

# Competition Tribunal provides important guidance on retroactive discounts

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## Introduction

## Facts

## Decision

## Comment

### Introduction

Target discounts are a form of conditional rebate, under which a customer is eligible to receive an incentive on meeting a certain business target. Such incentive can be paid for units exceeding the target or for all units, including units that were acquired before the target was reached (retroactive discounts). Target discounts are a common tool employed by suppliers to incentivise customers to increase their purchases from the supplier.

The subject of target discounts set by dominant firms has not been extensively analysed in Israeli case law. It has been more than 20 years since the Competition Tribunal published its decision concerning Israel's dominant newspaper (at the time) – *Yediot Aharonot*. That case provided the general framework to assess pricing practices by a dominant firm. However, the decision provided no clear and concrete reference on how to analyse retroactive pricing discounts. The use of retroactive rebates and their potential exclusionary effect was first analysed by the Israeli Competition Authority (ICA) in 2005, as part of the competition commissioner's Position on the Commercial Practices Between Dominant Food Suppliers and the Large Retail Chains. In the position paper, the ICA explained that in many markets, customers must source most of their demand from the monopoly (eg, because most consumers prefer the monopoly's product), while the remaining share of customer demand is subject to competition (the contested demand). The ICA explained that a retroactive rebate plan often excludes an equally efficient competitor's ability to compete on the contested demand, which is effectively provided to customers by the monopoly at a loss. However, the ICA did not condemn retroactive rebates *per se*, but rather suggested that their impact should be analysed on a case-by-case basis.

In a recent ruling, the Competition Tribunal partially rejected an appeal filed by Ashdod Port Company Inc (Ashdod Port) against the competition commissioner's decision to impose financial penalties on Ashdod Port for abuse of dominant position by way of retroactive discounts. The Competition Tribunal affirmed the competition commissioner's decision that Ashdod Port had a dominant position in the discharge of vehicles that were delivered by shipping carriers from the United States and the European Union. The Competition Tribunal also upheld the ICA's conclusion that the retroactive discount plan that Ashdod Port had applied was liable to harm competition with Haifa Port for the discharge of vehicles on those routes. The Competition Tribunal's judgment thoroughly analysed the legality of target discounts offered by a dominant firm to its customers. The Competition Tribunal adopted a cautious approach towards retroactive target discounts, ruling that such pricing schemes could be condemned even if an equally efficient competitor was not excluded by the target discount and the level of market foreclosure was limited. While the judgment can be read as setting a quasi *per se* prohibition on such discounts, it should be assessed against the background of Ashdod Port's alleged anti-competitive conduct.

### Facts

In 2015 the competition commissioner declared that Ashdod Port was a monopoly in the market for discharge of vehicles from the European Union and the United States in certain shipping lines. It was further declared that Ashdod Port had abused its dominant position by offering retroactive target discounts to vehicle importers that were derived from the expected demand of customers for the coming year. Such discounts made it difficult for Haifa Port to compete with Ashdod Port. Due to capacity constraints and other reasons, Haifa Port could not have competed on the customer's entire demand, but only on part of customer needs. This led to Ashdod Port's retroactive discount being disproportionately bigger than any reasonable discount that Haifa Port could

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have offered. According to the competition commissioner's decision, the target discount plan effectively locked a significant part of the customers' demand to Ashdod Port, resulting in some cases in a *de facto* exclusivity, as importers were economically compelled to discharge all of their imported vehicles in Ashdod Port.

Subsequently, the competition commissioner imposed financial penalties on Ashdod Port (amounting to NIS9 million, approximately €2.2 million) and on two of Ashdod Port's corporate officers (NIS20,000 each, approximately €5,000). The decision was mostly upheld on appeal to the Competition Tribunal, although the sum of the financial penalty on Ashdod Port was significantly reduced.

## Decision

The Competition Tribunal's decision refers to a discount that is offered to customers by the monopolist which is subject to reaching a pre-determined purchase target that is individually tailored to the customer by the monopolist (eg, the customer's total acquisitions in the previous year).

According to the Competition Tribunal, target discounts are not illegal *per se*. In certain cases, target discounts may entail competitive efficiencies, which should be weighed against potential concerns from harm to competition. However, the Competition Tribunal determined that absent a meaningful economic justification for the use of such discounts, they could be condemned if their structure makes it more difficult for competitors to compete on the merits. The Competition Tribunal emphasised that the illegality of such discounts, in such cases, can be determined without the need to assess the level of market foreclosure or the actual impact on competition. As regards the economic methodology that will be used to assess the potential harm to competition on the merits, the Competition Tribunal mentioned several approaches that were explored by the EU courts and the EU Competition Commission. The Competition Tribunal concluded that there is no single economic test that should be exclusively applied and rejected the use of the 'equally efficient competitor' test as the ultimate indicator on which such discounts should be judged (seemingly taking a stricter approach than the ICA's 2005 position, which used this test as the underlying principle).

The Competition Tribunal referred to several indications which could affect the legitimacy of a target discount pricing scheme, all of which existed in Ashdod Port's plan:

- individuality – if the discount is tailored to each customer's demand, the probability is that it is aimed at locking the customer to the monopoly increases;
- retroactivity – if the discount is offered retroactively (ie, applied from the 'first unit'), it provides incentive for customers to allocate as much demand as possible to the monopolist in order to reach the target; and
- secrecy – if the agreement with the customer includes a confidentiality provision, such that the customer cannot present to third parties the target discounts offered by the monopolist, it will be harder for competitors to counter the monopoly's offer.

## Comment

The Competition Tribunal's judgment adopted a strict approach to the competitive analysis of retroactive target discounts, determining that absent a significant economic justification, such discounts can be banned strictly based on their structure, without a need for substantive market assessment. The ruling could be misinterpreted as suggesting a quasi *per se* prohibition on target discounts, but a more careful reading shows that the Competition Tribunal's decision was anchored in the specifics of the case as these were described by the court – an individual, retroactive and secret target discount plan that encompassed the vast majority of the customer's annual demand, the purpose of which was to stifle competition. The Competition Tribunal's requirement to prohibit a target discount – that its structure is liable to harm competition on the merits – calls for a case-by-case assessment of the structure's potential impact on competition. While not necessarily equivalent to a rule of reason assessment, it is by no means a quasi *per se* prohibition on target pricing either.

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