Tomra: Exclusive Dealing and Rebates in the Light (and Shadows) of Dominance

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Case T-155/06, Tomra Systems ASA and Others v. European Commission

The General Court reaffirms its traditional form-based approach to dominance (author's headnote).

I. Facts

This case deals with an Application for annulment of the 2006 Commission Decision on the *Prokent-Tomra* case relating to proceedings under Article 102 of the Treaty of the Functioning of the European union [TFEU] and Article 54 of the EEA Agreement ('the contested decision').[1]

The applicants are the parent company of the Tomra group, Tomra Systems ASA, together with Tomra Europe AS, coordinator of the European activities of the Group, and five of its national distribution subsidiaries[2] (henceforth, 'Tomra'). Tomra manufactures different types of Reverse Vending Machines ('RVMs') used for the collection of used beverage containers and provides RVM-related services throughout the world.

The contested decision was adopted following an investigation initiated after *Prokent*, a German competitor which Tomra had failed to take over, denounced the practices carried out by the incumbent had driven it out of the market. The Commission found that Tomra had abused its dominant position from 1998–2002 by implementing an exclusionary strategy through the conclusion of 49 agreements with a number of supermarket chains that involved exclusivity agreements, individualised quantity commitments and individualised retroactive rebate schemes. The starting point of the period of the abuse coincided with the critical years when the relevant market (widely defined in favour of the applicant as including both high- and low-end RVMs) had taken off in the five countries at issue in anticipation of the implementation of national rules concerning the collection of used beverage containers. As a result of this connection with national legislation, the relevant geographical markets were identified as the five Member States where Tomra was active. The dominance of Tomra was supported not only by high market shares (consistently above 95 % after 1997), but also by the very weak position of potential competitors, the aggressive response given by the incumbent to new entrants, including the take-over of two competing companies, as well as the lack of countervailing buyer power. Moreover, the importance of intellectual property rights in the RVMs industry gave Tomra a clear advantage and represented an entry barrier for competitors.

The Commission performed an effect-based analysis of Tomra's conduct and concluded that, given its dominant position in the market, the exclusivity clauses applying to a substantial part of the demand had a market-distorting foreclosure effect. Additionally, the individualised quantity discounts and retroactive loyalty rebates[3] established on the basis of each customer's demand and designed to create a powerful inducement to purchase all, or almost all, of their requirements from Tomra had the same effects as the explicit exclusivity clauses. In the absence of cost efficiencies capable of justifying these anticompetitive effects or an apparent benefit for consumers,

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1 Case COMP/E-1/38.113–Prokent-Tomra [2006] OJ 734.

2 Tomra Systems GmbH in Germany, Tomra Systems BV in the Netherlands, Tomra Leergutsysteme GmbH in Austria, Tomra Systems AB in Sweden and Tomra Butikksystemer AS in Norway.

3 "Guidance on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings", Official Journal C 045, 24/02/2009, pp. 7–20, available on the Internet at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52009XC0224%2801%29:EN:NOT> (last accessed on 17 December 2010), the 'Guidance Paper', at para. 36. Retroactive loyalty rebates are applied to all purchases realised during a given period once the customer reaches the agreed-upon threshold; as opposed to incremental loyalty rebates where the discount is only applied to the units purchased beyond the threshold.

the contested decision established a fine against the applicants for an amount of EUR 24 million.

II. Judgment

The General Court upheld the contested decision and dismissed the claims put forward by Tomra.

The applicants had contended that the Commission was wrong when it had qualified the contracts at issue as 'exclusive', because, apart from being non-binding, they only gave Tomra the status of 'primary, main or preferred' supplier while allowing customers to test and buy competitors' machines if proven to be of a superior quality. The Court recalled that "there is no need for the practices of a dominant undertaking to tie purchasers by a formal undertaking in order for it to be found that those practices amount to an abuse of a dominant position within the meaning of Article [102 TFEU]. It is enough that those practices give customers an incentive not to turn to competing suppliers and to obtain all or most of their requirements exclusively from the undertaking concerned".[4]

Moreover, the applicants alleged that the thresholds attached to their discount schemes were not 'individualised' and targeted at capturing all (or almost all) of their customers' requirements. Not only did they lack capacity to estimate future demand accurately, but also ex-post analysis showed that in most cases "actual purchases were either significantly below or significantly above the alleged quantity commitments, while the customer also purchased RVMs from the applicants' competitors".[5] The Court found that the contested decision was correct, as the systematic correlation between purchases and thresholds did not need to correspond precisely with total actual demand as observed *ex-post facto.* The study showed that actual purchasing volumes were in most cases 'slightly above' the thresholds[6] and, even if in some cases the "the Commission did not prove that the agreement was individualised, it cannot be denied that what is at issue is an agreement for a progressive and retroactive rebate."[7]

However, the applicants contested the very notion that these practices were unlawful per se under Article [102 TFEU].[8] They opposed the idea that a mere formal analysis is enough to establish an abuse in the framework of dominance, and considered that the Commission had failed to explain the reasons why the agreements in question were capable of foreclosing competitors form the relevant market.[9] The Court referred to *Hoffman-La Roche* to point out that "an undertaking which is in a dominant position on a market and ties purchasers by an obligation or promise on their part to obtain all or most of their requirements exclusively from that undertaking abuses its dominant position within the meaning of Article [102 TFEU], whether the obligation in question is stipulated without further qualification or whether it is undertaken in consideration of the grant of a rebate."[10] However, this does not preclude the necessity "to ascertain whether, following an assessment of all the circumstances and, thus, also of the context in which those agreements operate, those practices are intended to restrict or foreclose competition on the relevant market or are capable of doing so."[11] In this respect, the Court stressed that "even though the case-law does not require it", the Commission did carry out an analysis of the actual effects of Tomra's practices in the light of the specific market conditions.[12] Moreover, established case-law demands that a decision adopted pursuant to Article [102 TFEU] shall "mention facts forming the basis of the legal grounds of the measure and the considerations which led to the adoption of the decision."[13] To this end, the Commission "gave a detailed explanation of the reasons which led it to believe that the agreements in question were capable of restricting or excluding competition."[14]

The applicants added that even if the Commission had shown the foreclosure effects of all contracts at issue, these would only have affected the parties to these agreements. Nothing prevented competitors from targeting other customers than those involved with Tomra. In this sense, the Commission would have failed to establish that the locked share of the demand was large enough to foreclose competition in

4 Case T-155/06, *Tomra Systems ASA and Others v. European Commission* [2010], at para. 59 citing Case 85/76 *Hoffmann-La Roche v. Commission* [1979] ECR 461, at paras. 89–90 and at para. 97.

5 Case T-155/06, Tomra Systems ASA and Others v. European Commission, paras. 68 and 73.

6 *Ibid.*, at paras. 84–86.

7 *Ibid.*, at para. 101.

8 *Ibid.*, at para. 198.

9 *Ibid.*, at para. 204.

10 *Ibid.*, at para. 208.

11 *Ibid.*, at para. 215.

12 *Ibid.*, at para. 219.

13 *Ibid.*, at para. 227.

14 *Ibid.*, at para. 228.

the market as a whole.[15] Although the Court acknowledged that the contested decision had not established "a precise threshold beyond which the applicants' practices would be capable of excluding competitors"[16], "foreclosure by a dominant undertaking of a substantial part of the market cannot be justified by showing that the contestable part of the market is still sufficient to accommodate a limited number of competitors (...) competitors should be able to compete on the merits for the entire market and not just for a part of it."[17] Rather than an ex-ante assumption of the minimum viable contestable share, all the circumstances of the case have to be taken into account. To this extent, a high 'tied demand' of end customers in the key years of market growth constituted particularly harmful circumstances.[18]

The Court considered ineffective the claim that the Commission had erroneously calculated as negative the price that other competitors would have to offer to capture even a small share of the demand in order to offset the loss of the retroactive rebate. These acknowledged errors could not undermine the anticompetitive nature of Tomra's practices, as "the exclusionary mechanism represented by retroactive rebates does not require the dominant undertaking to sacrifice profits, since the cost of the rebate is spread across a large number of units. If retroactive rebates are given, the average price obtained by the dominant undertaking may well be far above cost and ensure a high average profit margin. However, retroactive rebate schemes ensure that, from the point of view of the customer, the effective price for the last units is very low because of the 'suction effect'."[19] Due to the incumbent's status as 'unavoidable trade partner', "customers turned to alternative suppliers only for a limited portion of their purchases"[20]. Thus, unlike alleged by the applicants, competitors would not have been able to compensate for the lower prices that they would have had to offer to capture below-threshold units with higher prices charged for additional units or revenues from post-sale services.[21]

Finally, the applicants claimed that the effect-based analysis preformed by the Commission neither proved a correlation between the locked-in share of the demand and Tomra's market share nor established that their net effective (post-discount) prices were capable of driving an 'as efficient' competitor out of the market. However, the Court clarified that "for the purposes of establishing an infringement of Article [102 TFEU], it is not necessary to show that the abuse under consideration had an actual impact on the relevant markets. It is sufficient in that respect to show that the abusive conduct of the undertaking in a dominant position tends to restrict competition or, in other words, that the conduct is capable of having that effect (...) it is not necessary to consider whether the evidence adduced by the Commission demonstrated that the agreements in question had actually eliminated competition. In fact, even if the Commission had made a manifest error of assessment, as the applicants allege, in holding that those agreements actually eliminated competition, the legality of the contested decision would not be affected."[22]

III. Comment

The outcome of the case is somewhat disappointing for almost all the parties involved.

The European Commission, although the incontestable winner, thanks to the excellent craft of its Legal Service, has seen an undermining of the long process of reform carried out by DG Competition aimed at extending the 'more economic approach' to the field of dominance.[23] The Court's attachment to its forty-year-old formalistic assessment of exclu-

15 *Ibid.*, at paras. 231 and 236: The applicants alleged that the contestable share of the demand was between 30%–50%, well above the minimum viable share that a competitor would need to profitably remain in the market.

16 *Ibid.*, at para. 239.

17 *Ibid.*, at para. 241.

18 *Ibid.*, at paras. 242–245.

19 *Ibid.*, at para. 267.

20 *Ibid.*, at para. 269.

21 *Ibid.*, at paras. 270–271.

22 *Ibid.*, at paras. 289–290.

23 The process of reform of Article 102 TFEU started with the report "An economic approach to Article 82" elaborated by the Economic Advisory Group on Competition Policy, July 2005, available on the Internet at <http://ec.europa.eu/dgs/competition/economist/eagcp.html> (last accessed on 17 December 2010). This was followed in 2005 by DG Competition, "Discussion Paper on the application of Article 82 of the Treaty to exclusionary abuses" (the 'Discussion Paper'). Finally, after three years of intense debate, the European Commission published in 2009 a considerably shorter version under the title of "Guidance on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings" (see *supra* note 3). Both instruments are available on the Internet at <http://ec.europa.eu/competition/antitrust/art82/index.html> (last accessed on 17 December 2010). The contested decision was published after the 'Discussion Paper' and before the 'Guidance Paper'. Thus, although the so-called effect-based approach had not officially to be applied, the Commission carried out an analysis in line with it.

sive dealing and loyalty rebates in the framework of Article 102 leaves little room for a realistic evolution towards an effect-based approach capable of protecting competition as a whole rather than the competitors.[24] Additionally, the apparent irresponsibility of the Commission vis-à-vis the correctness of its calculations seems to deprive applicants of an effective right to due process as established in Article 6 of the European Convention of Human Rights.[25] The mere fact that the Court did not consider the effect-based analysis performed in the contested decision as 'necessary' for establishing the existence of an abuse does not cancel its specific role in configuring the Commission's reasoning. However, if such a crucial aspect stays unexamined, applicants indeed lack the right to contest the manifest errors present in an enforceable instrument. Moreover, it seems to undermine the expertise of the Commission as, even if calculations are accurate and results exact, they will unnecessarily remain stigmatised.

Firms fearing a finding of dominance seem to be almost handcuffed if the foreclosure effects of their practices are deemed irrelevant. Tomra's technological superiority,[26] combined with an average of 61 % of untied demand[27] in all five national markets examined, deserves proper consideration in order to provide a realistic assessment of market foreclosure. Even if one goes for a broad definition of foreclosure and considers that every contract virtually forecloses some share of the demand,[28] in most cases this is not only procompetitive but also constitutes the day-to-day routine of business making. It seems quite unrealistic to expect a competitive market only if every competitor can compete for the whole amount of the demand. Assuming that a certain degree of foreclosure is inherent to well-functioning markets, the key question is 'how much is too much?' While in some market structures even a small share of tied demand may foreclose competitors,[29] in others the competition for the contract might imply that even a large locked demand would pose few problems.[30] The mere existence of a foreclosed share of the demand does not necessarily foreclose competitors from the market as a whole. Thus, it is important to evaluate whether a given amount of foreclosure is, within a certain context, substantial enough to result in anticompetitive behaviour.

The Court rightly recalls that this assessment should be based upon the specific circumstances of the case rather than upon ex-ante market-share presumptions. In this case, the circumstances point towards an oscillating demand because of long lifecycle products and regulatory constraints/incentives. Nevertheless, an expanding demand with a shrinking minimum viable scale – expressed as a percentual of total demand – shows that efficient competitors had the chance not only of offering their products to Tomra's customers but also to address non-tied customers of growing national markets. In particular, Tomra's tied demand only corresponded to two-fifths of the total. Although the Court interpreted this as a clear sign of anticompetitive foreclosure, within the ambiguous circumstances of the case it somehow seems that when referring to the specific circumstances of the case, the Court is instead referring to the form of Tomra's practices, i.e. exclusive dealing and loyalty rebates and their per se illegality in the framework of Article 102 TFEU.[31]

This treatment of two practices common to a number of industries (and perfectly procompetitive in the absence of a finding of dominance) is to some extent disappointing. Particularly considering that the Court has acknowledged the multiple procompetitive effects of exclusivity in vertical restraints – even for dominant undertakings[32] – as well as the possibility

24 'Guidance Paper', at para. 6.

25 The European Convention on Human Rights (ECHR) of the Council of Europe, 4 November 1950, came in force 3 September 1953, available on the Internet at <http://conventions.coe.int/Treaty/en/Treaties/Html/005.htm> (last accessed on 17 December 2010).

26 Case T-155/06, *Tomra Systems ASA and Others v. European Commission*, at para. 221.

27 See *supra* note 15.

28 *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227 (1st Cir. 1983) at 236: "virtually every contract to buy 'forecloses' or 'excludes' alternative sellers from *some* portion of the market, namely the portion consisting of what was bought."

29 Willard K. Tom, David A. Balto and Neil Averitt, "Anticompetitive Aspects of Market-Share Discounts and Other Incentives to Exclusive Dealing", 67 *Antitrust L. J.* (2000), pp. 615, 625–26, offering examples of foreclosure strategies that deny rivals ability to reach minimum viable scale.

30 Daniel A. Crane and Graciela Miralles, "Toward a Unified Theory of Exclusionary Vertical Restraints" (October 7, 2010), *Southern California Law Review* (Forthcoming); University of Michigan Law & Econ, Empirical Legal Studies Center Paper No. 10-023; University of Michigan Public Law Working Paper No. 218. Available on the Internet at <http://ssrn.com/abstract=1689068>, at pp. 28–37. This paper proposes an assessment of the effects of exclusionary vertical restraints through a two-step test. The first step addresses the existence of foreclosure and, only if it exists, step 2 analyzes if the amount of foreclosure at issue is substantial i.e. can have anticompetitive effects in the relevant market as a whole.

31 See *supra* note 10.

32 See generally Case T-65/98 *Van den Bergh Foods v. Commission* [2003] ECR II-4653.

of providing a justification for the granting of loyalty rebates should they entail cost savings that can eventually be passed on to final consumers.[33] However, the Court remains extremely attached to the line of per se illegality established in *Hoffmann-La Roche* and has consistently reaffirmed its central role on every possible occasion.

Such an approach presents two problems of overall coherence. The first concerns the internal consistency of Article 102. The second, the relations articulated between Article 101 and Article 102.

While the analysis of exclusive dealing has certainly evolved in the framework of dominance, no such thing can be said regarding loyalty rebates even though they have quite similar market effects. In this sense, the General Court found in *Michelin II* that loyalty-inducing rebates categorically have foreclosure effects when undertaken by dominant firms.[34] In *Van den Bergh Foods*, however, the Court faced a firm with an even greater market share than in *Michelin II* and yet applied a foreclosure-based effects analysis.[35] The apparent difference was that the *Van den Bergh* restraints did not directly involve price. This harsher approach to price-based conduct (i.e. rebates) than to a non price-based conduct (i.e. exclusivity) seems further unjustified within an analysis of effects such as the one carried out in the contested decision. Particularly given that, rather than being more anticompetitive, price incentives provide easier exit strategies than exclusivity.[36] Thus, customers may more easily switch in case competitors' offer would compensate them for the loss of the rebate without having to breach an exclusivity contract or deal with penalty clauses.

Second, this somehow fictitious categorisation of loyalty rebates as being per se illegal creates an additional problem as it leads to two different standards for analysing discount practices depending on the Article under which they will be tackled. Thus, while the effects-based assessment performed under Article 101 takes into account the efficiencies associated with rebate systems in the framework of *single branding* vertical restraints – hold-up, adverse selection, and moral hazard problems[37] – the inference of foreclosure in *Michelin II* as recalled by the Court in *Tomra*[38] is based upon the assumption that, other than a strict cost-related justification, no efficiencies can come from such a system when enabled by a dominant undertaking. Proving cost justification is extremely difficult,[39] which means that dominant firms face a nearly irrebuttable presumption that certain practices foreclose and lack any efficiency justification.

After a long debate about the optimal application of the more economic approach to Article 102 cases, this judgment embodies the willingness of the Court to maintain its traditional line when confronted with abuse of dominance. By relegating the relevance of the effect-based analysis, the driving idea of symmetry between the application of Articles 101 and 102 has been set apart. The reasoning of Tomra indicates that, in the view of the Court, the characteristics of unilateral conduct in the presence of dominance involve certain specificities that prevent an actual transplant of the foreclosure assessment and the efficiency defence as enabled by Article 101. However, it is also true that the 'contested decision' was taken prior to the approval of the 2009 'Guidance Paper' on Article 102, and therefore performed a non-mandatory assessment of market effects. Now that the Commission has established a more or less 'compulsory' framework of analysis[40], let us expect it to find its way to the European Court eventually and provide, as intended, 'greater clarity and predictability' for dominant undertakings.[41]

33 Case T-219/99 *British Airways v. Commission* [2003] ECR II-5917, at paras. 69 and 86.

34 Case T-203/01 *Michelin v. Commission (Michelin II)* [2003] ECR II-4071, at para. 65: *"it may be inferred generally from the case-law that any loyalty-inducing rebate system applied by an undertaking in a dominant position has foreclosure effects prohibited by Article [102] EC"*.

35 Case T-65/98 *Van den Bergh Foods v. Commission*, at paras. 86 and 104.

36 Phillip Areeda and Herbert Hovenkamp, *Antitrust law: An Analysis of Antitrust Principles and their Application* (Aspen Publishers, 2006), at para. 768b4; Herbert Hovenkamp, "Discounts and Exclusions", 857 *Utah Law Review* (2006), at p. 844.

37 "Commission notice – Guidelines on Vertical Restraints", in *Official Journal C 130*, 19/05/2010, P. 0001–0046 2010), at paras. 125–144, the Guidelines establish that *single branding* obligations of up to 80% of a customer's requirements will be lawful if no longer than five years.

38 Case T-155/06 *Tomra Systems ASA and Others v. European Commission*, at para. 212.

39 This defence has never succeeded as the European Community Courts have consistently considered the cost-related justification put forward by the incumbents as too vague. See Case T-203/01 *Michelin v. Commission (Michelin II)*, at para. 108; Case T-219/99 *British Airways v. Commission*, at para. 285. See also the analysis of the cost-justification provided by Tomra in the contested decision, Case COMP/E-1/38.113–*Prokent – Tomra*, at para. 353.

40 Case T-7/89 *Hercules Chemicals v. Commission* [1991] ECR II-1711, para. 53: "According to settled case-law, the Commission may not depart from rules which it has imposed on itself".

41 The extent to which the 'Guidance Paper' represents a self-limitation for the Commission remains unclear (see paras. 2–3).