CLIFFORD
CHANCE

Submission to the joint Federal Trade Commission ("FTC")/ Antitrust Division of the Department of Justice ("DOJ") request for public comments on conditional pricing practices

1. Introduction

Thank you for the opportunity to comment on the economic analysis and legal policy implications of conditional pricing practices. On behalf of many of our global clients we look forward to more practical, predictable and pliable guidance from the FTC and DOJ (hereafter referred to collectively as the "**Agencies**") on this topic.

We believe that the output of the FTC-DOJ Workshop that was held on June 23, 2014 ("**Workshop**") on the topic and any future guidance that the Agencies may publish on the subject are of particular significance and importance to companies operating across multiple jurisdictions. Multi-nationals are often faced with the difficulty of trying to adapt a marketing or sales practice to comply with the laws of several jurisdictions. Global clients welcome the ability to predict ex ante how their practices will be examined in any given jurisdiction and the opportunity to adjust accordingly.

Moreover, there is a particular significance attached to how the Agencies treat this subject, and how US jurisprudence regarding this area of law develops more generally. The approach to conditional pricing practices adopted by the Agencies has the potential to significantly influence and shape both the analytical framework and antitrust enforcement policies adopted by other antitrust regulators globally in their approach to conditional pricing practices. The decisions of US Courts in this area also influence judicial and administrative bodies in other jurisdictions in shaping judicial and antitrust policy outcomes, particularly in the case of jurisdictions with developing antitrust regimes. The Agencies' efforts therefore have the potential to facilitate greater international convergence and consistency in an area of antitrust practice that has been the subject of diverging jurisprudence both within the United States, and between major antitrust regimes globally.

2. Executive Summary

In order for companies to adopt antitrust compliant conditional pricing, guidance from the Agencies is imperative. The guidance must provide a clear and practical means to evaluate whether an existing business practice falls within or outside of the antitrust laws, and to shape future practices to be antitrust compliant. We propose that the best approach to analyzing conditional pricing is to avoid economic and formulaic approaches, and rather to rely on the time-tested rule of reason. The former approaches fail to appreciate the procompetitive nature of

many conditional pricing programs while the latter appropriately balances all competitive effects. We also suggest that the Agencies provide safe harbors such that companies can simply identify when their conditional pricing program poses greater risk and/or requires antitrust review.

3. Guiding principles

Commissioner Ohlhausen began the Workshop by stating that, regardless of what analytical criteria is adopted by the Agencies, any analysis must be transparent, predictable and fair. We believe that for any guidance to be of benefit to practitioners and business, the Agencies must adopt an analytical process that is both administrable, consistent, and accurate.

Thus, as a primary matter, however the DOJ and FTC decide to examine the issue of conditional pricing practices, we would respectfully request that the Agencies together work towards producing guidelines in consultation with industry and the legal profession that explain with examples how conditional pricing practices will be examined. At a minimum, the Agencies should work to produce guidelines that identify characteristics of conditional pricing practices that are likely to act as "red flags" to the Agencies and which, as a result, are more likely to attract greater regulatory and litigation risk. In addition, the Agencies should also develop safe harbors or criteria that will enable clients to develop and implement conditional pricing with a degree of certainty that such conduct will not be challenged.

We acknowledge the potential difficulties associated with compiling comprehensive guidance in relation to the analytical framework to be adopted for the purposes of assessing such conduct, particularly given the potential divergence in developing appropriate analytical paradigms for assessing for both single and multi-product conditional pricing practices and rebates. However, we submit that the exercise of determining types of conditional pricing that is unlikely to be problematic or result in an anticompetitive effect is not as difficult or onerous as determining the precise boundary between what is lawful and what is anticompetitive.

On this basis, identifying certain "safe harbors" is likely to provide a level of certainty that is at least sufficient to assist practitioners and businesses in determining which conditional pricing practices are unlikely to be problematic and those which are more likely to be subject to regulatory investigation and possible litigation. In-house legal teams and practitioners are likely to find such guidance particularly helpful, especially when counseling clients whose principal jurisdiction may not be the United States. As noted during the Workshop, there is currently a degree of divergence between approaches towards conditional pricing practices by courts and regulators in the United States and those in Europe, which can create compliance challenges for even the most sophisticated clients.

Additionally, such guidance is also likely to be useful to regulators and courts in jurisdictions that are seeking to create antitrust laws to address conditional pricing practices, amend their current legal frameworks to address such practices more effectively, or to apply their existing

legal framework to a complex subject matter that they have not previously reviewed or considered in any great depth.

4. Inconsistencies associated with current approaches to conditional pricing practices

The Workshop revealed that the current treatment of conditional pricing under US antitrust law is inconsistent, opaque and confusing. At the Workshop, panelists identified several ways conditional pricing practices have been analyzed by US courts, including the disparate standards and anomalies that have emerged among the various district and circuit courts that have examined the issue. The principal analytical perspectives identified include applying existent analytics to conditional pricing, such as market concentration and foreclosure analysis, predatory pricing analysis, discount attribution tests, and exclusive dealing analysis. Many of these economic approaches to conditional pricing analysis can provide a bright line test and a degree of predictability. However, each is also subject to criticism from both economists and lawyers for potentially mischaracterizing conditional pricing practices as other forms of conduct that may not suitably reflect or share similar qualities for the purposes of antitrust analysis. This can result in the application of analytical paradigms that fail to appropriately consider the competitive effects of the conduct being examined.

We submit that economic and formulaic approaches to marketing practices are better suited toward ex post analysis and are frequently of little use to companies attempting to determine whether a practice is legal or illegal before implementing it. For example, oftentimes the data necessary to perform a formulaic analysis may be burdensome or expensive to assemble. Even where the data is available, performing an analytical assessment of such data before implementing a conditional pricing practice may at times be cost-prohibitive or otherwise so time and resource demanding as to be unfeasible — perhaps depriving consumers of the benefits of the practice. In many cases, the data needed to perform a concrete economic analysis may simply not be there at all. Economic and formulaic approaches may provide some insight into the adverse effects of conditional pricing ex post, but that is only half the story. None of these formulaic analytical frameworks address the pro-competitive aspects of conditional pricing, which are important considerations for ensuring effective competition policy and enforcement priorities.

Conditional pricing protects the manufacturer's investment in its own product, permits companies to meet competition, and oftentimes results in a more competitive marketplace. In some cases, conditional pricing can ensure that discounts are passed through to consumers. Such provisions often prevent free-riding and at the same time inspire competitors to offer equally discounted pricing. Conditional pricing provisions can keep smaller dealers in the market (who can then continue to provide competitive constraints on other entities in the market), incentivize the downstream sales effort by allowing for training, extra services and/or logistics, build downstream scale and scope, equalize supply and demand, and permit cross-product substitution making more types of products available to the marketplace. These benefits of conditional

pricing are often overlooked or inadequately addressed when the examination is whittled down to a purely economic and formulaic analysis. Indeed, in many instances such an inflexible analysis may chill pro-competitive behavior. In line with comments made by the US Supreme Court[1], we submit that while there is a role for economics to inform antitrust law, and to assist in understanding and resolving antitrust questions, antitrust law should not precisely replicate economists' (often conflicting) views for risk of affecting the administrability and consistency that should be associated with an effective antitrust framework.

5. Suggested approach: an analytical framework based on a rule of reason

Rather than adopting one of the economic and formulaic analytical frameworks identified above, we suggest that there is no one-size-fits-all approach to conditional pricing and that the better method of examining such provisions is to apply rule of reason analysis. While rule of reason is by no means the bright line test that many of the more economic and formulaic approaches provide, it is an analysis that private and inhouse practitioners, courts, and enforcers in the US are familiar with and understand how to employ. Rule of reason balances harms against the procompetitive benefits.

Conditional pricing is becoming ever more prevalent in cross-border, technology marketplaces where traditional methods of assessing antitrust harm are difficult to employ and which may produce misleading results. The law must be flexible enough to address these situations for both single and multi-product practices.

Rule of reason analysis provides necessary flexibility in the law. By applying a balancing test, false positive are less likely to be achieved and any resultant chilling effect diminished. When the requisite data is not available, companies can examine their situation through other lenses. In that way, companies can predict more reliably ex ante whether their conditional pricing practice is more likely at the end of the day to produce a net harm or net benefit, and act accordingly having a better understanding of any potential antitrust risk that may be associated with their conduct.

Adopting such an approach also has the potential to facilitate greater convergence between the United States and the approach adopted by the European Commission ("**EC**") in its 2009 Guidance Paper[2], which sets out an effects-based approach toward single-firm conduct. While the rule of reason and effect-based analysis are not one in the same, they are more akin than not.

---

[1] In *Leegin Creative Leather Prods., Inc v PSKS, Inc.*, 551 U.S. 877, 914-17 (2007).

[2] European Commission, Guidance Paper on the EC's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, 2009. We note that the European Commission does rely in part on formulaic economic approaches in determining cost benchmarks (e.g., its consideration of average avoidable cost (AAC) and long-run average incremental cost (LRAIC)). But, the European Commission also weighs the efficiencies and justifications of any loyalty scheme against any potential harms. And the European

Irrespective of the recent decision of the General Court in *Intel,* which appears to uphold a strait-jacketed, form-based approach (at least for exclusivity rebates) indicating that *exclusive rebates* are abusive unless justified by economic efficiencies, a rule of reason (or effects based approach) is more likely to provide the Agencies with an effective basis to differentiate between harm that results from competitive pressures (i.e. strong competition) and harm that is caused by another entity's conditional pricing practices. Such an approach is more likely to facilitate the widely-acknowledged improvements to antitrust policy regarding conditional pricing that have otherwise been associated with areas of antitrust that are subject to an effects-based analysis.

Notwithstanding the potential implications of the *Intel* decision on the EC's approach to investigating conditional pricing practices, a rule of reasons approach is also more likely to facilitate greater convergence between the approach of the Agencies and that of the EC. Any convergence between the approach of the Agencies and the EC in this respect is likely to have a positive effect on compliance burdens for multi-nationals that operate across both jurisdictions.

6. Providing workable and pragmatic guidance to practitioners and business

As noted above, guidance provided by the Agencies as to how they will assess conditional pricing practices is likely to be of great assistance to practitioners and businesses alike. However, given the current jurisprudence surrounding such practices we acknowledge the potential difficulties associated with compiling comprehensive guidelines on how conditional pricing practices will be assessed. While the Agencies should endeavor to settle on a clear and consistent analytical framework for assessing all types of conditional pricing, at a minimum the Agencies should provide guidance in the form of guidelines that at least enable practitioners and businesses to assess the level of associated regulatory and litigation risk with particular types of conditional pricing conduct. This could be achieved by using certain characteristics or criteria as a basis to determine whether the conduct in question is likely to be problematic or result in anticompetitive effects and will assist in reducing the burden of antitrust compliance.

Adopting a rule of reason approach as the analytical paradigm for assessing such conduct is likely to provide a framework for identifying certain characteristics or "safe harbors" that allow practitioners and businesses to advise on and develop conditional pricing practices, respectively, knowing that such conduct is unlikely to be problematic or challenged by the Agencies so long as certain conditions are present and/or criteria fulfilled. In this regard, we are of the view that certain "safe harbors" that have been put forward previously have merit in effectively balancing the need to ensure that practices that lessen competition substantially are caught while also providing businesses with a degree of certainty to engage in conduct that has pro-competitive

---

Court of Justice has emphasized recently the importance of focusing on effects rather than objective benchmarks when assessing antitrust harm. *See* Case C-67/13 P, Groupement des cartes bancaires (CB) v Commission [2014].

effects. As a starting point the Agencies may wish to consider each of the following, or a combination of the following, factors for the purposes of developing appropriate "safe harbors":

i. The supplier/ entity engaged in conditional pricing lacks market power;

ii. The level of competition for customer contracts is sufficient to reduce the effect that any exclusivity may have on pricing;

iii. Less than 30%-40% of the market(s) in question are covered or implicated by the relevant customer contracts; and

iv. The rebate or discount is not coercive.

Additional guidance might also include factors and characteristics that the Agencies consider to be more likely to lead to certain conduct being characterized as "inherently suspect" and leading to a truncated rule of reason approach. Doing so would assist in identifying factors that the Agencies may consider to be "red flags", likely to lead to regulatory scrutiny and/or litigation.

We are of the view that producing guidelines along these lines will assist practitioners and businesses in knowing the legal parameters of conditional pricing practices, which will reduce antitrust compliance burdens on business, facilitate more effective and consistent enforcement agendas for the Agencies, and will result in improvements to antitrust policy.

7. Conclusion

We look forward to practical, predictable and pliable guidelines from the Agencies that can hopefully steer clients, practitioners, courts, and other agencies, both domestic and foreign toward a common analytical framework. At a minimum, the Agencies should seek to produce guidelines that will enable practitioners and businesses to assess the level of associated regulatory and litigation risk with particular types of conditional pricing conduct and facilitate better decisional practice.