

Statement regarding the CMA's decision to close an investigation into a suspected breach of competition law in the pharmaceutical sector on the grounds of administrative priority

Party: The name of the party to the investigation has not been published.

Case reference: CE/9855-14

Case closed: June 2015.

Issue: Suspected loyalty-inducing discount scheme.

Relevant provision: Competition Act 1998 (the Act), Article 102 of the Treaty on the Functioning of the European Union (Article 102 TFEU).

Summary of closure decision

The CMA has closed its investigation into a suspected breach of competition law in the pharmaceutical sector on the grounds of administrative priority and has sent a warning letter to the party to the investigation identifying potential concerns that may arise in the context of discounts and rebates. Neither the decision to close the investigation on administrative priority grounds nor the decision to send a warning letter to the party amount to a statement as to whether the party to the investigation infringed competition law. The CMA has not reached a view as to whether the party to the investigation infringed competition law and no assumption should be made that there has been any such infringement.

Having identified part of the alleged conduct as a focus for the investigation and following a period of evidence gathering and assessment, the CMA considered whether to proceed with the investigation in light of its Prioritisation Principles.¹ The CMA decided, on administrative priority grounds, not to continue its investigation because it no longer fitted within the CMA's casework priorities, and the CMA considered that continuation of the investigation in order to determine whether an infringement had been committed was not warranted.

While the CMA would have needed to gather and assess further evidence in order to reach a provisional conclusion on such matters, the evidence that the CMA had

gathered to date suggested that further investigation of the conduct on which the CMA had focused would, in the particular circumstances of the case, have had limited, if any, impact on consumer welfare. Accordingly, the CMA considered that further commitment of its resources to gather sufficient evidence to determine whether an infringement of competition law had been committed was not warranted in the particular circumstances of this case.

The decision to close this investigation should not be taken to imply that the CMA would not prioritise investigations into suspected loyalty-inducing discount schemes in the future.

Potential competition concerns regarding discounts or rebates

In order to provide general guidance to businesses and their advisers, the CMA describes below some of the circumstances in which the provision of rebates or discountsⁱⁱ by a dominant company may raise competition concerns.ⁱⁱⁱ

The provision of discounts or rebates can benefit both customers – for example, through lower prices – and the business providing the discount or rebate – for example, by helping the firm to achieve economies of scale and expand production. Further, rebates or discount schemes which pass cost savings from increased volumes on to a customer by offering the customer lower prices on further units once a particular volume has been purchased are, in general, unlikely to raise competition concerns even when they are offered by a dominant company.^{iv}

However, even in the case of rebates or discounts which are not conditional on the customer obtaining all or most of its requirements from a dominant company, certain rebates or discounts offered by a dominant company may be capable of restricting competition contrary to the Chapter II prohibition of the Act and/or Article 102 TFEU by having a loyalty-inducing or fidelity-building effect.^v Such rebate or discount schemes may raise competition concerns due to their potential to exclude or limit the ability of competing firms to operate in the market. Where competition is thus restricted, the incentives for firms to innovate may be dampened and customers may suffer higher prices in the longer term.

For example, rebate or discount schemes which are offered by a dominant company and which, on condition that a volume threshold is reached, offer a customer lower prices on units below as well as above that threshold (a 'roll-back' rebate or discount)^{vi} may be capable of inducing the customer's loyalty. This may particularly be the case where:

- there are units which a customer is required, or has a strong preference, to buy from the dominant company (such units may be referred to as the

dominant company's 'assured base' or the 'non-contestable' share of the customer's demand);

- there are also units which the customer needs and which the customer may be willing and able to purchase either from the dominant company or from a competitor to the dominant company (such units may be referred to as the 'contestable share' of the customer's demand or the 'contestable sales'); and
- the grant of the rebate or discount is conditional on the customer purchasing contestable sales from the dominant company (in other words, the customer will be entitled to a rebate or discount if it purchases units from the dominant company that it might otherwise have chosen to buy from the competitor).

Such circumstances are likely to make it more difficult for a competitor to compete for the contestable sales because any competitor would, in order to win the relevant contestable sales, have to compensate the customer for the loss of the discount that it would have received on the assured base had it purchased those contestable sales from the dominant company.

Further, where the structure of the rebate or discount scheme means that the price which a competitor would have to charge to compete for contestable sales is below the dominant company's costs of production,^{vii} the CMA is likely to be concerned that a competitor that is equally as efficient as the dominant company could be foreclosed from competing for some, or all, of the contestable share of the market.^{viii}

Moreover, such concerns are likely to be exacerbated where the structure of the rebate or discount scheme is such that the customer is able to reduce its overall expenditure on the dominant company's products by increasing the volume of contestable sales it purchases from the dominant company (in other words, where the structure of the rebate or discount scheme leads to negative incremental prices for sales in the contestable share of the market). Such a scheme may have a particularly strong loyalty-inducing effect on the customer and make it particularly difficult for a competitor to compete for contestable sales, because any competitor would necessarily incur losses if competing on price for those sales.^{ix}

The above matters do not constitute an exhaustive list of the circumstances in which potential competition concerns may arise in respect of rebate or discount schemes when imposed by dominant companies.

The above does not constitute legal advice and should not be relied upon as such. Companies are advised to seek independent legal advice regarding compliance with competition law.

ⁱ [CMA Prioritisation Principles](#) (CMA16).

ⁱⁱ Rebates and discounts both involve reductions in the price paid by the customer. The difference is that with discounts the reduction in price is upfront such that the customer pays the lower price at the point of sale whereas with rebates the reduction in price occurs after the point of sale such that the customer receives a refund from the seller.

ⁱⁱⁱ General guidance on abuse of a dominant position, including details of how an assessment is made of whether a company has a dominant position, is available on the [CMA's webpages](#).

^{iv} Sometimes known as an 'incremental' rebate or discount.

^v When considering such rebates or discounts, the CMA is likely to consider 'all the circumstances, particularly the criteria and rules governing the grant of the rebate, and to investigate whether, in providing an advantage not based on any economic service justifying it, the rebates tend to remove or restrict the buyer's freedom to choose his sources of supply, to bar competitors from access to the market... or to strengthen the dominant position by distorting competition'. Case T-203/01 *Michelin II* (2003) ECR II-4071, paragraph 60.

^{vi} Sometimes also known as a 'retroactive' rebate or discount.

^{vii} That is, where the effective price charged by the dominant company for all, or a relevant range, of the contestable sales is below the dominant company's costs. The CMA is likely to consider that the lower that the estimated effective price over the relevant range is compared to the average price of the dominant company, the stronger the loyalty-enhancing effect. However, as long as the effective price remains consistently above the long run average incremental cost (LRAIC) of the dominant company, this would normally allow an equally efficient competitor to compete profitably notwithstanding the rebate or discount. In such circumstances the CMA is likely to consider that the rebate or discount is normally not capable of foreclosing in an anti-competitive way. Where the effective price is below average avoidable cost (AAC), as a general rule the CMA is likely to consider that the rebate or discount scheme is capable of foreclosing even equally efficient competitors. Where the effective price is between AAC and LRAIC, the CMA is likely to investigate whether other factors point to the conclusion that entry or expansion even by equally efficient competitors is likely to be affected.

^{viii} This is particularly the case where a competitor cannot employ effective counterstrategies, for example, due to long term contracts and a lack of price transparency.

^{ix} This is because, while not being able to generate any revenue from these sales, some costs would be incurred in supplying them.