme Court, this again recently mentioned these collusive risks in Trinko. See *Verizon Communications, Inc. v. Law Offices of Curtis Trinko*, LLP, 13 January 2004, 540 U.S.

1.1. Case law of the EC Courts and Commission decisions on geographic price discrimination

The leading case on geographic price discrimination is *United Brands*.[127] United Brands Company (UBC) unloaded at Rotterdam and Bremen ports bananas of a similar quality with identical unloading costs and then sold these bananas to customers (distributors/ripeners) from various Member States at significantly different prices. Customers were delivered the bananas at one of the ports of unloading and carried them to their own ripening rooms in their own Member States. UBC's general sales conditions incorporated a clause which had the effect of preventing parallel imports from one Member State to another by prohibiting the exports of green, unripened bananas. In its decision, the Commission considered that both the practice of differentiating prices according to the Member State of the customers and the clause seeking to prevent parallel imports amounted to abuses of a dominant position.

In its judgment, the ECJ upheld the decision of the Commission on both points. As far as the clause preventing arbitrage was concerned, the ECJ found that:

> "[T]he prohibition on resale imposed upon duly appointed Chiquita ripeners and the prohibition of the resale of unbranded bananas [...] where without any doubt an abuse of the dominant position since they limit markets to the prejudice of consumers and affect trade between Member States, in particular by partitioning national markets.
> Thus UBC's organization of the market confined the ripeners to the role of suppliers of the local market and prevented them from developing their capacity to trade vis-a-vis UBC, which moreover tightened its economic hold on them by supplying less goods than they ordered."[128]

The language used in the above quoted passage seems to suggest that the clause in question was considered abusive because: (i) it had the effect of partitioning national markets and (ii) prevented distributors/ripeners from developing an activity of cross-border traders in bananas.

As far as the imposition of different prices was concerned, the ECJ relying expressly on the language of Article 82(c) found that:

> "These discriminatory prices, which varied according to the circumstances of the Member States, were just so many obstacles to the free movement of goods and their effect was intensified by the clause forbidding the resale of bananas while still green and by reducing the deliveries of the quantities ordered.
> A rigid partitioning of national markets was thus created at price levels, which were artificially different, placing certain distributor/ripeners at a competitive disadvantage, since compared with what it should have been competition had thereby been distorted.
> Consequently the policy of differing prices enabling UBC to apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage, was an abuse of a dominant position."

[127] See ECJ, *United Brands Company v. Commission*, supra note 14.
[128] Id. at §159.

The analysis of the ECJ in the above passage postulates that the partitioning of national markets placed distributors/ripeners at a competitive disadvantage, one of the conditions required for a measure to fall under Article 82(c). In fact, the opposite is true. Price discrimination between different distributors/ripeners could have placed some of them at a competitive disadvantage on the cross-border market for the resale of bananas, thereby creating a secondary line injury. By contrast, once the markets were partitioned across national lines, different prices could no longer create a competitive disadvantage among ripeners/distributors since these traders could not compete with each other.

A similar practice of geographic price discrimination was held to be an abuse of a dominant position in *Tetra Pak II*.[129] In that case, Tetra Pak, the dominant undertaking in aseptic machines and cartons intended for the packaging of liquid foods, was charging considerably different prices for cartons and machines across Member States. Prices were considerably lower in Italy than in other Member States.[130] The fact that these disparities remained between Member States while the analysis had shown that the relevant geographical market was the Community as a whole and that the transport costs were fairly limited suggested that the differences in price could not be attributed to objective market conditions.[131] Both the Commission and the CFI thus estimated that these differences in pricing were the result of an overall market partitioning strategy pursued by the dominant operator.[132] The Commission and the CFI concluded that Article 82(c) had been infringed.[133]

The application of Article 82(c) in this case was problematic for the following reasons. First, the Commission and the Court failed to analyse whether Tetra Pak's trading parties were placed at a competitive disadvantage. Second, the fact that the Commission decision and the CFI judgment condemned as abuses of a dominant position a large number of contractual clauses through which Tetra Pak had compartimentalized markets should have sufficed to bring the geographic price differentials to an end.[134] There was thus no need to condemn geographic price discrimination as a distinct abuse.

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[129] See CFI, *Tetra Pak International SA v. Commission*, 6 October 1994, T-83/91 ECR [1994] II-755 and Commission Decision 92/163 of 24 July 1991 *Tetra Pak II*, OJ L 72 of 18 March 1992 pp.1-68. There were also a number of discrimination elements in the case which were not concerned with geographic price discrimination, but which related to price discrimination, within the Italian market, between users. See §158, 160, 161, 62-68 of the Decision.

[130] See Commission Decision supra note 129 at §52. Tetra Pak was indeed facing fierce competition from Elopak in Italy.

[131] See CFI, supra note 129 at §170 and Commission Decision, supra note 129 at §160

[132] See CFI supra note 129 at §171 and Commission supra note 129 at §160

[133] See CFI supra note 129 at §173.

[134] Two clauses in the contract limited the purchaser's right to resell or transfer the equipment to third parties: A first clause (referred to as clause xv) provided "the purchaser is required to obtain Tetra Pak's agreement before selling or transferring the use of the equipment (Italy), resale is subject to conditions (Spain), and Tetra Pak reserves the right to repurchase the equipment at a pre-arranged fixed price (all countries); failure to comply with this clause may give rise to a specific penalty (Greece, Ireland, United Kingdom)". A second clause (referred to as clause xvi) provided: "the purchaser must ensure that any third

A distinct, though related, pattern of price discrimination arose in two other cases In *British Leyland*, the Commission and the ECJ sanctioned a discriminatory pricing practice that sought to insulate the UK market for the selling of *Metro* cars from import competition.[135] In the UK, a person seeking to register a vehicle for usage on the roads had, unless he was importing the vehicle for personal use, to produce a certificate of conformity certifying that the vehicle conformed to a previously approved type vehicle. UK legislation gave British Leyland a monopoly on the market for issuing the certificates for imported British Leyland vehicles. British Leyland marketed its vehicles in Great Britain through a selective distribution network. However, a stream of re-imports from Metro cars took place from Belgium, as a result of the differences between the prices charged by British Leyland in the UK for right hand drive vehicles, and in the EC for left hand drive vehicles. This was made possible because conversion of left hand drive to right hand drive vehicles was fairly easy. In order to protect its domestic distributors, British Leyland tried to impose higher fees for the grant of certificates of conformity for imported left hand drive vehicles than for certificates of identical right hand drive vehicles (for which there were almost no exports/re-imports except for diplomatic or military personnel). The Commission found this difference of treatment discriminatory and held it to be an abuse of a dominant position.[136] In this case, the Commission was obviously concerned by the fact that the practice in question amounted "to a penalty on parallel trade" and "impeded [...] the free movement of goods and economic interpenetration which the EC Treaty aims to encourage".[137]

Similarly, in *Irish Sugar*, the Commission and the Court condemned the discriminatory "border rebates" granted by Irish Sugar to customers located close to the Northern Ireland border. The Commission mentioned in passing that the rebate was placing those who did not qualify for it at a competitive disadvantage. In contrast, the Commission focused on the fact that the rebate was intended to deter imports from Irish Sugar's competitors as

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party to whom he resells the equipment assumes all his obligations (Italy, Spain)". In its decision the Commission held that "The requirement that the purchaser obtain Tetra Pak's agreement before he can exercise his right to dispose of an asset in his property or even to transfer its use (Italy) not only has no connection with the purpose of the previously signed sales contract but also, in view of the effect it has on the very essence of the right of ownership, constitutes an unfair condition of the transaction. [...] These conditions prohibit export of the machine and forbid third parties which are potential purchasers from being offered conditions of resale which are more favourable than those which apply to Tetra Pak. Such conditions directly affect trade between the Member States and again limit the purchaser's outlets [...] Tetra Pak's automatic right of pre-emption must in itself be considered to constitute an abuse in so far as it again unduly limits the ability of the user, who does after all own the machine, to dispose of his asset as he wishes, and constitutes one of the instruments by which Tetra Pak is able to compartmentalize national markets [...]. Requirement to ensure that any third party purchasing equipment assume the obligations of the initial purchaser. Resale was made difficult because obliges the initial purchaser to ensure that the third party accepts a series of obligations which themselves constitute abuse". See Commission Decision, supra note 129 at §§123-128.

[135] See Commission Decision 84/379 of 2 July 1984, *BL*, OJ L 207 of 2 August 1984 pp.11-16. Confirmed implicitly by the ECJ on appeal, 226/84, *British Leyland plc v. Commission*, 11 November 1986, ECR [1986]-3263.

[136] See Commission Decision, supra note 135 at §26.

[137] See Commission Decision, supra note 135 at §29.

part of a policy of dividing markets and excluding competitors.[138] The CFI confirmed the finding of discrimination of the Commission and insisted on the fact that the practice ran contrary to the "essence of a common market" in that it created an obstacle to the achievement of [the] common market" and therefore constituted an abuse.[139]

In these last two cases, unlike in *United Brands* and *Tetra Pak II,* Article 82(c) did not strictly apply to geographic price discrimination. Rather these cases concerned practices taking the form of price discrimination (not necessarily geographically, e.g. *British Leyland*) which helped ensure that a given geographic market remained shielded from imports from other Member States. Of course, these practices may have contributed indirectly to the maintenance of different prices across different territories. But this effect was indirect and did not constitute the core target of the Article 82's infringement findings.

1.2. Is Article 82(c) the appropriate legal basis for geographic price discrimination and facilitating measures?

United Brands and *Tetra Pak II* cases are mistakenly based on Article 82(c). The conditions of Article 82(c) and, in particular, the condition that customers be placed at a competitive disadvantage did not appear to be fulfilled, precisely because the customers in question operated on different geographic markets and thus were not competing with each other. More generally, condemning outright geographic price discrimination runs contrary to the central goal of attaining a common market. The existence of price differentials among Member States is indeed the main driver for the emergence of patterns of parallel trade within the Community, which in turn ensures that prices across Member States converge towards the lower prices. Thus, provided resale is possible and profitable, the market mechanisms should be sufficient to approximate prices differences. Competition policy should thus not be concerned with the existence of price differentials, but rather seek to ensure that outside competition from parallel trade is not impeded by firms' practices maintaining artificial obstacles to trade.

Under EC competition law, a number of provisions can be used to ensure that firms do not artificially try to restrict trade between Member States. First, Article 81 EC has been applied on various occasions to practices seeking to prevent parallel trade. Often, a producer will try to induce its distributors not to resale the products in question so as to partition geographic markets and price discriminate along geographic lines. This is acknowledged in the Guidelines on Vertical Restraints which underline the anticompetitive effect of:

> "[...] territorial resale restrictions, the allocation of an area of primary responsibility, restrictions on the location of a distributor and customer resale restrictions. The main negative effect on competition is a reduction of intra-brand competition that may help the

[138] See Commission Decision, supra note 30 at §129.

[139] See CFI, supra note 54 at §183. In addition, the export rebates (granted to Irish Sugar's customers exporting sugar in processed form to other Member states) seemed designed to make sure that its customers contemplating sourcing to foreign suppliers would no switch to the latter in order to obtain supplies. See CFI at §139.

supplier to partition the market and thus hinder market integration. This may facilitate price discrimination."[140]

The Guidelines also evoke the facilitating effect of exclusive distribution agreements[141] as well as exclusive customer allocation agreements on price discrimination.[142]

Similarly, the Guidelines on the application of Article 81 EC to technology transfer agreements underline the risks of price discrimination stemming from captive use restrictions (i.e. obligations on a licensee to limit his production of the licensed product to the quantities required for the production of his own products, thus preventing resale)[143] and of quantity limitations aimed at partitioning markets.[144]

Besides the regulatory framework in place, the Commission and the EC Courts have often sanctioned concerted practices between producers and their distributors with a view to restricting parallel trade on the basis of Article 81 EC.[145] However, as the *Bayer* ruling showed, it may not be possible to apply Article 81 EC to measures restricting parallel trade when there is no agreement between a supplier and its retailers (i.e., when there is

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[140] See Commission Notice - Guidelines on Vertical Restraints, OJ C 291 of 13 October 2000, pp.1-44 at §114 that concerns market partitioning groups i.e. agreements whose main element is that the buyer is restricted in where he either sources or resells a particular product.

[141] Id at §161: "In an exclusive distribution agreement the supplier agrees to sell his products only to one distributor for resale in a particular territory. At the same time the distributor is usually limited in his active selling into other exclusively allocated territories. The possible competition risks are mainly reduced intra-brand competition and market partitioning, which may in particular facilitate price discrimination". Id at §172: "The combination of exclusive distribution with exclusive purchasing increases the possible competition risks of reduced intra-brand competition and market partitioning which may in particular facilitate price discrimination".

[142] See §178: "In an exclusive customer allocation agreement, the supplier agrees to sell his products only to one distributor for resale to a particular class of customers. At the same time, the distributor is usually limited in his active selling to other exclusively allocated classes of customers. The possible competition risks are mainly reduced intra-brand competition and market partitioning, which may in particular facilitate price discrimination".

[143] See Commission Notice - Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements, OJ C 101 of 27 April 2004, pp.2-42 at §188: "[...] there are two main competitive risks stemming from captive use restrictions: (a) a restriction of intra-technology competition on the market for the supply of inputs and (b) an exclusion of arbitrage between licensees enhancing the possibility for the licensor to impose discriminatory royalties on licensees. See also §186 which explains what a captive use restriction is: "In other words, this type of use restriction takes the form of an obligation on the licensee to use the products incorporating the licensed technology only as an input for incorporation into his own production; it does not cover the sale of the licensed product for incorporation into the products of other producers".

[144] Id. at §98: "quantity limitations are used to implement an underlying market partitioning agreement. Indications thereof include the adjustment of quantities over time to cover only local demand, the combination of quantity limitations and an obligation to sell minimum quantities in the territory".

[145] See e.g., Commission Decision of 20 September 2000, *Opel Nederland BV/General Motors Nederland BV*, OJ L 59, 28 February 2001, pp.1-42 and CFI, T-368/00, 21 October 2003, *General Motors Nederland and Opel Nederland v. Commission*, ECR [2003] II-4491 (partial annulment); CFI, T-62/98, 6 July 2000, *Volkswagen v. Commission*, ECR [2000] II-2707.

no "meeting of minds" or where the supplier is vertically integrated and operates himself the distribution of the products).[146]

If the supplier holds a dominant position, conduct aimed at hindering parallel imports can, however, fall within Article 82 EC.[147] As was the case in *Tetra Pak II*, such conduct may infringe Article 82(a) EC since it implies the application of unfair trading conditions to retailers. It may also fall under Article 82(b) when the dominant firm refuses to supply retailers to ensure that markets remained geographically compartmentalised.[148] As in *British Leyland* and *Irish Sugar*, Article 82(c) has also been applied to practices intended to limit trade flows between Member States to maintain price differentiation along geographic lines.

Absent measures aimed at facilitating price discrimination, the existence of price differences among different geographic markets suggests that (for reasons that will be explained in the following section) the conditions of competition in different areas are not homogeneous and that there are several distinct relevant geographic markets.[149] In such a situation, the reliance on Article 82(c) to condemn geographic price discrimination - in addition to making no sense on policy grounds - does not seem to be legally possible since Article 82(c) should only apply to differential pricing practices within one and the same market. The existence of different prices on different geographic markets should thus not be subject to challenge under Article 82(c). This does not mean, however, that the pricing policy of a dominant firm would be completely left unchecked. Indeed, there could be a case for intervention on the basis of Article 82(a) if the prices are excessive in certain markets.[150]

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[146] See CFI, *Bayer AG v. Commission*, 26 October 2000, T-41/96ECR 2000 II-3383 at §71; ECJ, *Bundesverband der Arzneimittel-Importeure eV and Commission v. Bayer AG*, 6 January 2004, C-2/01 P and C-3/01 P, ECR [2004] I-23 at §§101and 141. The ruling of the CFI in *Micro Leader Business* seems also to support this view. See CFI, *Micro Leader Business v. Commission*, 16 December 1999, T-198/98, ECR [1999] II-3989 at §56.

[147] See CFI, *Bayer AG v. Commission*, supra note 146 at §176.

[148] ECJ, *Syfait and Others v. GlaxoSmithKline plc*, 31 May 2005, C-53/03, not yet published. Note in addition that a gap in the EC competition system exists where, as the CFI held in *Bayer*, a supplier restricts parallel trade "without abusing a dominant position, and there is no concurrence of wills between him". This can, for instance arise if the supplier is vertically integrated and does not enjoy a dominant position on the market. The Court seems to recognise that, in such situation, "a manufacturer may adopt the supply policy which he considers necessary, even if, by the very nature of its aim, for example, to hinder parallel imports, the implementation of that policy may entail restrictions on competition and affect trade between Member States". See CFI, *Bayer AG v. Commission*, supra note 146 at §176. But this question falls outside the scope of this article which is only concerned with the scope of the liability imposed by Article 82 EC on dominant firms.

[149] As implicitly confirmed in the Commission Notice on the definition of the relevant market for the purposes of Community competition law, OJ C 372 of 9 December 1997, and more explicitly by the Commission in its market definition practice. See, e.g., Commission Decision 92/553 of 22 July 1992, *Nestlé/Perrier*, OJ L 356 of 5 December 1992 pp.1-31.

[150] In that respect, the Court held in *Bodson* that price differences in different locations may provide a basis for assessing whether or not the prices charged are excessive pursuant to Article 82(a). See ECJ, *Corinne Bodson v. SA Pompes funèbres des régions libérées*, 4 May 1988, 30/87, ECR [1988]-2479.

2. Geographic price discrimination and facilitating measures: An economic analysis

The economics of geographic price discrimination and of the measures facilitating geographic price discrimination are quite straightforward. It is indeed widely admitted that sanctioning the application of different prices to distinct markets does not make sense. This is the case for several reasons. First, geographic price discrimination does in fact stimulate free trade and promotes market integration. It is therefore odd that both the ECJ and the CFI forbade price discrimination on face value in *United Brands* and *Tetra Pak II*. In particular, the statement by the ECJ in *United Brands* that the "discriminatory prices, which varied according to the circumstances of the Member States, were just so many obstacles to the free movement of goods" defies economic logic. If the prices of bananas happened to be similar in all Member States, there would not be any trade in bananas across national borders. The only measure that was likely to partition market across national lines was the clause which prevented ripeners/distributors from reselling unripened bananas.[151] This is what the ECJ seems to have acknowledged by stating that the effect of the discriminatory prices "was intensified by the clause forbidding the resale of bananas while still green". Since this clause was, however, already banned in another part of its judgment, prohibiting price discrimination as a separate infraction was neither desirable, nor necessary.[152]

Second, basic economics show that a ban on geographic price discrimination can lead to undesirable distributive consequences.[153] Indeed, when an operator sells a product or service at different prices depending on the conditions of demand in the different countries, an obligation to adopt a uniform price will generally have adverse distributive consequences in the countries where prices were low. Indeed, the uniform price will certainly be higher than what the consumers of these would have been charged in the absence of this obligation. Mandatory uniform pricing will thus trigger a transfer of wealth from the (generally poor) consumers of the low price countries to the consumers (generally rich) of the high price ones. Worse even, the firm in question may simply decide no longer to serve the consumers of the low price countries and focus on those from the high price countries.

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[151] As well as the clauses preventing resale of Tetra Pak's machines in *Tetra Pak II*.

[152] Another passage of the ECJ's judgment was quite problematic. Indeed, while the ECJ acknowledged that "differences in transport costs, taxation, customs duties, the wages of the labour force, the conditions of marketing, the differences in the parity of currencies, the density of competition may eventually culminate in different retail selling price levels according to the Member States", it also stated that those differences were factors which UBC could only take into account to a limited extent since it was selling an identical product at an identical place to ripeners/distributors who alone "bear the risks of the consumers' market" (see ECJ, *United Brands Company v. Commission*, supra note 14 at §228). This part of the decision was not only criticized for the fact that it was not true that only ripeners/distributors bore the risks of the market, but also because it created incentives to operators, such as UBC to vertically integrate production and retailing functions. Indeed, the Court judgment led to the odd situation that while operators which combined production and retailing functions could take demand considerations to differentiate prices, a non vertically-integrated operator, such as UBC, could not do so.

[153] See William Bishop, "Price Discrimination under Article 86: Political Economy in the European Court", (1981) 44, *Modern Law Review*, 282, at pp.288-289.

The only issue of concern for enforcement authorities should be to prevent measures impeding resale. For geographic price discrimination to stimulate market integration, it is necessary that customers be able to resell the goods among each others.[154] Dominant companies may, however, be interested in preventing "arbitrage" in order to maintain different prices in different geographic areas. These practices, which artificially distort patterns of trade should be challenged on the basis of competition rules. In that respect, the case law of the EC Courts and the decisional practice of the Commission appear to be in line with economic theory. In both *United Brands* and *Tetra Pak II*, clauses preventing resale were held to be abuses of a dominant position.

For these reasons, we consider that the Commission should no longer sanction geographic price discrimination as such. Differences in prices across Member States should generally be welcome as they stimulate flows of goods across Member States. When price differences subsist within a relevant geographic (an area where the competitive conditions and prices should in theory be homogeneous), an inquiry might be needed to verify whether such differences result from private obstacles to trade (such as contractual clauses preventing resale). Competition authorities and competition law should not be concerned with public obstacles to trade (such as discriminatory legislation), which should be dealt with under the free movement of goods provisions of the EC Treaty. When private obstacles to trade can be identified, a prohibition rule is probably justified.[155]

VI. Conclusion

Price discrimination involves many different practices relied upon by firms in dominant, as well as non-dominant, positions. In this paper, we argue that the only competition law provision of the EC Treaty specifically dealing with (price) discrimination in the context of dominance, i.e. Article 82(c), has been applied to a range of situations that have little to do with its specific purpose of preventing secondary line injury price discrimination. The application of Article 82(c) to practices, including rebates, selective price cuts, tied and bundled prices, discriminatory pricing of inputs by vertically-integrated operators, and geographic price discrimination, is an unwelcome development. The progressive extension of the scope of Article 82(c) can be explained by a variety of reasons, such as the relatively low evidentiary threshold required by this provision as interpreted by the ECJ compared to Article 82(b), the fact that price discrimination can be observed in most forms of pricing abuses, etc. This extension is not without consequences since it has allowed the Commission to condemn under Article 82(c) pricing practices allegedly designed to exclude competitors by simply showing the presence of some form of vaguely defined price discrimination. In this paper, we show that Article 82(c) should be limited to a narrow set of circumstances where price discrimination practices engaged in

[154] See M. Motta, supra note 6 at p.492.

[155] EC Competition law forbids, in that respect, restriction to passive sales. It does not, however, prohibit restrictions to active sales inserted within exclusive distribution agreements. See §§49 and 50 of the Guidelines on Vertical Restraints, supra note 140.

by non vertically-integrated firms place the dominant firm's customers at a competitive disadvantage vis-à-vis other customers.

In addition to selecting the wrong legal basis, the Commission and the Community courts have generally taken an over-restrictive stance to price discrimination. The excessive severity of the case-law can, for instance, be found with respect to rebates, which have been deemed illegal except in the limited circumstances where they could be justified by cost savings. This approach largely ignores the various pro-competitive effects that can be generated by rebates, as well as the need for firms facing declining average total costs to use rebates to efficiently recover their fixed costs. A more cautious approach, based on the examination of the effects of price discrimination schemes, is thus warranted. In other circumstances, the Commission and the Community courts have relied on Article 82(c) to condemn geographic price discrimination. Condemning this form of price discrimination on the ground that it would impede the creation of a common market makes no sense. The focus of the competition law enquiry should be on the measures seeking to prevent resale. Although such measures have in some cases been condemned on the basis of Article 82(c), other legal bases would have generally been more appropriate.

<table>
<tr><th colspan="3">PRIMARY LINE INJURY ABUSES</th><th colspan="2">SECONDARY LINE INJURY ABUSES</th><th colspan="2">GEOGRAPHIC PRICE DISCRIMINATION AND FACILITATING MEASURES</th></tr>
<tr><td rowspan="3">Rebates</td><td>Loyalty/ Fidelity Rebates</td><td>Suiker Unie
Hoffman- La Roche
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<tr><td>Target Rebates</td><td>Michelin I
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<tr><td>Tying and Bundling</td><td colspan="2">Digital
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Compagnie Maritime Belge</td></tr>
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Foreclosure/Leverage/Extension of a Dominant Position Abuses