Monopolization: Anticompetitive Conduct

Antitrust
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Monopolization elements

(1) monopoly power in a relevant market

(2) anticompetitive conduct

a/k/a "exclusionary conduct," "predatory conduct," "monopoly conduct"

Monopolization elements

Re-run

"The offense of monopol[ization] under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in [a] relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."

United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966)

Monopolization elements

anticompetitive conduct →

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United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966)

ANTICOMPETITIVE CONDUCT

What counts as anticompetitive conduct?

From *Grinnell*:

"the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident"

ANTICOMPETITIVE CONDUCT

What counts as anticompetitive conduct?

- Must look to economic realities of the situation.
- Must be injury to competition. Injury to competitors is not enough.
- Note: Charging monopoly prices is not anticompetitive conduct! (In fact, it's often the opposite.)

ANTICOMPETITIVE CONDUCT

What counts as anticompetitive conduct?

"In short, under U.S. law, a monopolist's unilateral conduct is governed by the same rule of reason to judge whether it is anticompetitive as is concerted action by firms that lack monopoly power or any reasonable probability of acquiring it."

"General standards ... provide little guidance. To get a concrete sense of what conduct is deemed anticompetitive, one needs to examine the standards used to evaluate specific conduct."

– Elhauge 3d. ed., p. 276-277.

ANTICOMPETITIVE CONDUCT

Intent requirement

Some intent is required, but only objective intent that can be inferred from actions. A purposeful act is required, but there is no need to show a specific, subjective intent to monopolize. "Moral wrong" on the part of the defendant is not required. *But* malicious intent can be evidence of the anticompetitive nature of the conduct.

I/o/w, evidence of subjective intent is not necessary to prove a § 2 claim, but if available, it can definitely help the plaintiff.

“Defendant having willed the means, has willed the end.”

– Judge Charles Edward Wyzanski, Jr. in *U.S. v. United Shoe*, 110 F.Supp. 295 (D. Mass 1953)

Some specific examples of anticompetitive conduct (1/3)

- **Predatory pricing** (Brooke Group)
- **Refusals to deal with competitors** (Aspen Skiing)
- **Refusals to deal with those who deal with competitors** (Lorain Journal)
- **Denial of access to an essential facility** (Otter Tail)

Some specific examples of anticompetitive conduct (2/3)

- **Coercing a competitor's suppliers/partners** (Standard Oil, Microsoft)
- **Acquisition and retirement of assets** (American Tobacco)
- **Acquisitions of competitors** (Standard Oil)

Some specific examples of anticompetitive conduct (3/3)

- **Preventing formation of second-hand market** (United Shoe)
- **Tying arrangements** (United Shoe, Microsoft)
- **Setting and controlling standards** (Microsoft)
- **Raising competitor's costs**
- **Loyalty discounts**
- **Bundled loyalty discounts**

Fallacious arguments sometimes asserted by defendants:

- Illusory choice
  - example: maybe you don't have to buy the maintenance with the machine, but the price is the same
- Evils of competition
  - "competition will be ruinous," etc.

A couple of fantastic quotes from United Shoe

“[I]t is delusive to treat opinions written by different judges at different times as pieces of a jig-saw puzzle which can be, by effort, fitted correctly into a single pattern.” – Judge Charles Edward Wyzanski, Jr. in *U.S. v. United Shoe*, 110 F.Supp. 295 (D. Mass 1953)

"[O]ne of the dangers of extraordinary experience is that those who have it may fall into grooves created by their own expertness. They refuse to believe that hurdles which they have learned from experience are insurmountable, can in fact be overcome by fresh, independent minds." – Judge Charles Edward Wyzanski, Jr. in *U.S. v. United Shoe*, 110 F.Supp. 295 (D. Mass 1953)

The three principal sources of United's power have been the original constitution of the company, the superi[illegible]ity of United's products and services, and the le[illegible] two of these are plainly b[illegible]s not rest solely on its c[illegible], or its economies of scale. T[illegible]d these barriers were erected b[illegible] policies. Much of United's market power is tra[illegible] to the magnetic ties inherent in its system of leasing, and not selling, its more important machines. The lease-only system of distributing complicated machines has many 'partnership' aspects, and it has exclusionary features such as the 10-year term, the full capacity clause, the return charges, and the failure to segregate service charges from machine charges. Moreover, the leasing system has aided United in maintaining a pricing system which discriminates between machine types.

In addition to the foregoing three principal sources of United's power, brief reference may be made to the fact that United has been somewhat aided in retaining control of the shoe machinery industry by its purchases in the secondhand market, by its acquisitions of patents, and to a lesser extent, by its activities in selling to shoe factories supplies which United and others manufacture.

Here's a big quote from the case. Let's rework it into an outline of the anticompetitive features …

The three principal sources of United's power have been the original constitution of the company, the superiority of United's products and services, and the leasing system. The first two of these are plainly beyond reproach.~ But United's control does not rest solely on its original constitution, its ability, its research, or its economies of scale. There are other barriers to competition, and these barriers were erected by United's own business policies. Much of United's market power is traceable to the magnetic ties inherent in its system of leasing, and not selling, its more important machines. The lease-only system of distributing complicated machines has many 'partnership' aspects, and it has exclusionary features such as the 10-year term, the full capacity clause, the return charges, and the failure to segregate service charges from machine charges. Moreover, the leasing system has aided United in maintaining a pricing system which discriminates between machine types.

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The three principal sources of United's power have been

- the original constitution of the company, ← okay
- the superiority of United's products and services, and ← okay
- the leasing system. ← problematic

The lease-only system of distributing complicated machines has many ... has exclusionary features such as:

- the 10-year term,
    - *keeps customers from trying a competitor*
- the full capacity clause,
    - *keeps customers from trying a competitor*
- the return charges, and
    - *keeps customers from trying a competitor*
- the failure to segregate service charges from machine charges.
    - *competitors need to provide maintenance to enter the market, because there's no existing market*
    - *prevents the creation of expertise in people and firms outside of United Shoes' control that could evolve into competitors*
- *[prevents the sale of used machines*
    - *prevents another way for a firm to move toward market entry in evolutionary steps]*

In addition to the foregoing three principal sources of United's power:

- [acquisitions:] purchases in the secondhand market, by its acquisitions of patents,

ANTICOMPETITIVE CONDUCT

Predatory pricing

To count as anticompetitive conduct under § 2:

1. The conduct must discipline or eliminate a competitor
2. Defendant's prices must be below an appropriate measure of defendant's costs
   - it's not enough for prices to be below market
   - it's not enough for prices to be below competitors' costs
3. Defendant must have a dangerous probability of recoupment
   - "The inquiry is whether, given the aggregate losses caused by the below-cost pricing, the intended target would likely succumb."
   - Court must assess extent and duration of predation, relative financial strengths of predator and victim, their incentives and will, the capacity of defendant to absorb rival's market share, and the condition of the market incl. ease of new entry

     (*Brooke Group v. Brown & Williamson*)

L&M LIGHTS

BROWN & WILLIAMSON TOBACCO

Predatory pricing

ANTICOMPETITIVE CONDUCT

Brooke Group v. Brown & Williamson, 509 U.S. 940 (1993):

For a predatory pricing claim under § 2 of the Sherman Act, there are two prerequisites:

First, plaintiff must prove that the complained-of prices are below an appropriate measure of its rival's costs.

In Brooke Group, the court used average variable cost because the parties stipulated to it.

"[W]e have rejected elsewhere the notion that above-cost prices that are below general market levels or the costs of a firm's competitors inflict injury to competition cognizable under the antitrust laws."

"As a general rule, the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting."

Predatory pricing

ANTICOMPETITIVE CONDUCT

Brooke Group v. Brown & Williamson, 509 U.S. 940 (1993):

Second, plaintiff must demonstrate "that the competitor had … a dangerous probability, of recouping its investment in below-cost prices."

"For the investment to be rational, the [predator] must have a reasonable expectation of recovering, in the form of later monopoly profits, more than the losses suffered."

"Recoupment is the ultimate object of an unlawful predatory pricing scheme; it is the means by which a predator profits from predation. Without it, predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced. Although unsuccessful predatory pricing may encourage some inefficient substitution toward the product being sold at less than its cost, unsuccessful predation is in general a boon to consumers."

Predatory pricing

ANTICOMPETITIVE CONDUCT

Brooke Group v. Brown & Williamson, 509 U.S. 940 (1993):

"That below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured: It is axiomatic that the antitrust laws were passed for 'the protection of competition, not competitors.'"

"For recoupment to occur, below-cost pricing must be capable, as a threshold matter, of producing the intended effects on the firm's rivals, whether driving them from the market, or ... causing them to raise their prices to supracompetitive levels within a disciplined oligopoly. This requires an understanding of the extent and duration of the alleged predation, the relative financial strength of the predator and its intended victim, and their respective incentives and will. ... The inquiry is whether, given the aggregate losses caused by the below-cost pricing, the intended target would likely succumb.

Predatory pricing

ANTICOMPETITIVE CONDUCT

Brooke Group v. Brown & Williamson, 509 U.S. 940 (1993):

"If circumstances indicate that below-cost pricing could likely produce its intended effect on the target, there is still the further question whether it would likely injure competition in the relevant market. The plaintiff must demonstrate that there is a likelihood that the predatory scheme alleged would cause a rise in prices above a competitive level that would be sufficient to compensate for the amounts expended on the predation, including the time value of the money invested in it. As we have observed on a prior occasion, '[i]n order to recoup their losses, [predators] must obtain enough market power to set higher than competitive prices, and then must sustain those prices long enough to earn in excess profits what they earlier gave up in below-cost prices.'"

ANTICOMPETITIVE CONDUCT

Predatory pricing

Brooke Group v. Brown & Williamson, 509 U.S. 940 (1993):

"These prerequisites to recovery are not easy to establish, but they are not artificial obstacles to recovery; rather, they are essential components of real market injury. As we have said in the Sherman Act context, 'predatory pricing schemes are rarely tried, and even more rarely successful,' and the costs of an erroneous finding of liability are high. '[T]he mechanism by which a firm engages in predatory pricing—lowering prices—is the same mechanism by which a firm stimulates competition; because "cutting prices in order to increase business often is the very essence of competition ...[;] mistaken inferences ... are especially costly, because they chill the very conduct the antitrust laws are designed to protect."' It would be ironic indeed if the standards for predatory pricing liability were so low that antitrust suits themselves became a tool for keeping prices high."

ANTICOMPETITIVE CONDUCT

Predatory pricing

To count as anticompetitive conduct under § 2:

1. The conduct must discipline or eliminate a competitor
2. Defendant's prices must be below an appropriate measure of defendant's costs *[← Brooke Group's 1st prerequisite]*
   - it's not enough for prices to be below market
   - it's not enough for prices to be below competitors' costs
3. Defendant must have a dangerous probability of recoupment *[← Brooke Group's 2nd prerequisite]*
   - "The inquiry is whether, given the aggregate losses caused by the below-cost pricing, the intended target would likely succumb."
   - Court must assess extent and duration of predation, relative financial strengths of predator and victim, their incentives and will, the capacity of defendant to absorb rival's market share, and the condition of the market incl. ease of new entry

(*Brooke Group v. Brown & Williamson*)

ANTICOMPETITIVE CONDUCT

Predatory pricing

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(*Brooke Group v. Brown & Williamson*)

←This is commonly average variable costs (AVC), functioning as a proxy for marginal costs (MC).

HexOil and Aunt Glenda's Gas

In Verdant Valley, a town of 50,000 people that is a three-hour drive from any other town, there are 12 gas stations, all owned by multi-billion-dollar behemoth HexOil. HexOil's average variable costs are $1.00/gallon, and it sells retail for $4.59/gallon. Independent Aunt Glenda's Gas pops up, with costs at $1.50/gallon, and starts selling at $4.00/gallon. HexOil lowers its price. Then Aunt Glenda does, all the way to $1.51/gallon. Then HexOil goes down to $1.21/gallon, and it keeps that price for six months until Aunt Glenda goes out of business. Then it jacks prices back up to $4.59.

Is HexOil liable for monopolization?

HexOil and Aunt Glenda's Gas
Analysis 1/2

The first element is monopoly power. Gasoline seems like a relevant product market because there are no reasonable substitutes for people with regular gas-powered cars. Verdant Valley is a relevant geographic market because gas stations three hours away aren't a reasonable substitute. HexOil has 100% market share, which is, of course, monopoly level. There are plausibly barriers to entry because gas stations involve large start up costs and, plausibly, the predatory behavior of HexOil is giving such an investment poor prospects (so getting financing could be unlikely).

HexOil and Aunt Glenda's Gas
Analysis 2/2

The second element is anticompetitive conduct. Here, the theory is predatory pricing. This first requirement appears to be satisfied because Aunt Glenda's was eliminated as a competitor. The second requirement is that the defendant's prices have to be below an appropriate measure of costs. Average variable costs are accepted as an appropriate measure. Here, HexOil's AVC is $1.00/gallon. HexOil's lowest alleged predatory price is $1.21/gallon, which is above AVC. So this claim fails the first prong of Brooke Group. It does not matter that this was below Aunt Glenda's Gas's costs at $1.50/gallon. Thus, no § 2 monopolization claim is stated.

HexOil and Aunt Glenda's Gas

In Verdant Valley, a town of 50,000 people that is a three-hour drive from any other town, there are 12 gas stations, all owned by multi-billion-dollar behemoth HexOil. HexOil's marginal costs are $1.00/gallon, and it sells retail for $4.59/gallon. Independent Aunt Glenda's Gas pops up, with costs at $1... elling at $4... Then Aunt Gl... way to $1.51/gallon. Then HexOil goes down to $0.90/gallon, and it keeps that price for four months until Aunt Glenda goes out of business. Then it jacks prices back up to $4.59.

Is HexOil liable for monopolization?

Let's change the facts …

HexOil and Aunt Glenda's Gas

In Verdant Valley, a town of 50,000 people that is a three-hour drive from any other town, there are 12 gas stations, all owned by multi-billion-dollar behemoth HexOil. HexOil's marginal costs are $1.00/gallon, and it sells retail for $4.59/gallon. Independent Aunt Glenda's Gas pops up, with costs at $1.50/gallon, and starts selling at $4.00/gallon. HexOil lowers its price. Then Aunt Glenda does, all the way to $1.51/gallon. Then HexOil goes down to $0.90/gallon, and it keeps that price for four months until Aunt Glenda goes out of business. Then it jacks prices back up to $4.59.

Is HexOil liable for monopolization?

HexOil and Aunt Glenda's Gas (variation)

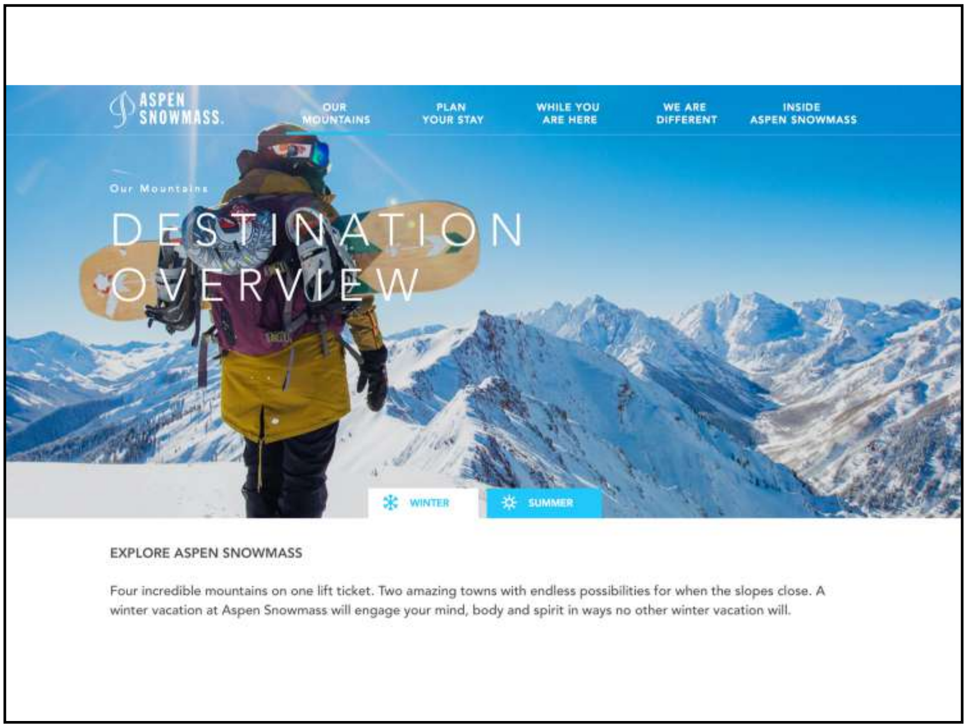
Analysis

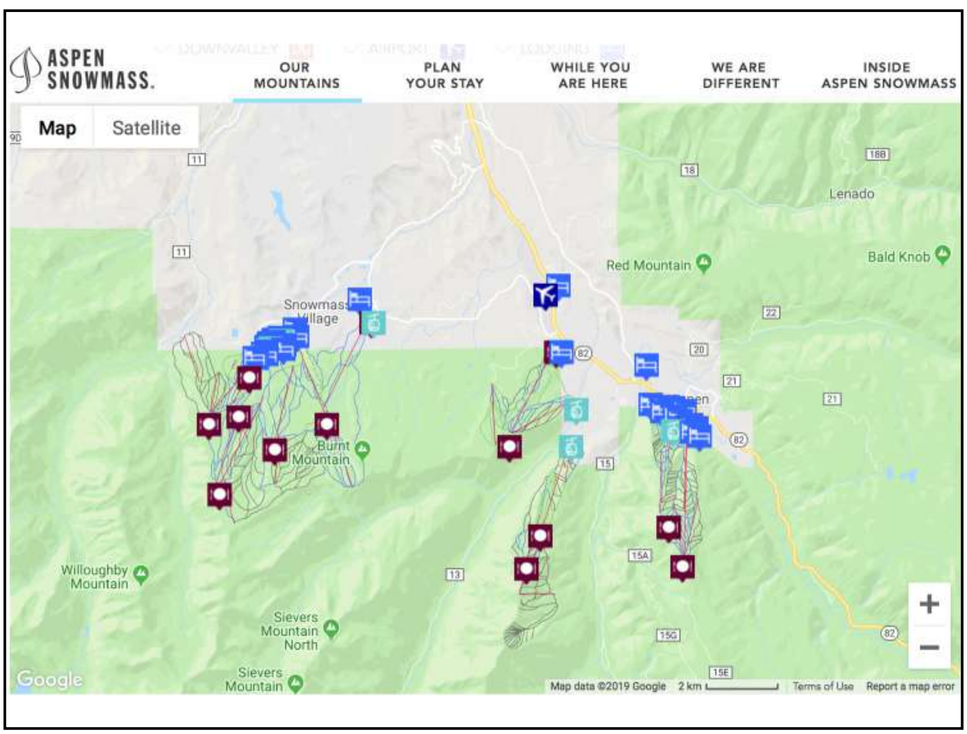
The first element, monopoly power, is the same.

The second element, anticompetitive conduct, depends on a predatory pricing theory. The first requirement appears to be satisfied because Aunt Glenda's was eliminated as a competitor. The second requirement is met here, because 90¢/gallon is below HexOil's marginal cost (which, like AVC, is an appropriate measure of cost) at $1/gallon.

The third element seems met. HexOil seems to have have had a dangerous probability of recoupment because they drove Aunt Glenda's out of the market in four months and jacked prices back up to $4.59, which seems like it should quickly pay back their investment in predatory pricing.

ASPEN SKIING COMPANY


ASPEN SNOWMASS.
OUR MOUNTAINS
PLAN YOUR STAY
WHILE YOU ARE HERE
WE ARE DIFFERENT
INSIDE ASPEN SNOWMASS
Our Mountains
DESTINATION OVERVIEW
WINTER
SUMMER
EXPLORE ASPEN SNOWMASS
Four incredible mountains on one lift ticket. Two amazing towns with endless possibilities for when the slopes close. A winter vacation at Aspen Snowmass will engage your mind, body and spirit in ways no other winter vacation will.


ASPEN SNOWMASS.
OUR MOUNTAINS
PLAN YOUR STAY
WHILE YOU ARE HERE
WE ARE DIFFERENT
INSIDE ASPEN SNOWMASS
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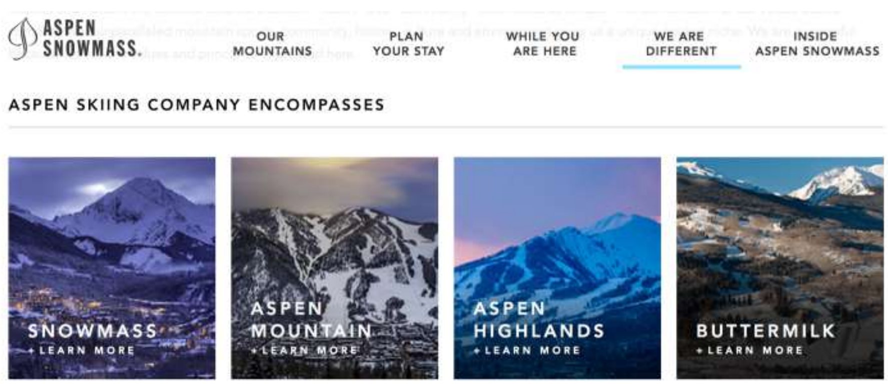

ANTICOMPETITIVE CONDUCT

Aspen Skiing

filled out interactively in class

What's the biggest obstacle to Highlands' case?

- All they did was not cooperate with a competitor! Isn't that their choice! And isn't cooperating with competitors even sus under Sherman Act § 1! Freedom of choice, man! This is America! (paraphrased, obvs)

What does Highlands have going for it?

- Demonstrated consumer preferences for the six-day all mountain
- Not novel – it's something that existed previously
- Highlands lost a lot of market share since Aspen did this
- Took choices away from consumers
- Per day average of six-day Aspen pass being below single-day price locks consumers out of Highlands – skiing there is no longer sensible as a choice
- Defendant was doing the same sort of six-day deals with competitors in other markets that it claimed was so distasteful with Highlands.
- Their claims about the awkwardness/problematic nature of monitoring were belied by their own internal monitoring that they apparently found satisfactory
- Defendant wouldn't sell to Highlands even at full retail prices
- They wouldn't accept money on account at Aspen banks
- There doesn't seem to be any legitimate business reason for defendant's conduct
- Relatedly, defendant offered no efficiency justification for its conduct (p.331, ¶3)

WEATHER

THE LORAIN JOURNAL

And The Lorain Times-Herald

FINAL EDITION

LORAIN, OHIO, WEDNESDAY, SEPT. 22, 1948

PRICE FIVE CENTS

FIRE WRECKS BRUSH BERYLLIUM PLANT; LOSS SET AT $350,000

RUSSIAN QUESTION DELAYED

Big Three Holds Off On Asking U. N. Aid In Berlin Crisis

MAP FINAL MOVE

French Sources Report Soviets to Be Given One More Week

General View as Flames Engulfed Brush Beryllium Plant

MAGNESIUM LIGHTS UP ENTIRE AREA, DRAWS THOUSANDS

Series of Blasts Blamed on Bursting Oxygen Tanks; Company Plans To Rebuild; Use of Explosive Chemicals Denied

DISMISS CHARGE ON SOUND TRUCK

Elyria Mayor's Verdict Upholds Labor Leader

FIRST BANK OF RURAL KANBRASKA

First Bank of Rural Kanbraska

Hypo: Family-owned First Bank of Rural Kanbraska has been the only bank in the small rural town of Oak Corner for more than a century. When a new bank opens up, First Bank sends them a relentless stream of black faxes to run down their toner supply, tells local businesses they will delay clearing checks for any firm opening an account at the new bank, and tells individual customers they can't have accounts at both banks. Eventually, the new bank gives up and leaves town. ***Has First Bank engaged in anticompetitive conduct?***

(This is for discussion in class … There's no pre-prepared answer slide.)

Verizon v. Trinko

ANTICOMPETITIVE CONDUCT

In what ways does the *Verizon v. Trinko* case express reservations about antitrust claims in this area?

- The court thinks where there is a regulatory scheme, it's better for the agency to sort this out according to that scheme than get the generalist courts to mess with it using general antitrust law.
- References to "central planners"
- Talk in terms of an unwillingness to create new "exceptions," of which Aspen Skiing is depicted as one
- P. 339 Section III Paragraph 2: "[A]s a general matter, the Sherman Act 'does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.'"
- Providing remedies of forcing people to deal gets us close to something that seems akin to "collusion," which is "the supreme evil of antitrust"
- worries about false positives
- "The mere possession of monopoly power is not only not unlawful; it is an important element of the free-market system"

filled out interactively in class

Verizon v. Trinko

ANTICOMPETITIVE CONDUCT

filled out interactively in class

What are differences between plaintiff Highlands in *Aspen Skiing* and alleged victims in this case? (Or, more generally, key differences in the facts ...)

- In Aspen, there was NO federal regulation that had already intervened and there WAS a deal in the past that clearly produced the best result for consumers (established expectations, market-created solutions)
- In Aspen, there was a unilateral termination of a voluntary course of dealing, which suggested a willingness to forsake short-term profits to achieve an anticompetitive end. Here, the complaint didn't allege that Verizon voluntarily engaged in dealing with rivals.
- Here the services were not otherwise offered to the public. "The unbundled elements offered …. exist only deep within the bowels of Verizon...."
- Aspen involved refusal to sell at *retail* prices. That was not the case here.
- The plaintiff Highlands was fighting for its survival as the main victim of the anticompetitive conduct. Trinko is a law firm that's leading a class action – the stakes for Trinko are personally much lower.