



Vertical Restraints Part 3 (Loyalty and Bundled Discounts)

Antitrust
Eric E. Johnson
ericejohnson.com



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LePage's v. 3M

(3d. Cir. 2003 en banc)

Pittsburgh-based 127-year-old LePage's claimed 3M was trying to run it out of business with exclusive contracts and bundled loyalty rebates.



LePage's v. 3M

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Pittsburgh-based 127-year-old LePage's claimed 3M was trying to run it out of business with exclusive contracts and bundled loyalty rebates.

This case is in the casebook, if you want to reference it. But I put the key parts in this slide show for us to do in story-time fashion ...



Changes in the market, allegations ...

Distribution patterns and consumer acceptance accounted for a shift of some tape sales from brand-name tape to private label (a/k/a “store brand”) tape. With the rapid growth of office superstores, such as Staples and Office Depot, and mass merchandisers, such as Wal-Mart and Kmart, distribution patterns for second brand (a/k/a “discount brand”) and private label tape changed as many of the large retailers wanted to use their own brand names to sell stationery products, including transparent tape. 3M also entered the private label business during the early 1990s and sold its own second brand under the name “Highland.”

This text in these slides is taken directly from the case, lightly edited.

LePage's claims that, in response to the growth of this competitive market, 3M engaged in a series of related anticompetitive acts aimed at restricting the availability of lower-priced transparent tape to consumers. It also claims that 3M devised programs that prevented LePage's and the other domestic company in the business, Tesa Tuck, from gaining or maintaining large volume sales and that 3M maintained its monopoly by stifling growth of private label tape and by coordinating efforts aimed at large distributors to keep retail prices for Scotch tape high.

An example of what happened to LePage's in the 1990s:

Before 1992, Wal-Mart bought private label tape only from LePage's but, in August 1992, decided to buy private label tape from 3M as well. In response, LePage's lowered its prices and increased its sales to Wal-Mart. In 1997, Wal-Mart stopped buying private label tape but offered LePage's's branded tape as its "second tier" offering. In 1998, however, Wal-Mart told LePage's that it was going to switch to a tape program from 3M. Wal-Mart drastically cut back their purchases.

Is there a § 2 claim here?

Where do we start the analysis?

Monopolization analysis to-do list Re-run

- (1) monopoly power in a relevant market
 1. figure out a relevant product market
 2. figure out a relevant geographical market
 3. look at the market share
 4. consider barriers to entry
 5. consider whether future capacity constraints, changing consumer demand, or demand elasticity might let an alleged monopolist off the hook
- (2) anticompetitive conduct
[for this analysis, you'll use what we cover next ...]

Is there a § 2 claim here?

Where do we start the analysis?

§ 2 element 1 analysis: monopoly power

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monopoly power

????

Can you brainstorm some guesses based on having seen tape in the store and having purchased it?

§ 2 element 1 analysis:
monopoly power

In this case, the parties agreed that the relevant product market is transparent tape and the relevant geographic market is the United States. Moreover, as to the issue of monopoly power, 3M concedes it possesses monopoly power in the United States transparent tape market with a 90% market share. In fact, the evidence showed that the household penetration of 3M's Scotch-brand tape is virtually 100%.

[And ...] there was no ease of entry [into the transparent tape market.

Monopoly-level market share

Re-run

The law doesn't say exactly what market share constitutes monopoly power (MP), but some flags have been planted by various courts:

- 90% is enough for MP (L. Hand, J., in *Alcoa*)
- 87% "leaves no doubt" that MP exists
- 80-95% is enough for Π to survive sum. j'ment on MP
- 75% means MP "may be assumed"
- min. 70-80% is what lower courts "generally require"
- >66% might be MP
- 60-64% is doubtful for MP (L. Hand, J., in *Alcoa*)
- 50% is the bare minimum for MP for many lower courts
- 30% is insufficient even for \S 1 market power

(from p.21 of DOJ'08 report; p. 226 of Elhauge, 3d ed.)

Is there a \S 2 claim here?

Where do we start the analysis?

\S 2 element 1 analysis: monopoly power

What's next in the analysis?

\S 2 element 2 analysis: exclusionary 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.)

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- Note: Charging monopoly prices is not anticompetitive conduct! (In fact, it's often the opposite.)

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)**

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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**

Some specific examples of anticompetitive conduct (3/3)

- Preventing formation of second-hand market (United Shoe)
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- **Raising competitor's costs**
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- **Bundled loyalty discounts**

§ 2 element 2 analysis: exclusionary conduct

LePage's argues that 3M willfully maintained its monopoly in the transparent tape market through exclusionary conduct, primarily by bundling its rebates and entering into contracts that expressly or effectively required dealing virtually exclusively with 3M, which LePage's characterizes as de facto exclusive. 3M does not argue that it did not engage in this conduct. It agrees that it offered bundled rebates and entered into some exclusive dealing contracts, although it argues that only the few contracts that are expressly exclusive may be considered as such. Instead, 3M argues that its conduct was legal as a matter of law because it never priced its transparent tape below its cost.

getting into the facts ...

The rebates were considerable, not "modest" as 3M states. For example, Kmart, which had constituted 10% of LePage's business, received \$926,287 in 1997. And in 1996 Wal-Mart received more than \$1.5 million, Sam's Club received \$666,620, and Target received \$482,001. Just as significant as the amounts received is the powerful incentive they provided to customers to purchase 3M tape rather than LePage's in order to get the maximum rebate 3M offered. The penalty would have been \$264,000 for Sam's Club, \$450,000 for Kmart, and \$200,000 to \$310,000 for American Stores.

3M does not deny that it offered these programs. As it responds to each of LePage's allegations, it returns to its central premise "that it is not unlawful to lower one's prices so long as they remain above cost." (citing *Brooke Group*). However, one of the leading treatises discussing the inherent anticompetitive effect of bundled rebates, even if they are priced above cost, notes that "the great majority of bundled rebate programs yield aggregate prices above cost. Rather than analogizing them to predatory pricing, they are best compared with tying, whose foreclosure effects are similar. Indeed, the 'package discount' is often a close analogy."



LePage's introduced powerful evidence that rebates and discounts to Kmart, Staples, Sam's Club, and others were designed to induce them to award business to 3M to the exclusion of LePage's. Many of LePage's former customers refused even to meet with LePage's sales representatives.



A buyer for Kmart, LePage's largest customer which accounted for 10% of its business, told LePage's: "I can't talk to you about tape products for the next three years" and "don't bring me anything [that's competitive with what] 3M makes."

Kmart switched to 3M following 3M's offer of a \$1 million "growth" reward which could be understood to require that 3M be its sole supplier. Similarly, Staples was offered an extra 1% bonus rebate if it gave LePage's business to 3M. 3M argues that LePage's did not try hard enough to retain Kmart, its customer for 20 years, but there was evidence to the contrary.

Prior to the introduction of 3M's rebate program, LePage's sales had been skyrocketing. Its sales to Staples increased by 440% from 1990 to 1993.

Following the introduction of 3M's rebate program which bundled its private-label tape with its other products, 3M's private-label tape sales increased 478% from 1992 to 1997. LePage's in turn lost a proportional amount of sales. It lost key large volume customers, such as Kmart, Staples, American Drugstores, Office Max, and Sam's Club. Other large customers, like Wal-Mart, drastically cut back their purchases. As a result, LePage's manufacturing process became less efficient and its profit margins declined.

In transparent tape manufacturing, large volume customers are essential to achieving efficiencies of scale. As 3M concedes, "'large customers were extremely important to [LePage's], to everyone.' . . . Large volumes . . . permitted 'long runs,' making the manufacturing process more economical and predictable."



There was a comparable effect on LePage's share of the transparent tape market. In the agreed upon relevant market for transparent tape in the United States, LePage's market share dropped 35% from 1992 to 1997.

In 1992, LePage's net sales constituted 14.44% of the total transparent tape market. By 1997, LePage's sales had fallen to 9.35%. Finally, in March of 1997, LePage's was forced to close one of its two plants. That same year, the only other domestic transparent tape manufacturer, Tesa Tuck, Inc., bowed out of the transparent tape business entirely in the United States.

Had 3M continued with its program it could have eventually forced LePage's out of the market.

3M could effectuate such a plan because there was no ease of entry.

There was evidence from which the jury could have determined that 3M intended to force LePage's from the market, and then cease or severely curtail its own private-label and second-tier tape lines. For example, by 1996, 3M had begun to offer incentives to some customers to increase purchases of its higher priced Scotch-brand tapes over its own second-tier brand.

Black letter law

When a monopolist's actions are designed to prevent one or more new or potential competitors from gaining a foothold in the market by exclusionary, i.e. predatory, conduct, its success in that goal is not only injurious to the potential competitor but also to competition in general.

The result

There is considerable evidence in the record that 3M entered the private-label market only to "kill it." A 3M executive in internal memorandum stated that "I don't want private label 3M products to be successful in the office supply business, its distribution or our consumers/end users").

That is precisely what § 2 of the Sherman Act prohibits.

The rest of the story ...

From a news report:

A jury verdict resulted in an order for 3M to pay LePage's \$68 million in damages plus attorneys fees.

The victory came just in the nick of time. "We were all going to be out of jobs," said CEO Gary Dean. "That was coming very soon."

In 2021, LePage's continues to exist.



