

Unclassified

DAF/COMP/WD(2016)3

Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

06-Jun-2016

English - Or. English

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

Cancels & replaces the same document of 31 May 2016

FIDELITY REBATES

-- Note by Japan--

15 - 17 June 2016

*This document reproduces a written contribution from Japan submitted for item 6 of the 125th OECD Competition committee on 15-17 June 2016.
More documents related to this discussion can be found at www.oecd.org/daf/competition/fidelity-rebates.htm*

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JT03397458

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--JAPAN--

1. Introduction

1. While offering rebates in itself is not always problematic under the Antimonopoly Act (hereinafter referred to as ‘AMA’) in general, there are some possibilities for such a conduct to violate the AMA as “private monopolization” (exclusionary private monopolization (Article 2(5) of the AMA)), or “unfair trade practice” such as discriminatory treatment on trade term (Item (4) of the Designation of Unfair Trade Practices (hereinafter referred to as ‘Designation’)), exclusive dealing (Item (11) of the Designation), dealing on restrictive terms (Item (12) of the Designation), depending on the ways or the effects of the rebates.

2. The Japan Fair Trade Commission (hereinafter referred to as ‘JFTC’) published several guidelines focusing on specific types of conduct or specific business fields, which clarify the viewpoints regarding the application of the AMA. The JFTC considers whether rebate-offering is problematic under the AMA or not, based on the guidelines corresponding to the types of conduct, etc.

3. There is no specific provision which describes the definition and the nature of “fidelity” rebates as well as their impacts on competition in the AMA, relevant legislations, and guidelines. The illegality of each case will be judged according to the relevant guidelines which describe the viewpoint on rebate-offering.

4. In this contribution paper, we would like to introduce “Guidelines for Exclusionary Private Monopolization under the AMA” and “Guidelines Concerning Distribution Systems and Business Practices” which are considered useful in understanding the JFTC’s viewpoints on rebate-offering. We would also like to introduce as a reference the case against Intel in Japan (2005) which is relevant to offering of rebates.

2. Outline of “Guidelines for Exclusionary Private Monopolization under the Antimonopoly Act” (2009) and “Guidelines Concerning Distribution Systems and Business Practices”² (1991)

2.1 Guidelines for Exclusionary Private Monopolization under the Antimonopoly Act

5. The AMA prohibits “such business activities, by which any enterprise, individually or by combination or conspiracy with other enterprises, or by any other manner, excludes or controls the business activities of other enterprises, thereby causing, contrary to the public interest, a substantial restraint of competition in any particular field of trade” (Article 2(5) of the AMA) as private monopolization (Article 3 of the AMA). Furthermore, “exclusionary conduct” is interpreted as various conducts that would cause difficulty for other enterprises in continuing their business activities or for new market entrants in commencing their business activities, thereby would be likely to cause a substantial restraint of competition in a particular field of trade (1(1) of Part2 of the guidelines).

6. The guidelines were formulated¹ mainly in order to respond to opinions that the regulation against exclusionary conduct might cause a so-called chilling effect for enterprises and interfere with their fair and free business activities, because of the difficulty in distinguishing exclusionary conduct from normal business activities leading to exclude the business activities of other enterprises as a result.

7. The guidelines include exclusive rebate-offering as a conduct which could be exclusionary conduct².

2.2 *Guidelines Concerning Distribution Systems and Business Practices*

8. The guidelines are intended to contribute to preventing firms and trade associations from violating the AMA and helping them in the pursuit of appropriate activities, by specifically describing, with respect to Japanese distribution systems and business practices, the types of conduct which may impede free and fair competition and violate the AMA. Part 2 of the guidelines, mainly keeping in mind transactions in the distribution process in which consumer goods reach their consumers, shows the viewpoints of the AMA, in light of the regulation of unfair trade practices³ (discriminatory treatment on trade term, exclusive dealing, dealing on restrictive terms; etc.) (Article 19 of the AMA).

9. The guidelines include rebates provided as a means of restricting a distributor's business activities, rebates based on market shares, remarkably progressive rebates and rebates that have the function of requiring designated accounts, as rebates which may restrict the business activities of distributors and could be problematic under the AMA. Out of these rebates, rebates provided as a means of restricting a distributor's business activities (of which rebates provided as a means of restricting handling of competing products), rebates based on market shares and remarkably progressive rebates are judged if the conducts may fall under unfair trade practices, from the perspective of whether or not "the restriction may result in making it difficult for new entrants or competitors to easily secure alternative distribution channels".

2.3 *Differences between the viewpoints of the rebates in the above two guidelines*

10. The AMA regulates anticompetitive unilateral conduct not only by the provision of "private monopolization" (Article 3 of the AMA) but also by the provision of "unfair trade practices" (Article 19 of the AMA).

11. Unilateral conduct by an enterprise restricting its trading partners to deal with its competitors, etc. (in this context, through rebate-offering which has the effects of making its trading partners refrain from dealing with its competitors) is prohibited as private monopolization if a dominant firm uses this kind of conduct, excludes its competitors from a particular field of trade, and causes substantial restraint of competition in the field. On the other hand, even if the conduct does not cause such a restraint, in cases where rebate-offering is imposed by an influential manufacturer in a market, and if the restriction results in making it difficult for new entrants or competitors to easily secure alternative distribution channels, such conduct may be prohibited as unfair trade practices

¹ The amendment of the AMA enacted in June 2009 introduced the surcharges against exclusionary private monopolization and the Guidelines for Exclusionary Private Monopolization were formulated in October 2009.

² More fully discussed in 3.1 below.

³ The JFTC can order payment of a surcharge against certain types of unfair trade practices, but cannot order surcharge payment against exclusive dealing and dealing on restrictive terms; etc.

12. For this reason, whereas the Guidelines Concerning Distribution Systems and Business Practices clarify the viewpoint on rebate-offering which may be problematic under the AMA in terms of the regulation against the unfair trade practices, the Guidelines for Exclusionary Private Monopolization clarify the viewpoint whether or not the rebate-offering which have the effects of restraining the trade partners' dealings of competitors' products (exclusive rebate-offering) falls under the exclusive conduct in terms of the regulation against the exclusionary private monopolization. However, these viewpoints on rebate-offering in both guidelines have similarities as well.

3. Viewpoint on each type of rebates under the AMA

3.1 Viewpoint on exclusive rebate-offering in Guidelines for Exclusionary Private Monopolization under the Antimonopoly Act

13. Rebates are actually used for a variety of purposes such as sales promotions and adjustment of purchase prices. In fact, rebates may have the procompetitive effect to stimulate the demand or, as an element of prices, promote formation of prices that reflect the actual market situation. Therefore, rebate-offering in itself does not immediately fall under an exclusionary conduct.

14. However, when an enterprise offers rebates to trade partners on the condition that the amount or volume of purchase from the enterprise or the proportion of amount (volume) of purchase from the enterprise to the total amount (volume) of its purchase reaches a particular threshold or more during a specified period, such conduct may have effects in restraining the trade partners' dealings of competitors' products. Thus, where rebate-offering to the trade partners on the condition for certain amount of purchase from the alleged enterprise, etc. has effects in restraining the trade partners' dealings of the competitors' products⁴, such conduct (hereinafter referred to as 'exclusive rebate-offering') may have the same effect as exclusive dealing.

15. Therefore, whether such conduct falls under exclusionary conduct will be determined on the basis of the factors for assessment such as conditions of the entire market of the product, position of the said enterprise in the market, position of the competitors in the market, period of the conduct, number of trade partners, their share and conditions of the conduct.

16. The JFTC will comprehensively consider the following factors to assess whether or not rebate-offering has an effect of restraining the dealings of competitors' products and have the same effect as exclusive dealing.

A. Level of rebates

17. Where the amount or rate of rebates is set at a higher level, the trade partners would be more likely to purchase more products from the enterprise. Such rebate-offering is highly effective in restraining the dealings of competitors' products.

B. Threshold of offering rebates

18. Where threshold for rebate-offering is set at the higher level within the achievable range for the trade partners, the rebates function more effectively to have the trade partners deal products from the

⁴ In addition to cases in which exclusive rebate-offering in itself functions in the same way as exclusive dealing, there are cases in which rebates are used to ensure the effectiveness of exclusive dealing in restraining the dealings of competitive products.

enterprise more preferentially than those from the competitors, and the trade partners would be more likely to purchase more products from the enterprise.

19. Where rebates are offered based on an individual threshold for each trade partner, the trade partners would be more likely to purchase more products from the enterprise than when the same threshold is set for all the trade partners, because the enterprise can set the threshold in accordance with the individual circumstances of each trade partner so that the rebates function more effectively to have the trade partners deal the enterprise's products with greater preference than the competitors' products. Rebate-offering is highly effective in restraining the dealings of competitors' products in such a case.

C. Progressiveness of rebates

20. When the level of rebates is progressively set in accordance with the quantity of trade, etc. in a specified period, the rebates function more effectively to have the trade partners deal products from the enterprise more preferentially than those from the competitors, and the trade partners would be more likely to purchase more products from the enterprise. Such rebate-offering is highly effective in restraining the dealings of the competitors' products

D. Retro activeness of rebates

21. If rebates are offered for the entire quantity of trade made thus far in case that the quantity of trade has exceeded a certain threshold, the rebates function more effectively in having the trade partners deal products from the enterprise more preferentially than those from the competitors, and the trade partners would be more likely to purchase more products from the enterprise than when rebates are offered only for the portion of the quantity of trade, etc. which exceed the threshold required for rebate-offering. Such rebate-offering is highly effective in restraining the dealings of competitors' products.

3.2 Viewpoint on the rebate-offering in the Distribution Systems and Business Practices Guidelines

A. Viewpoint

22. The nature of rebates provided by manufactures to distributors is diverse, including those that adjust billing prices, and those that promote sales. Thus, rebates are offered for a variety of purposes, and rebates as one element of price also have the aspect of promoting price formation reflecting the actual conditions in a market. Accordingly, the rebate-offering in itself does not necessarily present a problem under the AMA.

23. There are cases, however, where, they may restrict the business activities of distributors and present a problem under the AMA, depending on the ways in which rebates are provided.

B. Cases where there is a problem under the AMA

a. Rebates provided as a means of restricting a distributor's business activities

24. Rebates might be provided as a means of restricting a distributor's sales price, handling of competing products, sales territory, customers, etc. For example, rebates might be reduced if the distributor does not sell products at the price indicated by the manufacturer. It needs to be judged whether such restrictions fall under unfair trade practices, including "dealing on exclusive terms" (unjustly trading with another party on condition that the said party shall not trade with a competitor, thereby tending to reduce trading opportunities for the said competitor), "dealing on restrictive terms" and "resale price restriction".

25. Furthermore, the conduct of discriminating against distributors in the provision of rebates depending on the price, handling of competing products, or the like, is illegal as an unfair trade practice (“discriminatory treatment on transaction terms”, etc.) if it has the same or similar function as the imposition of illegal restrictions on distributors.

26. Also, the same shall apply to cases where a “repayment system” (under which a manufacturer collects all or a part of the margin from the distributors and pays it back after a certain period) is used as a way of illegal restriction, or has the same or similar functions as the imposition of illegal restriction on the distributors.

b. Share rebates

27. A manufacturer sometimes provides rebates to its distributors according to the percentage of sales of the manufacturer’s products in the total business of each distributor during a specific period, or according to the share that the manufacturer’s products have in the display of all goods at the distributor’s store.

28. The offering of such rebates by an influential manufacturer⁵, if it has the function of restricting a distributor’s handling of competing products and may result in making it difficult for new entrants or competitors to easily secure alternative distribution channels, is illegal as an unfair trade practice (“trading on exclusive terms”, etc.).

c. Remarkably progressive rebates

29. At times a manufacturer in providing volume rebates may set a rebate rate progressively, according to a ranking of distributors based on criteria such as quantity of products supplied to each distributor during a certain period. While progressive rebates have the aspect of promoting price formation reflecting actual conditions in a market, if the rate is remarkably progressive, they have the function of encouraging the preferential handling of that manufacturer’s products over those of others.

30. The offering of such rebates by an influential manufacturer, if it has the function of restricting a distributor’s handling of competing products and may result in making it difficult for the new entrants or existing competitors to easily secure alternative distribution channels is illegal as an unfair trade practice (“trading on exclusive terms”, etc.).

⁵ The guidelines stipulate that “whether a firm is ‘influential in a market’ is judged by the market share of the firm, that is, whether it has no less than 10% or its position is within the top three in the market (meaning a product market that consists of a group of products with the same or similar function and utility as the product covered by the conduct, and competing with each other judging from geographical conditions, transactional relations and other factors). Nevertheless, even if a firm falls under this criterion, the firm’s conduct is not always illegal.”

Furthermore, as of April 2016, the JFTC is amending the guidelines and the proposed amendment of the guidelines stipulates that “whether a firm is ‘influential in a market’ is judged by the market share of the firm, that is, whether it has no less than 20% in the market (meaning a product market that consists of a group of products with the same or similar function and utility as the product covered by the conduct, and competing with each other judging from geographical conditions, transactional relations and other factors. Basically, it is judged in terms of the substitutability for consumers, but it is also judged in terms of the substitutability for suppliers, as appreciate.). Nevertheless, even if the market share of a firm goes beyond the threshold, the firm’s conduct is not always considered illegal.”

3.3 *Summary*

31. As explained in 2.3 above, while the intentions and purposes of the two guidelines are different, we can find some commonality in them about which aspects of rebates we should focus on to judge illegality such as progressiveness of rebates and level of offering rebates (mainly based on market share).

4. **Relevant case**

32. There are few cases where rebate-offering was used as tools for anti-competitive conducts in Japan. "Case against Intel Kabushiki Kaisha", however, on which a decision was rendered in 2005, is one such case. Therefore, we would like to introduce this case.

33. Case against Intel Kabushiki Kaisha (recommendation decision on 13 April 2005)⁶⁷

4.1 *Outline of the case*

34. Intel Kabushiki Kaisha⁸ (hereinafter referred to as 'Intel K.K.')

was engaged in imports and sales of CPUs manufactured in the United States by Intel Corporation. In addition to Intel K.K., AMD Japan Ltd. (hereinafter referred to as 'AMD Japan') and Transmeta Corporation (hereinafter referred to as 'Transmeta') in the United States were also selling CPUs to PC manufacturers in Japan. The total sales volume of CPUs that three companies sold to domestic PC manufacturers directly or through agents constituted almost all of CPUs which were sold in Japan. In 2003, the percentage of Intel's CPU sales volume sold by Intel K.K. to the total domestic CPU sales volume was approximately 89%. Furthermore, Intel's CPU was widely known by consumers who want to buy PCs and had a strong brand status. It was important for domestic PC manufacturers that they had PC equipped with Intel's CPU in their PC lineup they sell.

35. After around 2000, AMD Japan started to sell its CPUs in competition with Intel's CPUs at a lower price, which, together with other factors, led domestic PC manufacturers to incorporate AMD's CPUs into their PCs. Consequently, the percentage of AMD's CPU sales volume to the total domestic CPU sales volume increased from approximately 17% in 2000 to approximately 22% in 2002. Based on such facts, Intel K.K. became apprehensive about a continuing increase in the sales volumes of AMD's CPUs. Since May 2002, Intel K.K. began to make five major domestic PC manufacturers refrain from adopting competitors' CPUs for all or most of the PCs manufactured and sold by them or all of the PCs that belonged to specific categories, by making commitments to provide the five PC manufactures with rebates and/or sales promotion funds on condition that

- (a) They have the share of Intel's CPU at 100% and refrain from adopting competitors' CPUs.
- (b) They have the share of Intel's CPU at 90%, and the share of other CPU's at 10%; or
- (c) They refrain from adopting competitors' CPUs to be incorporated into all PCs that belonged to specific categories with relatively large production volume.

⁶ Press Release in English; http://www.jftc.go.jp/en/pressreleases/yearly_2005/mar/2005_mar_8.files/2005-Mar-8.pdf

⁷ The case was concluded before the enactment of the Guidelines for Exclusionary Private Monopolization under the AMA.

⁸ Kabushiki Kaisha in Japanese means a stock company.

36. Such conduct by Intel K.K. decreased the percentage of AMD's and Transmeta's CPU sales volume in the total domestic CPU sales volume from approximately 24% in 2002 to approximately 11% in 2003.

4.2 *Application of the AMA*

37. With regard to the above conducts, the JFTC found that Intel K.K. had, contrary to the public interest, substantially restrained the competition in the market of CPUs sold to the PC manufacturers, by acting to exclude its competitors' business activities related to the sales of CPUs to the five PC manufacturers in Japan. Therefore, the JFTC required Intel K.K. to cease and desist its conducts which violate Section 3 of the AMA (Private Monopolization).