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Predatory Pricing Law in the United States and Canada

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PREDATORY PRICING LAW IN THE UNITED STATES AND CANADA

NORMAN W. HAWKER*

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I. INTRODUCTION

Over the past twenty years, trade between the United States and Canada has grown from just under \$58 billion¹ to over \$322 billion per year.² Beginning with the Canada-United States Free Trade Agreement in the 1980's³ and

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¹ See U.S. Department of Commerce, Survey of Current Business, Dec. 1977, at 32.

² See U.S. Department of Commerce, Survey of Current Business, Apr. 1998, at 80, 81.

³ See generally, J. Timothy Kennish, Competition Issues Arising from Free Trade—A Canadian Practitioner's Perspective (1988).

continuing into the 1990's with the North American Free Trade Agreement ("NAFTA"),⁴ the United States and Canada have sought to increase the already large volume of trade between the two countries. As trade between the United States and Canada increases, it becomes increasingly important to understand each other's domestic laws,⁵ including antitrust law.⁶ Not surprisingly, the increase in trade has brought with it an increase in transborder antitrust enforcement activity.⁷

An examination of Canadian predatory pricing law is justified not only by the volume of trade between the United States and Canada, but also by the treaties and agreements between the two countries that call for cooperation in the enforcement of antitrust law. As one commentator noted, "effective antitrust enforcement goes hand in hand with the lowering of governmental barriers in achieving open and competitive markets,"⁸ and promotion of "fair competition" is one of NAFTA's express objectives.⁹ NAFTA requires the signatories to adopt their antitrust laws,¹⁰ but it does not specify a basis for harmonizing their antitrust policies.¹¹ Instead, NAFTA requires *cooperation*

⁴ The North American Free Trade Agreement is reprinted at James R. Holbein & Donald J. Musch, *The Practitioner's Deskbook Series: NAFTA 105-939* (1994).

⁵ See Paul Collins & D. Jeffrey Brown, *National Antitrust Laws in a Continental Economy: A Comparison of Canadian and American Antitrust Laws*, 65 ANTITRUST L.J. 495, 534 (1997) ("The increasing level of economic integration... between Canada and the United States... demands a certain cognizance respecting the application of the laws of the country in which an entity carries on its business.")

⁶ Stephen F. Ross, *Antitrust Lessons from "The True North Strong and Free"*, 65 ANTITRUST L.J. 467, 492 (1997) ("Expanding trade between the United States and Canada makes knowledge of the competition laws of our northern neighbors vital to antitrust practitioners and scholars.")

⁷ Charles S. Stark, *International Antitrust Cooperation in NAFTA: The International Antitrust Assistance Act of 1994*, 4 UNITED STATES—MEXICO L.J. 169, 173-74 (1996).

⁸ *Id.* at 169.

⁹ NAFTA Art. 102(b).

¹⁰ NAFTA Art. 1501(1) ("Each Party shall adopt or maintain measures to proscribe anti-competitive business conduct and take appropriate action with respect thereto.") This is consistent with the United States' policy of treating antitrust law as a matter of domestic policy. Spencer Weber Waller, *National Laws and International Markets: Strategies of Cooperation and Harmonization in the Enforcement of Competition Law*, 18 CARDOZO L. REV. 1111, 1118 (1996) ("The United States has staked its policy for the foreseeable future on [international] cooperation as an alternative to either unilateralism, harmonization, or the creation of a true international antitrust law. ... Enforcement plus cooperation maintains our commitment to antitrust as an important dimension of this country's legal and civic system... Harmonization and true international antitrust would only weaken national power, ultimately require externally driven change in doctrine and procedure, and expose U.S. firms to majoritarian international controls that have been historically unacceptable.") Note that this stands in contrast to the European Union which has a body antitrust law subscribed to by all its members. Kathleen Murtaugh Collins, *Harmonizing the Antitrust Laws of NAFTA Signatories*, 17 LOY. L.A. INT'L & COMP. L.J. 157, 158 (1994).

¹¹ Mark R. Joelson, *Antitrust/Competition Law Aspects of NAFTA*, 40 FED. B. NEWS & J. 573 (1993) ("The reader who plunges into the provisions of the proposed North American Free Trade Agreement... in the expectation of finding a well developed set of competition or antitrust law principles

in the enforcement of each country's domestic antitrust laws.¹² NAFTA also establishes a Working Group on Trade Competition with a mandate to make recommendations "on relevant issues concerning the relationship between competition laws and policies and trade."¹³ A variety of other agreements between the United States and Canada pledge cooperation in the enforcement of antitrust laws supplement NAFTA's provisions.¹⁴ In an effort to facilitate further agreements, Congress enacted the International Antitrust Assistance Act of 1994.¹⁵

Furthermore, the Canadian approach to antitrust law may offer the United States a viable alternative to the approach offered by the dominant "Chicago School."¹⁶ Antitrust law in the United States has entered a period of reassessment. Although the United States Supreme Court continues to rely heavily on Chicago School analysis and scholarship,¹⁷ other policy makers and legal scholars have begun to abandon Chicago's monomaniacal focus on economic efficiency. For example, Gerla has sought to restore rivalry as the central tenet of antitrust law.¹⁸ Averitt and Lande have proposed a "consumer sovereignty" model for antitrust law that emphasizes the existence of consumer choices.¹⁹ Nader has urged an antitrust policy that focuses on concentration and wealth transfers rather than economic efficiency.²⁰ Even

will be disappointed"). Indeed, NAFTA even denies the signatories "recourse to dispute settlement under this Agreement for any [antitrust] matter." NAFTA Art. 1501(3).

¹² NAFTA Art. 1501(2) ("The Parties shall cooperate on issues of competition law enforcement policy.").

¹³ NAFTA Art. 1504.

¹⁴ For an overview of these agreements through the summer of 1995, see Stark, *supra* note 7, at 170-73.

¹⁵ International Antitrust Enforcement Assistance Act of 1994, 15 U.S.C. §§ 6201-6212 (1994).

Talks between the United States and Canada quickly followed the enactment of the IAEEA. Waller, *supra* note 10, at 1118. It appears, however, that the first IAEEA agreement will be with Australia, not Canada. U.S., *Australia Propose First-Ever Mutual Antitrust Assistance Agreement*, 72 Antitrust & Trade Reg. Rep. (BNA) 386 (1997).

¹⁶ Christopher J. Maule & Thomas W. Ross, *Canada's New Competition Policy*, 23 GEO. WASH. J. INT'L L. & ECON. 59, 62 (1989) ("Given the structural similarities between the Canadian and U.S. economies, it seems likely that any Canadian success could be readily transferable south of the Canadian border.").

¹⁷ See, e.g., *State Oil Co. v. Khan*, 118 S.Ct. 275, 282 (1997) (Court explicitly relied on Posner and Bork to support its conclusion that "vertically imposed maximum prices" cannot "harm consumers or competition.").

¹⁸ Harry S. Gerla, *Restoring Rivalry As a Central Concept in Antitrust Law*, 75 NEB. L. REV. 209 (1996).

¹⁹ Neil W. Averitt & Robert H. Lande, *Consumer Sovereignty: A Unified Theory of Antitrust and Consumer Protection Law*, 65 ANTITRUST L.J. 713 (1997).

²⁰ Ralph Nader, *The Proper Goals of Antitrust: When Public and Private Interests Collide*, 9 LOY. CONSUMER L. REP. 115 (1997). For a more sophisticated argument regarding antitrust law as a prohibition

scholars who are not yet ready to abandon economic efficiency as a goal of antitrust law have attacked the Chicago School's "reliance on a selective, even myopic, use of economic arguments and claims" that generate "legal tolerance of undesirable structures and inefficient economic conduct."²¹

Scholars dissatisfied with the Chicago School of antitrust law have yet to fashion an equally coherent alternative.²² The antitrust laws of other countries may embody different values than the Chicago School.²³ An examination of the actual workings of antitrust laws in other countries may yield better alternatives to the Chicago School approach or other theoretical models developed by economists and legal scholars. Given its proximity to the United States, as well as a common language and a shared legal history, Canada is a natural choice for such consideration.²⁴

Predatory pricing offers an excellent place to begin the study of the similarities and differences between the antitrust laws of the United States and the competition laws of Canada. Since predatory pricing can constitute a criminal offense in both countries, it is a particularly important issue for business. Furthermore, hostility to predatory pricing claims has long been a hallmark of the Chicago School model.²⁵ Although Canadian scholars have advocated development of predatory pricing law along the lines advocated by Chicago scholars in the United States, Canadian law has actually developed an approach to predatory pricing that emphasizes empirical evidence over economic theory.

II. PREDATORY PRICING LAW IN THE UNITED STATES

Few areas of United States antitrust law proved more problematic over the past thirty years than predatory pricing. Conceptually, the doctrine is easily

on wealth transfers, see, Robert H. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust*, 34 HASTINGS L.J. 65 (1982).

²¹ Peter C. Carstensen, *Director and Levi after 40 Years: The Anti-Antitrust Agenda Revisited*, 17 MISS. C. L. REV. 37, 38 (1996).

²² See, e.g., David F. Shores, *Law, Facts and Market Realities in Antitrust Cases After Brooke and Kodak*, 48 SMU L. REV. 1835, 1855 n.88 (1995) (Advocating a "more judicious if less tidy approach [which] recognizes that proper application of the antitrust laws often requires a balancing of competing goals embraced by Congress.").

²³ See, e.g., Eleanor M. Fox, *Antitrust and Values: Where Liberals and Libertarians Meet*, 9 LOY. CONSUMER L. REP. 132, 134-36 (1997) (Contrasting various European approaches to antitrust law with that of the United States.).

²⁴ Cf. Ross, *supra* note 6, at 469 ("[B]ecause Canada's legislative response to economic problems has often been passed or reformulated after the American legislation is in place, their approach can reflect a fresher and possibly superior look.").

²⁵ See Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U. PA. L. REV. 925, 926-27 (1979).

understood. Predatory pricing occurs when the predator firm drops its prices and sells its products at loss in an effort to drive its competitors from the market. Once the competitors have left the market, the predator may raise its prices and enjoy monopoly profits.²⁶ Although the United States Supreme Court has primarily dealt with predatory pricing under the Robinson-Patman Act,²⁷ predatory pricing can also constitute monopolization or attempted monopolization in violation of the Sherman Act.²⁸ The standards under the two statutes are essentially the same.²⁹

²⁶ See Herbert Hovenkamp, *Federal Antitrust Policy: The Law of Competition and Its Practice* 298 (1994) ("In its most orthodox form, 'predatory pricing' refers to a practice of driving rivals out of business by selling at a price below cost. The predators intent—and the only intent that can make predatory pricing rational, profit-maximizing behavior—is to charge monopoly prices after rivals have been dispatched or effectively disciplined."); Stephen F. Ross, *Principles of Antitrust Law* 55-56 (1993) ("Predation is best defined as a generic term to describe a firm's sacrifice of short-term profits in the expectation that these losses will be recouped in the future through the realization of monopoly profits"); Robert H. Bork, *The Antitrust Paradox: A Policy at War with Itself* 144 (1978) ("Predation may be defined... as a firm's deliberate aggression against one or more rivals through the employment of business practices that would not be considered profit maximizing except for the expectation either that (1) rivals will be driven from the market, leaving the predator with a market share sufficient to command monopoly profits, or (2) rivals will be chastened sufficiently to abandon competitive behavior the predator finds inconvenient or threatening.").

²⁷ The Robinson Patman Act amended section 2 of the Clayton Act, and provides in relevant part:

It shall be unlawful for any person... to discriminate in price between different purchasers of commodities of like grade and quality, ... where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them...

15 U.S.C. § 13(a).

The Robinson Patman Act also contains a criminal provision which provides in pertinent part: It shall be unlawful for any person... to sell... goods at unreasonably low prices for the purpose of destroying competition or eliminating a competitor.

15 U.S.C. § 13a.

²⁸ Section 2 of the Sherman Act provides:

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding \$10,000,000 if a corporation, or, if any other person, \$350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

15 U.S.C. § 2.

²⁹ This was not always the case. In *A.A. Poultry Farms, Inc.*, the Seventh Circuit noted that "[t]o conclude that [the defendant] did not engage in predatory pricing [under section 2 of the Sherman Act] is not necessarily to absolve it under the Robinson-Patman Act." 881 F.2d 1396, 1404 (7th Cir. 1989). The problem stemmed from the Supreme Court's decision in *Utah Pie* that simple "price discrimination in an oligopolistic market contributing to the erosion of price levels may violate" the Robinson-Patman Act. 881 F.2d at 1404. In other words, *Utah Pie* suggested that the Robinson-Patman Act condemns primary-line discrimination because of its potential to lower prices below competitive levels. The Seventh Circuit,

Beginning with some of their earliest writings in the late 1950's,³⁰ Chicago School scholars began to argue that predatory pricing rarely, if ever occurred.³¹ No rational firm, they argued, would engage in such tactics. Since the predator loses profits on each unit of product sold, the predator suffers increasing losses as its competitors retreat and the predator's unit sales expand.³² Even if the predator eliminates all of its competitors, the successful predator cannot raise its prices above competitive levels because monopoly profits would attract new entrants into the market and force prices back down to competitive levels.³³ Because the current losses from predatory pricing are

however, felt that the Sherman Act condemned predatory pricing only for its potential to raise prices above a competitive level. Thus, it seemed that "the Robinson-Patman Act condemns at least some primary line discrimination that the Sherman Act permits." 881 F.2d at 1405.

Brooke Group, discussed *infra*, resolved this apparent conflict between the Sherman Act and Robinson-Patman Act. Rather than overruling *Utah Pie* or adopting different tests for the different statutes, *Brooke Group* denied the existence of a conflict between the recoupment test and its reasoning in *Utah Pie*. 509 U.S. 209, 221(1993). The Court held that "the Robinson-Patman Act should be construed consistently with [the] broader policies of the antitrust laws," 509 U.S. at 220 (quoting *Great Atlantic & Pacific Tea Co., Inc. v. FTC*, 440 U.S. 69, 80 n.13 (1979)), i.e., "primary-line competitive injury under the Robinson-Patman Act is of the same general character as the injury inflicted by predatory pricing schemes under Section 2 of the Sherman Act" 509 U.S. 209, 221(1993). The Court, therefore, required proof of below-cost pricing and recoupment for both Sherman Act predatory pricing claims and Robinson-Patman Act primary-line discrimination claims. 509 U.S. at 222-27. According to the Court, the two claims differ only in that primary-line price discrimination under the Robinson-Patman Act requires "a reasonable prospect" of recoupment, while predatory pricing under Section 2 of the Sherman Act requires "a dangerous probability" of recoupment. 509 U.S. at 224. (Under Section 2 of the Sherman Act, "it is generally required that to demonstrate attempted monopolization a plaintiff must prove (1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power." *Spectrum Sports, Inc. v. McQuillan*, 113 S.Ct. 885, 890-91 (1993)).

³⁰ See, e.g., John S. McGee, *Predatory Price Cutting: The Standard Oil (N.J.) Case*, 1 J.L. & ECON. 137 (1958).

³¹ See, e.g., Bork, *supra* note 26, at 155 ("predatory price cutting is most unlikely to exist"); Kenneth G. Elzinga, *Predatory Pricing: The Case of the Gunpowder Trust*, 13 J.L. & ECON. 223 (1970); Roland H. Koller II, *The Myth of Predatory Pricing: An Empirical Study*, 4 ANTITRUST L. & ECON. REV. 105 (1971); Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263 (1981).

³² See Easterbrook, *supra* note 31, at 268 ("The larger the predator's market share, the faster it loses money"); Bork, *supra* note 26, at 149 ("Losses during a price war will be proportionally higher for the predator because he faces the necessity of expanding his output at ever higher costs, while the victim not only will not expand output but has the option of reducing it and so decreasing his costs.").

³³ See Posner, *supra* note 25, at 927 ("[I]f [the predator] tries to recoup [his lost profits] by raising his price, new entrants will be attracted, the price will be bid down to the competitive level, and the attempt at recoupment will fail.") Although a leading scholar and jurist in Chicago School, Posner disagrees with the notion that predatory pricing is irrational. *Id.* at 940. Posner suggests that strategic considerations may cause a rational firm to engage in predatory pricing. *Id.* at 939-40. Posner further suggests that most of his fellow Chicago School adherents have missed this point because "economics contains no generally accepted

certain and the future gains are speculative, no firm would consider predatory pricing a profitable long run strategy.³⁴ Finally, the Chicago School argued that evidence of the predator's intent to hurt competitors should be irrelevant because economic efficiency is the only goal of antitrust law³⁵ and a firm's subjective intent has no bearing on economic effects of its conduct.³⁶

At first, the doctrines suggested by the Chicago School had little influence on mainstream antitrust law scholarship and jurisprudence. In 1967, for example, the United States Supreme Court established a low threshold for predatory pricing claims in *Utah Pie Co. v. Continental Baking Co.*³⁷ Professors Areeda and Turner set off an avalanche of predatory pricing scholarship with a suggestion in 1975 that antitrust laws should only condemn below-cost pricing, regardless of the alleged predator's intent to eliminate its competitors.³⁸ Although Areeda and Turner gave much more credence to predatory pricing claims than Chicago School scholars, their use of a cost based test instead of evidence of subjective intent was consistent with Chicago School thinking.³⁹ During the 1980's, the Supreme Court seemed to embrace the Chicago School skepticism about predatory pricing in a series of cases dealing with other issues, and, as discussed *infra*, the Court hinted that it would condemn only below-cost pricing. Nonetheless, the Court refused to address the issue of predatory pricing directly, and the different circuits split on whether and to what extent they would adopt the "Areeda-Turner test" for predatory pricing.

theory of strategic behavior." *Id.* at 939.

³⁴ See Easterbrook, *supra* note 31, at 272 ("Because the losses during the predation may be large, and the risk of nonrecoupment great, even the ability to collect a monopoly profit after knocking the victim out of the market may not be enough to make predation profitable when evaluated *ex ante*.").

³⁵ See Easterbrook, *supra* note 31, at 266 n.11 ("[T]he antitrust laws should be treated as if they served no other goal than economic efficiency.").

³⁶ See Easterbrook, *supra* note 31, at 280 ("A predator's malicious intent could not increase the economic effects of its conduct.").

³⁷ 386 U.S. 685 (1967).

³⁸ Phillip E. Areeda and Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975). Among the more widely cited responses to the so-called Areeda-Turner test were F.M. Scherer, *Predatory Pricing and the Sherman Act: A Comment*, 89 HARV. L. REV. 868 (1976); Oliver E. Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284 (1977); Paul L. Joskow and Alvin K. Klevorick, *A Framework for Analyzing Predatory Pricing Policy*, 89 YALE L.J. 213 (1979). A more complete, albeit somewhat dated, discussion of the scholarship can be found in Joseph F. Brodley and George A. Hay, *Predatory Pricing: Competing Economic Theories and the Evolution of Legal Standards*, 66 CORNELL L. REV. 738 (1981).

³⁹ See Posner, *supra* note 25, at 940-44.

A. *Brooke Group*

In 1993, the case of *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*,⁴⁰ presented the Supreme Court with an almost textbook example of predatory pricing in an oligopolistic industry.⁴¹ Faced with a declining demand for its branded cigarettes, the plaintiff introduced “black and white” generic cigarettes in 1980. Generic cigarettes proved to be a great success, and the plaintiff’s market share nearly doubled “from a low of just over 2% in 1980 to a high of just over 5% in 1984.”⁴² Among the other five firms which dominated the cigarette industry, the growth of the plaintiff’s generic cigarettes hit the defendant the hardest.⁴³ The defendant responded by introducing its own generic cigarettes in 1984 with wholesale prices below the plaintiff’s and a price war ensued. Previously, the six firms which made up the cigarette industry had not engaged in any significant price competition,⁴⁴ and “[l]ist prices for cigarettes increased in lock-step, twice a year, ... irrespective of the rate of inflation, changes in the costs of production, or shifts in consumer demand.”⁴⁵ The plaintiff alleged that the defendant had entered into the generic segment of the market and ignited the price war in order to coerce the plaintiff into raising its prices, thereby narrowing the gap in price between generic and branded cigarette and returning the industry to oligopolistic rather than competitive price levels.

1. BELOW-COST PRICING

As noted *supra*, Professors Areeda and Turner laid out the fundamental arguments in favor of a below cost pricing test nearly twenty years prior to *Brooke Group*.⁴⁶ The Areeda-Turner test quickly caught on in the lower federal courts, and in *Matsushita Electric Industrial Co. v. Zenith Radio*

⁴⁰ 509 U.S. 209 (1993).

⁴¹ The Supreme Court found that:

The cigarette manufacturing has long been one of America’s most concentrated industries. ... The cigarette industry also has long been one of America’s most profitable, in part because for many years there was no significant price competition among the rival firms. ... Substantial evidence suggests that... the industry reaped the benefits of prices above a competitive level....

Id. at 213.

⁴² *Id.* at 213.

⁴³ *Id.* at 214 (“Although [the defendant] sold only 11.4% of the market’s branded cigarettes, 20% of the converts to [the plaintiff’s] black and whites had switched from a ... brand [of the defendant’s]”).

⁴⁴ *Id.* at 213.

⁴⁵ *Id.*

⁴⁶ Areeda and Turner, *supra* note 38.

Corp.,⁴⁷ the Supreme Court suggested in dicta⁴⁸ that predatory pricing consisted of "pricing below some appropriate measure of cost."⁴⁹ A year later, in *Cargill, Inc. v. Monfort of Colorado, Inc.*,⁵⁰ a case which turned on the question of "antitrust injury,"⁵¹ the Court reiterated its dicta that predatory pricing "may be defined as pricing below an appropriate measure of cost."⁵² Even though the Court did not squarely hold that predatory pricing requires pricing to be below the alleged predator's costs,⁵³ most observers viewed the appropriate measure of cost as the next major issue for the Court to resolve. Indeed, the Court seemed to indicate as much in *Cargill* when it acknowledged a conflict among the circuits on the issue.⁵⁴

Brooke Group clearly held "only below cost prices should suffice" to state a claim for predatory pricing and rejected "the notion that above-cost prices that are below general market levels or the costs of a firm's competitors inflict injury on competition cognizable under the antitrust laws."⁵⁵ The Court feared that it could not prohibit predatory above cost price cutting "without courting intolerable risks of chilling legitimate price-cutting."⁵⁶ Furthermore, the Court believed that price cutting is "most conducive to a breakdown of oligopoly pricing and the onset of competition" in a concentrated market such as the cigarette industry even if the purpose behind the price cutting was "to demonstrate to a maverick the unprofitability of straying from the group."⁵⁷ Finally, the Court felt that it simply "does not constitute sound antitrust

⁴⁷ *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986).

⁴⁸ *Matsushita* involved allegations that Japanese television manufacturers had violated Section 1 of the Sherman Act by conspiring to use predatory prices for their television sets sold in the United States. 475 U.S. at 578. Although *Matsushita* involved predatory claims, the Court decided the case based on the plaintiff's inability to offer sufficient evidence of a conspiracy. 475 U.S. at 595-98.

⁴⁹ 475 U.S. at 584 n.8.

⁵⁰ 479 U.S. 104 (1986).

⁵¹ Antitrust injury is a doctrine which requires a private plaintiff to prove not only that it has been injured by the defendant's violation of the antitrust laws, but also that its injury is "injury of the type the antitrust laws were intended to prevent." 479 U.S. at 109; see also, Norman W. Hawker, *The New Antitrust Paradox: Antitrust Injury*, 44 RUTGERS L. REV. 101 (1991).

⁵² 479 U.S. at 117 ("Predatory pricing may be defined as pricing below an appropriate measure of cost for the purpose of eliminating competitors in the short run and reducing competition in the long run.").

⁵³ Although the dicta in both *Matsushita* and *Cargill* left open the possibility that a price above cost but "below the level necessary to sell [the alleged predator's] products," the decisions were generally understood as endorsing the requirement of below-cost pricing. 479 U.S. at 117-18 n.12 ("[W]e find it unnecessary to [consider]... whether above-cost pricing coupled with predatory intent is ever sufficient to state a claim of predation.").

⁵⁴ 479 U.S. at 117 n.12.

⁵⁵ 509 U.S. at 223.

⁵⁶ *Id.*

⁵⁷ *Id.*

policy” to “depriv[e] consumers of the benefits of lower prices” during the period of predatory conduct.⁵⁸ Unfortunately, the Court did not give a clear indication of what is the appropriate measure of cost.⁵⁹ Instead, the Court chose to focus on a new issue, recoupment.

2. RECOUPMENT

The Court’s insistence on proof of recoupment represented a significant change in its approach to predatory pricing law. As noted *supra*, although *Matsushita* accepted the reasoning that predatory pricing rarely occurred because firms could not rationally expect to recoup the losses generated from predatory pricing, it defined predatory pricing as simply “pricing below some appropriate measure of cost.”⁶⁰ *Utah Pie* ignored the issue of recoupment altogether, focusing instead on predatory intent.⁶¹

Although the recoupment test represented a significant change to the Court’s approach to predatory pricing, it was not altogether unanticipated. Professors Joskow and Klevorick proposed a similar framework for predatory pricing analysis some fifteen years prior to *Brooke Group*.⁶² Furthermore, the Seventh Circuit had already adopted a recoupment test in its 1989 decision, *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*,⁶³ stating that below-cost pricing “bestows a gift on consumers [, and] antitrust laws are designed for the benefit of consumers.”⁶⁴

The underlying basis for the recoupment test in *Brooke Group* may be found in the Court’s statement that the “painful losses” imposed by below-cost pricing on the predator’s “targets is of no moment... if competition is not injured.”⁶⁵ The Court has long held that Congress adopted the antitrust laws

⁵⁸ *Id.* at 224.

⁵⁹ *Id.* at 223 n.1 (“Because the parties in this case agree that the relevant measure of cost is average variable cost, ... we again decline to resolve the conflict among courts over the appropriate measure of cost.”).

⁶⁰ 475 U.S. 574, 585 n.8 (1986). *Cargill* also defined predatory pricing as “pricing below an appropriate measure of cost for the purpose of eliminating competitors in the short run and reducing competition in the long.” 479 U.S. at 117.

⁶¹ *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685, 696 (1967).

⁶² Joskow and Klevorick, *supra* note 38.

⁶³ 881 F.2d 1396 (7th Cir. 1989).

⁶⁴ *Id.* at 1401. In addition to its shared concern about depriving consumers of the benefits of below-cost pricing, the Seventh Circuit felt that it “is much easier to determine from the structure of the market that recoupment is improbable than it is to find the cost a particular producer experiences.” *Id.* at 1401.

⁶⁵ 509 U.S. 209,224 (1993); *see also Id.* at 225 (“[I]t was not enough to inquire ‘whether the defendant has engaged in ‘unfair’ or ‘predatory’ tactics’; rather, ... the plaintiff must prove ‘dangerous probability that [the defendant] would monopolize a particular market’”).

for "the protection of *competition*, not *competitors*."⁶⁶ What matters, however, is what the term "competition" means. The Court in *Brooke Group* defined competition in terms of low prices to consumers,⁶⁷ i.e., competition would be injured only if the predator were ultimately able to raise prices. The Court emphasized its belief that the "costs of an erroneous finding of liability are high"⁶⁸ because low standards would turn predatory pricing claims into "a tool for keeping prices high."⁶⁹ Thus, a predatory pricing claim requires proof not only of below-cost pricing, but also of the predator's recoupment of "its investment in below-cost prices."⁷⁰

The recoupment test, as defined by the Court, consists of two elements. First, the plaintiff must show that "below-cost pricing [is] capable... of producing the intended effects on the firm's rivals."⁷¹ This in turn requires evidence "of the extent and duration of the alleged predation, the relative financial strength of the predator and its intended victim, and their respective incentives."⁷² Second, the plaintiff must prove that there is a "likelihood" that a successful predator would raise prices high enough for a long enough period of time to "compensate [the predator] for the amounts expended on predation, including the time value of the money invested in it."⁷³ In other words, the plaintiff must show that at the time the defendant began to engage in below-cost pricing, the scheme had a determinable expected net present value of at least zero. This "requires an estimate of the cost of the alleged predation and

⁶⁶ *Brown Shoe Co. v. United States*, 370 U.S. 294, 320 (1962) (emphasis in the original).

⁶⁷ The Court stated that without recoupment through higher prices, "predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced." 509 U.S. at 224. Despite the fact that *Brooke Group* produces a result favored by the so-called "Chicago School" of antitrust analysis, the Chicago School holds that "antitrust should concern itself solely with allocative and productive efficiency." Bork, *supra* note 26, at 109. By definition, below-cost pricing does not flow from productive efficiency (lower costs of production), nor does it promote allocative efficiency. Indeed, "[t]he relationship between the inefficiency caused by predatory prices that drop below marginal cost and the undercharges associated with such pricing is conceptually similar to the relationship between the inefficiency caused by cartel prices that rise above marginal cost and the overcharges associated with such pricing." Wesley J. Liebler, *Whither Predatory Pricing? From Areeda and Turner to Matsushita*, 61 NOTRE DAME L. REV. 1052, 1071 (1986). The Court acknowledged that a failed attempt at predatory pricing would cause allocative inefficiencies, but it was not concerned about this since "unsuccessful predation is in general a boon to consumers." 509 U.S. at 224. In the Court's mind, low prices for consumers, not efficiency, must be the overriding goal of antitrust law.

⁶⁸ 509 U.S. at 226.

⁶⁹ *Id.* at 227.

⁷⁰ *Id.* at 224.

⁷¹ *Id.* at 225.

⁷² *Id.*

⁷³ 509 U.S. 209, 225 (1993).

a close analysis of both the scheme alleged... and conditions of the relevant market."⁷⁴

3. APPLICATION

Although the test for predatory pricing established in *Brooke Group* need not be interpreted as setting an especially high threshold to recovery,⁷⁵ the Supreme Court expressly stated it's intent to establish a difficult standard.⁷⁶ In an apparent attempt to emphasize the difficulty of satisfying the recoupment test,⁷⁷ the Court, in an unprecedented move,⁷⁸ reviewed the sufficiency of the evidence presented at trial rather than remanding the case back to the district court.⁷⁹ The Court's application of the recoupment standard has led some to conclude that *Brooke Group* "is likely to have the same effect as if it had created a flat prohibition on" predatory pricing claims.⁸⁰

The plaintiff in *Brooke Group* seemed to have presented "unusually strong evidence" in support of its case,⁸¹ and the Court conceded that "as an abstract

⁷⁴ *Id.* at 226.

⁷⁵ Professors Joskow and Klevorick proposed a similar framework for predatory pricing analysis some fifteen years prior to *Brooke Group*. Joskow and Klevorick, *supra* note 38. Although Joskow and Klevorick offered a framework which they believed would minimize the errors of wrongly finding predatory pricing and wrongly failing to find predatory pricing, *id.* at 215 & 217, they later suggest that an examination of the market structure to gage the chances of long term gains from predatory pricing, i.e., recoupment, would "eliminate the need for further judicial inquiry into pricing behavior" for "most firms in the economy." *Id.* at 258. More recently, Professor Klevorick has criticized the law of predatory pricing as it had developed prior to the *Brooke Group* decision for failing to take into account economic literature suggesting that predatory pricing may be rational and, therefore, more commonly occurring than had been previously thought. Alvin K. Klevorick, *The Current State of the Law and Economics of Predatory Pricing*, 83 AM. ECON. REV. 162 (1993).

⁷⁶ 509 U.S. at 226 ("[T]hese prerequisites to recovery are not easy to establish.").

⁷⁷ Phillip Areeda & Herbert Hovenkamp, *Antitrust Law An Analysis of Antitrust Principles and Their Application* ¶711.2, at 395 (Supp. 1994) ("Rather than leave the lower courts to apply its standard, the Supreme Court took pains to review the factual basis for the jury verdict... and thereby to demonstrate the stringency of its test.").

⁷⁸ See Kenneth L. Glazer, *Predatory Pricing and Beyond: Life After Brooke Group*, 62 ANTITRUST L.J. 605 (1994).

⁷⁹ The Court conceded that it was "not customary" for it "to review the sufficiency of the evidence," 509 U.S. 209, 230 (1993), but it felt compelled to do so in *Brooke Group* in order to provide "guidance concerning the proper application of [the] legal standard." *Id.*

⁸⁰ Glazer, *supra* note 78, at 624; Areeda & Hovenkamp, *supra* note 77 at 396 ("By the stringency of its demand for proof of recoupment, the Court cleared the way for summary rejection of most predatory pricing claims"); cf. Shores, *supra* note 22, at 1858 (Arguing that "practical market realities were not critical to the Court's decision.... [T]he reasonableness of the expectation of recoupment was tested against economic theory rather than actual market realities, [and] the Court applied economic theory to overrule fact-findings.").

⁸¹ Glazer, *supra* note 78, at 606.

matter” the plaintiff’s claim in *Brooke Group* was “within the reach of” a predatory pricing claim.⁸² The Court found that the plaintiff had successfully established specific intent⁸³ and below-cost pricing.⁸⁴ The Court even found that the below-cost prices had the intended effect of disciplining the plaintiff.⁸⁵ Nonetheless, the Court found that the plaintiff failed “to show that in pursuing this scheme, [the defendant] had a reasonable prospect of recovering its losses from the below-cost pricing.”⁸⁶

Surprisingly, the Court did not engage in the careful analysis of the market factors it had called for in setting forth the recoupment test, choosing instead to focus on what it saw as deficiencies in the plaintiff’s argument that the defendant would recoup its losses when the plaintiff raised its prices on generic cigarettes.⁸⁷ According to the plaintiff, as the price difference between generic and branded generics narrowed, many price sensitive consumers would switch back to branded cigarettes, “thus slowing the growth of the [generic] segment and reducing cannibalization of branded sales and their associated supracompetitive profits.”⁸⁸ The Court had already noted the existence of “[s]ubstantial evidence... that... the industry reaped the benefits of prices above a competitive level” for branded cigarettes,⁸⁹ and the Court did not dispute that some consumers would switch to branded cigarettes as the difference in price between branded and generic cigarettes narrowed.⁹⁰ The Court, however, held that it was not enough to show that the price gap between generics and branded cigarettes narrowed and that the consumers who reacted to higher priced generics by switching back to branded cigarettes would pay supracompetitive prices. The Court insisted that the narrowing of the price gap had to result from the raising of generic prices *above a*

⁸² 509 U.S. at 230.

⁸³ *Id.* at 231 (“[T]he record contains sufficient evidence from which a reasonable jury could conclude that [the defendant] envisioned or intended this anticompetitive course of events.”).

⁸⁴ *Id.* at 231 (“[T]here is also sufficient evidence in the record from which a reasonable jury could conclude that for a period of approximately 18 months, [defendant’s] prices on its generic cigarettes were below its costs.”).

⁸⁵ 509 U.S. at 209, 231 (1993) (“[T]his below-cost pricing imposed losses on [plaintiff] that [plaintiff] was unwilling to sustain, given its corporate parent’s effort to locate a buyer for the company.”).

⁸⁶ *Id.* at 231.

⁸⁷ Kenneth G. Elzinga & David E. Mills, *Trumping the Areeda-Turner Test: The Recoupment Standard in Brooke Group*, 62 ANTITRUST L.J. 559, 575 (1994).

⁸⁸ 509 U.S. at 231.

⁸⁹ *Id.* at 213.

⁹⁰ The Court, however, did dispute that the price gap had in fact narrowed. *Id.* at 236. Yet that is not the issue, even on the Court’s own terms. What matters is not whether price gap *actually narrowed* enough to allow recoupment, but whether the defendant *reasonably believed* the price gap *would narrow enough* to allow recoupment.

*competitive level.*⁹¹ This is not to say the recoupment had to come from the sale of generic cigarettes at supracompetitive prices, but if recoupment were to come from branded cigarettes, then the price increase in generics which caused consumers to switch to brand cigarettes must be the “product of nonmarket forces.”⁹²

The Court held that only two types of evidence could establish a reasonable prospect of raising generic prices above competitive levels: “first, if generic output or price information indicates that oligopolistic price coordination in fact produced supracompetitive prices in the generic segment; or second, if evidence about the market and [the defendant’s] conduct indicate that the alleged scheme was likely to have brought about tacit coordination and oligopoly pricing in the generic segment, even if it did not do so.”⁹³ With respect to the first point, plaintiff’s evidence revealed that after the predatory pricing caused it to relent and raise prices on generics, “list prices on... generic... cigarettes increased twice a year.” These semiannual “price increases outpaced increases in costs,” and the “list prices of generics... rose at a faster rate than the prices of branded cigarettes, thus narrowing the list price differential between branded and generic products.”⁹⁴ Although the Court had earlier suggested that the semiannual, “lockstep” price increases of branded cigarettes constituted “[s]ubstantial evidence” of “prices above a competitive level” for branded cigarettes,⁹⁵ it flatly refused to draw the same inference from the same type of evidence regarding the pricing of generic cigarettes. The Court disputed the veracity of the plaintiff’s evidence of price increases, pointing out that “promotional schemes, including coupons, stickers, and giveaways” may have reduced the actual prices paid by consumers.⁹⁶ The Court cited the introduction of “subgeneric” cigarettes in 1988 at even steeper discounts from branded cigarettes than those previously

⁹¹ The thrust of the Court’s reasoning here is that non-collusive price increases are allocatively efficient. “If prices rise in response to an excess of demand over supply, or segment growth slows as patterns of consumer preference become stable, the market is functioning in a competitive manner.” 509 U.S. at 209, 232 (1993). Consequently, “[o]nly if those higher prices are a product of nonmarket forces has competition suffered.” *Id.* There are numerous problems with the Court’s application of this reasoning in *Brooke Group*. First, the Court ignored its own finding that the plaintiff raised its prices in response not to shifting demand or preferences, but rather in response to the defendant’s below-cost pricing. *Id.* Second, what matters is *not what actually happened, but what the defendant reasonably expected to occur*, since the issue for recoupment is whether the defendant reasonably expected to recoup its losses in a case of attempted monopolization.

⁹² *Id.*

⁹³ *Id.* at 233.

⁹⁴ *Id.* at 235.

⁹⁵ *Id.* at 213.

⁹⁶ *Id.* at 236.

associated with generics in support of its conclusion that the price gap actually increased, rather than decreased.⁹⁷ Finally, the Court concluded that even if prices had increased, the price increases could not support an inference of oligopolistic price coordination. First, since production of generics had increased, “rising prices are equally consistent with growing product demand.”⁹⁸ Second, and perhaps more importantly, the plaintiff’s “own officers and directors consistently denied that they or other firms in the industry priced their cigarettes through tacit collusion or reaped supracompetitive profits.”⁹⁹

In a case of attempted monopolization, the issue is not whether the defendant succeeds in recouping its losses from predatory pricing, but whether there was a dangerous probability of success. Here too, the Court found the plaintiff’s evidence lacking. Plaintiff offered no evidence of overt collusion between the defendant and its competitors. Consequently, as the Court noted, the “only means by which [the defendant could] have established oligopoly pricing... is through tacit price coordination with the other cigarette firms.”¹⁰⁰

The Court examined the evidence regarding the market structure and found that the characteristics of the industry were such that notwithstanding the defendant’s stated objective “to slow the growth of the [generic] segment, no objective evidence of its conduct permits a reasonable inference that it had any real prospect of doing so through anticompetitive means.”¹⁰¹ The Court stated that tacit coordination is facilitated by “a stable market environment, fungible products, and a small number of variables upon which the firms seeking to coordinate their pricing may focus.”¹⁰² All of these were absent, according to the Court. When the defendant began its below-cost pricing, “the cigarette market was in an obvious state of flux.”¹⁰³ Furthermore, the “large

⁹⁷ 509 U.S. at 209, 236 (1993).

⁹⁸ *Id.* at 237.

⁹⁹ *Id.* While it is not surprising for the Court to reject an inference oligopolistic pricing for generic cigarettes which contradicts the plaintiff’s own testimony, it is surprising for the Court to draw the inference of oligopolistic pricing for branded cigarettes when the inference is drawn from the same evidence and contradicted by the same testimony.

¹⁰⁰ *Id.* at 238.

¹⁰¹ *Id.* at 241. This is a particularly troublesome holding given that the Court had previously noted the cigarette industry had successfully avoided price competition “for many years” in the branded segment, *Id.* at 213, which suggests that the market structure for cigarettes was conducive to tacit collusion. With respect to the defendant’s stated belief that it could succeed in achieving coordinated pricing of generics after its below-cost pricing succeeded in disciplining the plaintiff, the dissent aptly noted that according to classic Chicago School analysis, “lawyers know less about the business than the people they represent [and the] judge knows even less about the business than the lawyers. *Id.* at 257 n.18 (Stevens, J., dissenting) (quoting Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1, 5 (1984).

¹⁰² 509 U.S. 209, 238 (1993).

¹⁰³ *Id.*

number of product types and pricing variables also decreased the probability of effective parallel pricing.”¹⁰⁴

Finally, the Court said, “[e]ven if all the cigarette companies were willing to participate in a scheme to restrain the growth of the generic segment, they would not have been able to coordinate their actions and raise prices above a competitive level unless they understood that [the defendant’s] entry into the segment was not a genuine effort to compete with” the plaintiff.¹⁰⁵ The Court rejected the plaintiff’s argument that the defendant signalled its intent through the defendant’s price lists, because the plaintiff could produce “no documents... that indicated any awareness of [the defendant’s] supposed signal by its principal rivals.”¹⁰⁶

B. *Summary and Critique*

The basic elements of a predatory claim are easily stated. A plaintiff must prove below-cost pricing and recoupment. Recoupment requires proof that the intended victim would likely succumb, which in turn depends on “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.”¹⁰⁷ Recoupment also requires proof that the predatory pricing scheme will ultimately prove profitable. This depends on three factors: (1) whether “the market is highly diffuse and competitive,” (2) the existence of barriers to entry in the market, and (3) whether the defendant has or easily can obtain the “capacity to absorb the market shares of his rivals.”¹⁰⁸ Finally, in conspiracy cases, the fact that prices rise steeply after the plaintiff succumbs to the defendant’s below-cost pricing will not prove recoupment unless the plaintiff can also show that the price increase resulted from concerted action.

Despite the clarity as to the elements necessary to prove predatory pricing, the Court failed to articulate a coherent rationale for its stringent application of the test to the facts presented in *Brooke Group*. Chicago scholars have generally applauded the result in *Brooke Group*,¹⁰⁹ but the test it established is not truly consistent with Chicago reasoning. *Brooke Group*, to be sure,

¹⁰⁴ *Id.* at 239.

¹⁰⁵ *Id.* at 240.

¹⁰⁶ *Id.* at 241.

¹⁰⁷ *Id.* at 225.

¹⁰⁸ *Id.* at 226.

¹⁰⁹ See, e.g., Elzinga & Mills, *supra* note 87; Keith Allen May, Casenote, *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.: A Victory for Consumer Welfare Under the Robinson-Patman Act*, 28 U. RICH. L. REV. 507 (1994); Daniel J. Gifford, *Predatory Pricing Analysis in the Supreme Court*, 39 Antitrust Bull. 431 (1994); Mark I. Schwartz, *The Brooke Decision: The Supreme Court Revisits Predatory Pricing*, 99 COMM. L.J. 276 (1994).

adopts Chicago's beliefs that "predatory pricing schemes are rarely tried, and even more rarely successful,' ... and the costs of an erroneous finding of liability are high."¹¹⁰ There are, however, distinctly non-Chicago elements in the Court's reasoning. For example, Chicago School analysis holds that a small firm can always raise enough capital to wait out the predation of its larger rival,¹¹¹ but *Brooke Group* includes the relative financial strength of the parties as part of the recoupment test.¹¹² Chicago, moreover, holds that efficiency, i.e., "consumer welfare," is the only valid goal of antitrust law.¹¹³ Nonetheless, *Brooke Group* acknowledges that even without recoupment, below-cost pricing is inefficient.¹¹⁴

Although *Brooke Group* is not an unqualified endorsement of Chicago, the decision fails to consider any of the "post-Chicago" economic learning about the strategic use of predatory pricing. This is indeed an unfortunate oversight. As the Supreme Court has grown increasingly skeptical about the existence of predatory pricing in the "real world,"¹¹⁵ economists have developed an increasing body of scholarship based on strategic behavior and other factors which suggests that predatory pricing is a rational, if not frequent, form of business conduct.¹¹⁶ Strict adherence to the elements of recoupment as defined in *Brooke Group* would nonetheless deny consideration of the strategic factors identified by post-Chicago thought as essential for understanding predatory pricing as a rational phenomenon.¹¹⁷

¹¹⁰ 509 U.S. 209, 226 (1993) (Quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 589 (1986)); Jonathan B. Baker, *Predatory Pricing After Brooke Group: An Economic Perspective*, 62 ANTITRUST L.J. 585, 603 (1994) (The Court "awarded judgment as a matter of law based on Chicago School presumptions, without reconsidering Chicago arguments in light of contemporary developments in economics.").

¹¹¹ *Elzinga & Mills*, *supra* note 87, at 575 ("[A] small firm with few internal resources may be able to ride out a time of predation by borrowing in the capital markets against its prospects in the future once prices rise.").

¹¹² 509 U.S. at 225.

¹¹³ *Bork*, *supra* note 26, at 51, 91.

¹¹⁴ 509 U.S. at 224 ("[U]nsuccessful predatory pricing may encourage some inefficient substitution toward the product being sold at less than its cost.").

¹¹⁵ *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 589 (1986) ("[T]here is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful.").

¹¹⁶ See James E. Meeks, *Predatory Behavior as an Exclusionary Device in the Emerging Telecommunications Industry*, 33 WAKE FOREST L. REV. 125, 132, 136-41 (1998); Walter Adams & James W. Brock, *Predation, "Rationality," and Judicial Somnambulism*, 64 U. CIN. L. REV. 811, 855-67 (1996); Alvin K. Klevorick, *The Current State of the Law and Economics of Predatory Pricing*, 83 AM. ECON. REV. 162 (1993).

¹¹⁷ *Baker*, *supra* note 110, at 602 ("[P]ost-Chicago developments were not noted by the Court in *Brooke Group*, and they were not brought to the Court's attention by the parties."); *Elzinga & Mills*, *supra* note 87, at 579 (The plaintiff "did not appeal explicitly to any established theory of strategic behavior and

If the Court in *Brooke Group* was not concerned with economic efficiency or post-Chicago economic theory, then what was it concerned with? The answer may be low prices.¹¹⁸ The Court repeatedly stated that it feared that low standards for predatory pricing claims might result in the use of antitrust suits as “a tool for keeping prices high.”¹¹⁹ Indeed, although the Court conceded the inefficiency of below-cost pricing without recoupment, it nonetheless insisted on proof of recoupment because “unsuccessful predation is in general a boon to consumers.”¹²⁰ *Brooke Group* stopped short of saying that lowering prices is legal *per se*, but that may have been the Court’s message.¹²¹

Read in its entirety, *Brooke Group* suggests there is no such thing as an illegal price cut, but businesses may act on that thinking at their own peril. Since the “death knell” of predatory pricing is found in *Brooke Group*’s application of the test to the evidence and not the test itself, and since *Brooke Group* failed to articulate a coherent basis for its stringent application of the test, *Brooke Group* will be as easily distinguished when post-Chicago attorneys ascend to the bench as *Utah Pie* was in *Brooke Group*.¹²² Indeed, one seeking to distinguish *Brooke Group* need only point out that the plaintiff’s own executives denied the existence of an essential fact needed to prove recoupment in the cigarette industry, tacit coordination.

While the Areeda-Turner test’s conclusive presumption that prices above average variable cost were not predatory¹²³ was not without faults, it had the singular virtue of clearly delineating legal conduct. By referring to its own cost data, a firm could know whether it had violated the antitrust law. Given that recoupment ultimately turns on the court’s interpretation of evidence regarding not only the alleged predator’s costs, but also the victim’s financial

the Court saw no need to shoehorn one into the case.”).

¹¹⁸ Cf. Shores, *supra* note 22, at 1854 (“The most likely explanation for the Brooke Court’s treatment of the recoupment issue is the notion that the antitrust laws, including the Robinson-Patman Act, only prohibit conduct injurious to consumers. Below-cost pricing with no reasonable prospect of recoupment cannot injure consumers regardless of the predator’s subjective intent because the predator will never be able to realize its goal of increasing price.”).

¹¹⁹ 509 U.S. 209, 227 (1993).

¹²⁰ *Id.* at 224.

¹²¹ If so, this would place the Supreme Court squarely at odds with the original intent of the Sherman Act. This statute was enacted in an era characterized by consistently falling price levels, therefore, it makes little sense that Congress would have adopted it as an anti-inflationary measure. See Norman W. Hawker, *The New Antitrust Paradox: Antitrust Injury*, 44 RUTGERS L. REV. 101, 119 (1991).

¹²² Stephen Calkins, *The October 1992 Supreme Court Term and Antitrust: More Objectivity Than Ever*, 62 ANTITRUST L.J. 327, 391 (1994) (“Any application of *Brooke Group*... should recognize the many respects in which it was a unique case.”).

¹²³ Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697, 733 (1975).

structure and industry-wide market characteristics, a firm cannot assess the legality of a proposed price. Only after a competitor or the government challenges the price can a firm know if the below-cost price violated the federal antitrust laws. Business would have benefited more from a conclusive presumption that average variable cost separates illegal from legal prices, than from a test that depends on an *ex post facto* determination of the appropriate economic theory used to interpret data in the possession of the firm's rivals.¹²⁴

Furthermore, the addition of the recoupment test by itself will not likely stem the tide of predatory pricing. The Seventh Circuit saw the test as a mechanism to provide quick dismissal of predatory pricing claims, but *Brooke Group* calls for "close analysis of both the scheme alleged by the plaintiff and the structure and conditions of the relevant market."¹²⁵ This will undoubtedly mean extensive discovery of economic evidence even if trial courts hold discovery of cost data in abeyance until the issue of recoupment is resolved.¹²⁶ Predatory pricing litigation will continue to be lengthy and expensive.

Finally, *Brooke Group* ignores the fundamental fact that even unsuccessful predatory pricing produces victims,¹²⁷ and there is a great deal of evidence which suggests that Congress meant to protect all of the predator's victims, not just consumers.¹²⁸ By the same token, there is scant evidence that Congress intended to promote low consumer prices or economic efficiency to the exclusion of everything else when it enacted the antitrust laws.¹²⁹

¹²⁴ Michael L. Denger & John A. Herfort, *Predatory Pricing Claims After Brooke Group*, 62 ANTITRUST L.J. 541, 558 (1994).

¹²⁵ 509 U.S. 209, 226 (1993).

¹²⁶ Denger & Herfort, *supra* note 124, at 545.

¹²⁷ Cf. Edwin J. Hughes, 77 MARQ. L. REV. 265 (1994) (Antitrust law not only promotes efficiency, it also redresses "particular acts of wrong doing" in the context of "damaging and unfair competition.").

¹²⁸ F.T. Stimson, *Trusts*, 1 HARV. L. REV. 132, 134 (1887); William Letwin, *Law and Economic Policy in America* 70 (1965).

¹²⁹ As previously noted, it defies common sense to suggest that Congress was concerned with low prices. See Hawker, *supra* note 51, at 119; cf. Bryce J. Jones, II & James R. Turner, *Can an Operating System Vendor Have a Duty to Aid Its Competitors?*, 37 JURIMETRICS J. 355, 375 (1997) ("Although the legislators emphasized during their debate that one purpose of the act was to lower prices to consumers, they were also concerned that trusts were resulting in tremendous inequality of power and wealth, and they called for fair, equal, and open opportunities for businesses to compete.").

Economists at the end of the nineteenth century, much like modern Chicago School antitrust scholars and judges, felt that efforts by firms to monopolize markets were either economically efficient or doomed to failure because monopoly profits would attract new entrants. Alan J. Meese, *Price Theory and Vertical Restraints: A Misunderstood Relation*, 45 UCLA L. REV. 143, 144-45 (1997). The Sherman Act, therefore, may be best understood as a rejection of such thinking. *Id.* at 145. See also James May, *Antitrust in the Formative Era: Political and Economic Theory in Constitutional and Antitrust Analysis, 1880-1918*, 50 OHIO ST. L.J. 257, 394 (1989) ("[A]ntitrust analysis in 1890 substantially focused on the protection of basic rights of labor, property, and exchange as a means to attain not only efficiency but also opportunity, prosperity, justice, and freedom...").

Thanks to *Brooke Group*, the federal antitrust laws now have a set of relatively clear standards for predatory pricing claims. A coherent basis for applying those standards, however, does not exist, and the standards do not promise any assistance to businesses attempting to gage the legality of alternative pricing strategies. Furthermore, the apparent basis for the test, low consumer prices at any cost, is not consistent with the Congressional intent, the nature of law in general.

III. CANADIAN PREDATORY PRICING LAW

The earliest version of Canada's first competition law statute, the Combines Investigation Act,¹³⁰ predates the Sherman Act by at least year.¹³¹ After nearly a century of piecemeal amendments,¹³² Canada substantially revised the Combines Investigation Act and renamed it the Competition Act ("the Act") in 1986.¹³³ Although some commentators have suggested that Canada adopted the Act with the single minded purpose of promoting economic efficiency,¹³⁴ Section 1.1 of the Act reveals that it serves a myriad

¹³⁰ Combines Investigation Act, R.S.C., ch. C-23 (1970) (Can.).

¹³¹ See William T. Stanbury, *Competition Policy in Canada: Evolution, Effectiveness and the Changing Context of Competition*, Policy Options, Oct., 1997, at 3 ("Canada's competition policy began with a law in 1889 aimed at price-fixing agreements"); Collins & Brown, *supra* note 5, at 497; Collins, *supra* note 10, at 170; Maule & Ross, *supra* note 16, at 63 ("The Canadian Parliament passed the first version of its antitrust law in 1889."); see generally Gordon E. Kaiser & Ian Nielsen-Jones, *Recent Developments in Canadian Law: Competition Law*, 18 OTTAWA L. REV. 401 (1986); see also J. Timothy Kennish, *Competition Law and Enforcement in Canada*, 20 INT'L LAW. 81, 84 (1986) ("The first Canadian statute dealing with competition law matters was enacted in 1888...").

¹³² See Maule & Ross, *supra* note 16, at 63-74 (1989); Carol Hamilton Jordan, *An Examination of the Proposed Amendments to the Canadian Competition Law: Bill C-91*, 10 SUFFOLK TRANSNAT'L L. REV. 473, 473-77 (1986).

¹³³ Competition Act, R.S.C., ch. C-34 (1985) (Can.), reprinted in Robert S. Nozick, *The 1997 Annotated Competition Act 1-238* (1996); see also Thomas W. Ross, *Introduction: The Evolution of Competition Law in Canada*, 13 Rev. Indus. Org. 1, 3-9 (1998); Lawson A.W. Hunter, Q.C. & John F. Blakney, *An Overview of the New Competition Law: Issues for the Oil and Gas Industry*, 26 ALBERTA L. REV. 59 (1987).

¹³⁴ See, e.g., Stanbury, *supra* note 131, at 3 ("The purpose clause of the *Competition Act* makes it clear that efforts to maintain and encourage competition is a means to an end, namely promoting efficiency and adaptability of the Canadian economy."); Donald G. McFetridge, *Efficiencies Considerations in the Competition Act: Where Now?*, Policy Options, Oct., 1997, at 17 ("The philosophy underlying the Act was that competition was a means of achieving efficient market outcomes rather than an end in itself."); Maule & Ross, *supra* note 16, at 60 ("[The Act] reflects the view that competitive markets are efficient and that the central goal of antitrust policy should be the enhancement of competition to promote the efficient use of resources.").

of goals.¹³⁵ The Act defines a series criminal offenses which can be tried in either federal or provincial courts¹³⁶ and a series civil offenses that are adjudicated by the Competition Tribunal ("the Tribunal"), a special administrative body established by the Competition Tribunal Act in 1986.¹³⁷ Predatory pricing violates both criminal¹³⁸ and civil provisions¹³⁹ of the Act.¹⁴⁰

A. Criminal Provisions

Canada amended its original Combines Investigation Act in 1935 to prohibit predatory pricing and price discrimination.¹⁴¹ The prohibition on predatory pricing is currently codified in Section 50(1)(c) of the Act which provides:

"[E]very one engaged in a business who... engages in a policy of selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition or eliminating a competitor, or designed to have that effect, is guilty of an indictable offence and is liable to imprisonment for a term not exceeding two years."¹⁴²

¹³⁵ "The purpose of this Act is to maintain and encourage competition in Canada in order to promote the efficiency and adaptability of the Canadian economy, in order to expand opportunities for Canadian participation in world markets while at the same time recognizing the role of foreign competition in Canada, in order to ensure that small and medium sized enterprises have an equitable opportunity to participate in the Canadian economy and in order to provide consumers with competitive prices and product choices." Combines Investigation Act, R.S.C., ch. C-34, § 1.1 (1985) (Can.). In the one words of one commentator, Section 1.1 "[m]ight not be as clear a statement of the primacy of efficiency as a goal of competition as some economists might have wished..." Ross, *supra* note 133, at 9; *see also* Hunter & Blakney, *supra* note 133, at 70 n.34.

¹³⁶ *See* American Bar Association. International Antitrust Committee., *The Competition Laws of NAFTA, Canada, Mexico, and the United States: A Practitioner's Guide* 37 (1997).

¹³⁷ Competition Tribunal Act, R.S.C., ch. 19 (2nd Supp.1985) (Can.). For an overview of the Competition Tribunal *see* Ross, *supra* note 133, at 12-13; Hunter & Blakney, *supra* note 133, at 71-73; Warren Grover & Robert Kwinter, *The New Competition Act*, 66 CAN. B. REV. 267, 268-71 (1987).

¹³⁸ Combines Investigation Act, R.S.C., ch. C-34, § 50(1)(c) (1985) (Can.).

¹³⁹ Section 78(i) of the Act provides that sale of "articles at a price lower than the acquisition cost for the purpose of disciplining or eliminating a rival," R.S.C., c. C-34, § 78(i) (1985) (Can.), by a dominant firm in a market may constitute an abuse of dominant position in violation of Section 79 of the Act. R.S.C. 1985, c. C-34, § 79(1).

¹⁴⁰ *See* Maule & Ross, *supra* note 16, at 81 n.167 ("It is not clear why predation appears twice in this way, or which route will be easier for a Director seeking to enjoin the practice.").

¹⁴¹ Stanbury, *supra* note 131, at 3.

¹⁴² Combines Investigation Act, R.S.C., ch. C-34, § 50(1)(c) (1985) (Can.). One could argue that Section 50(1)(b)'s prohibition on price discrimination also prohibits predatory pricing. *See* Kennish, *supra* note 131, at 88-89. To some extent this parallels the relationship of Sherman and Robinson Patman Acts

This is essentially identical to the language previously used in Section 34(1)(c) of the earlier Combines Investigation Act.¹⁴³

Only a few criminal predatory pricing cases have been reported under Canadian competition law. In an effort to deal with the paucity of case law interpreting the section 50(1)(c) of the Act, the Canadian Director of Investigation and Research ("the Director"), who is charged with enforcement of the Act, issued Predatory Pricing Enforcement Guidelines ("the Guidelines") in 1992.¹⁴⁴ Consistent with the case law, the Guidelines define predatory pricing in general terms as "a dominant firm setting its prices so low... that it may drive on or more of its competitors from the market," enabling the successful predator "to raise prices significantly."¹⁴⁵

The Guidelines suggest that predatory pricing "has proven to be a rare... occurrence in Canada" and that predatory pricing "does confer some benefits" to consumers.¹⁴⁶ Nonetheless, the Guidelines state that the benefits of predatory pricing to consumers "will be transitory or short-term, and eventually outweighed by increased costs during the period of recoupment."¹⁴⁷ Predatory pricing, moreover, frustrates and interferes "with the process of competition in the longer term, an outcome ultimately detrimental to consumers."¹⁴⁸ At least one case¹⁴⁹ goes beyond the position of the Guidelines and states that "[P]arliament has decided to forbid these practices because the

in the United States. This article, however, will concentrate on the "pure" predatory pricing provisions of the Competition Act and leave the issue of price discrimination for another day.

¹⁴³ See *Regina v. Consumers Glass Co. Ltd.*, [1981] 33 O.R.2d 228 at 230 (Quoting Section 34(1)(c) of the 1970 Combines Investigation Act: "Every one engaged in a business who... engages in a policy of selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition or eliminating a competitor, or designed to have such effect, is guilty of an indictable offence and is liable to imprisonment for two years.").

¹⁴⁴ Director of Investigation and Research, Predatory Pricing Enforcement Guidelines (1992) (hereinafter "Guidelines").

¹⁴⁵ *Id.* at 1; cf. *Consumers Glass*, O.R.2d at 231 ("[T]he Act penalizes predatory pricing—the cutting of prices for anticompetitive reasons. The classically-feared case of predation has been the deliberate sacrifice by the predator of present returns by lowering the selling price for the purpose of driving rivals out of the market, followed by the recovery of losses and the earning of higher profits by the predator in the absence of competition"); *Regina v. Hoffman-La Roche Ltd.*, [1980] O.R.2d 192 ("[T]he evil of predatory pricing is this: One company, the predator, decides to sell its product at a very low price in order to put his competitor out of business, because they cannot or will not sell at such a low price. If the competitor goes out of business, the predator may then increase his prices, make back the any loss as a result of the predatory campaign and continue to reap the benefits of greater profits, because his former competitor has now departed from the scene.").

¹⁴⁶ Guidelines, *supra* note 144, at 1.

¹⁴⁷ *Id.* at 1.

¹⁴⁸ *Id.* at 2.

¹⁴⁹ *Hoffman-La Roche Ltd.*, O.R.2d at 192.

public interest demands a system in which fair competition thrives" even if "[t]actics such as this may good business sense in certain circumstances..."¹⁵⁰

On a more specific level, the Guidelines and case law agree that the criminal offense of predatory pricing consists of four basic elements: (1) that the defendant engaged in a *business*, (2) that the defendant engaged in a *policy of selling* products, (3) that the defendant charged unreasonably low prices, and (4) that the defendant did these things with the *design, tendency or effect of lessening competition or eliminating a competitor* from the market.¹⁵¹ Nonetheless, the case law and the Guidelines present markedly different approaches to dealing with a number of these elements.

1. ENGAGED IN A BUSINESS

The Act defines "business" in very broad terms,¹⁵² as did its predecessor, the Combines Investigation Act.¹⁵³ Although there are no cases directly on point, the apparent thrust of this requirement is to exempt transactions by private individuals in the conduct of their personal affairs from the reach of the statute.¹⁵⁴

2. ENGAGED IN A POLICY OF SELLING

Only a "policy of selling" will violate Section 50(1)(c). The focus is on the deliberateness and duration of the conduct. Thus, the Guidelines call for evidence "to determine whether the prices in question have resulted from, and

¹⁵⁰ *Id.*

¹⁵¹ See Guidelines, *supra* note 144, at 3; Hoffman-La Roche Ltd., O.R.2d at 193-213; see also, Presley L. Warner, *Canada-United States Free Trade: The Case for Replacing Antidumping with Antitrust*, 23 *Law & Pol'y Int'l Bus.* 791, 860 ("The four elements of the 50(1)(c) offense are: (1) The accused must be engaged in a business; (2) the accused must engage in a policy of selling products; (3) the products must be sold at unreasonably low prices; and (4) that the policy must have the effect or tendency of substantially lessening competition or eliminating a competitor or be designed to have that effect.")

¹⁵² Combines Investigation Act, R.S.C., ch. C-34, § 2(1) (1985) (Can.) provides that: "business" includes the business of:

(a) manufacturing, producing, transporting, acquiring, supplying, storing and otherwise dealing in articles, and

(b) acquiring, supplying and otherwise dealing in services.

¹⁵³ Combines Investigation Act, R.S.C., ch. C-23, § 2 (1985) (Can.), provides: "business" includes the business of

(a) manufacturing, producing, transporting, acquiring, supplying, storing and otherwise dealing in articles, and

(b) acquiring, supplying and otherwise dealing in services."

¹⁵⁴ See Hoffman-La Roche Ltd., O.R.2d at 193 ("If someone, as a private person not engaged in a business, sells an article for an unreasonably low price to lessen competition, he cannot be found guilty.")

are part of, a deliberate corporate program of pricing in the market."¹⁵⁵ The trial court in *Hoffman-La Roche*, however, emphasized that a policy did not require "a formal corporate by-law or resolution approving a particular course of action."¹⁵⁶ Rather, the Act simply requires "a planned and deliberate course of conduct by responsible employees of the company."¹⁵⁷ As to duration, both the Guidelines and the case law indicate that an isolated sale transaction will not suffice.¹⁵⁸

The Guidelines suggest that price cuts made as "defensive reactions to the pricing initiatives or behaviour of other firms" will not constitute a policy of selling even if the price cuts are deliberate and sustained. This position finds support in *R. v. Producers Dairy Ltd.*¹⁵⁹ where the court held that a price cut made in response to a price concession made by a competitor did not constitute a policy. In *Hoffman-La Roche*, however, the trial court seemed to reject this position, holding instead that defensive nature of the defendant's conduct "is a factor to be considered in deciding whether the prices were unreasonably low... and whether intent of the accused was to substantially lessen competition."¹⁶⁰

Hoffman-La Roche raised one of the more intriguing technical issues with respect to this element. The defendant gave away an enormous amount of its products. Some of this consisted of buy one/get one free types of promotions,¹⁶¹ but the defendant also gave Valium to hospitals for free.¹⁶² The trial court rejected the defendant's argument that "no sale occurs when a give-away takes place."¹⁶³ The buy one/get one free promotions really amounted to a sale at half the regular price.¹⁶⁴ Noting that it "would be ridiculous to hold that a sale takes place when 1,000 pills are sold for a \$1, but not if they were given away for free,"¹⁶⁵ the trial court held that "even when the goods are given away totally free by the a producer to a customer in a commercial context."¹⁶⁶ Furthermore, the trial court pointed out that both sides presented

¹⁵⁵ Guidelines, *supra* note 144, at 12.

¹⁵⁶ *Hoffman-La Roche Ltd.*, O.R.2d at 193, 194.

¹⁵⁷ *See id.*

¹⁵⁸ *Id.* at 193 ("[T]he selling must be continuing or repeated sales"); Guidelines, *supra* note 144, at 12 ("[C]omplaints about a particular price which applies to one, or relatively few, market transactions are unlikely to satisfy this test.").

¹⁵⁹ *Regina. v. Producers Dairy Ltd.* [1966], C.P.R.2d 265.

¹⁶⁰ *Hoffman-La Roche*, O.R.2d 193, 195.

¹⁶¹ *Id.* at 173-74 and 176-77.

¹⁶² *Id.* at 177-80.

¹⁶³ *Id.* at 195.

¹⁶⁴ *Id.*

¹⁶⁵ *Id.* at 196.

¹⁶⁶ *Id.*

evidence from economic experts to the effect that a “zero price” transaction constituted a sale.¹⁶⁷ Finally, the trial court also relied on evidence on that the defendant considered and treated the free Valium as a commercial transaction, not a gift.¹⁶⁸ The Court of Appeals agreed with the trial court that the free Valium constituted a policy of selling since the defendant “intended to have the long run effect of generating future sales after the elimination of the competitor.”¹⁶⁹

3. UNREASONABLY LOW PRICES

Although the Guidelines describe the reasonableness of the prices as the threshold issue in predatory pricing claims,¹⁷⁰ this is almost certainly the most problematic of the four elements. Indeed, three distinct approaches to the determination of whether the prices are unreasonably low appear to have developed.

4. THE TWO STAGE ANALYSIS

Under the Guidelines, whether or not the prices are unreasonably low depends on a two stage analysis. First, the Director examines whether the alleged predator has market power “or the potential for building” market power in order to determine if “it is plausible that this pricing could achieve the anticompetitive effects described in section 50(1)(c) of the Act.”¹⁷¹ The existence of market power depends on market shares, concentration, and barriers to entry.¹⁷² A firm with a market share of less than 35 percent is unlikely to have the requisite market power,¹⁷³ absent some barrier to entry.¹⁷⁴

¹⁶⁷ *Id.*

¹⁶⁸ *Id.* (In this case, it is clear on the evidence that the drugs being “given away” were part of a commercial operation, not a charitable one. Invoices were normally sent to the recipients with ‘no charge’ marked thereon, a practice seldom followed in a true gift situation. The donor’s aim was to combat its competitors, and to maintain its place in the market in future. The so-called free drugs, therefore, were not really gifts from the accused; the motivation behind them being completely commercial, they were all sales.)

¹⁶⁹ Hoffman-La Roche Ltd., 33 O.R.2d 694 at 710.

¹⁷⁰ Guidelines, *supra* note 144, at 3 (“[T]he threshold issue in a predatory pricing complaint is the reasonableness of the prices themselves.”).

¹⁷¹ *Id.* at 6.

¹⁷² *Id.* at 6-10.

¹⁷³ *Id.* at 6-7 (“It is unlikely that an alleged predator with a market share of less than 35 percent would have the ability to unilaterally industry pricing.”).

¹⁷⁴ *Id.* at 7 n.8 (Market power might exist “where a firm has market share of less than 35 percent but is able to build and entrench market power through strategic behavior.”).

Even if the Director does not find sufficient evidence of predatory pricing in the first stage of the analysis, he may “infer the likelihood of unreasonably low prices from the totality of the circumstances, including such factors as evidence of predatory intent or the manner and extent of elimination or exclusion of competitors by pricing practices.”¹⁷⁵

In the second stage of the analysis, the Director confirms whether the “prices are indeed unreasonably low by evaluating the relationship between the alleged predator’s prices and costs.”¹⁷⁶ Prices at or above average total cost are reasonable *per se*.¹⁷⁷ Prices below average variable cost are “likely to be regarded as ‘unreasonably low’ . . . , unless there is a clear justification such as the need to sell off perishable inventory.”¹⁷⁸ A “grey range” exists “between average total cost and average variable cost.”¹⁷⁹ In this grey range, the Director will look to “the surrounding circumstances”¹⁸⁰ to determine whether the prices are unreasonably low. Among other things, the Director will consider evidence of “declining demand or substantial excess capacity in the market, . . . proof that the accused was ignoring opportunities to raise prices in the face of increasing demand, [and] evidence of the firm’s intent to use pricing for an anti-competitive purpose.”¹⁸¹

B. *The Average Variable Cost Approach*

In *R. v. Consumers Glass Co. Ltd.*,¹⁸² the Crown charged that the defendants, Consumers Glass Co. and its subsidiary, Portion Packaging, had engaged in predatory pricing in the small plastic lid market.¹⁸³ More specifically, the Crown alleged that the defendants had sold the lids at prices substantially below cost in an effort to drive a new competitor, Amhil Enterprises Ltd.,¹⁸⁴ out of the market.¹⁸⁵ Although Portion had been the only

¹⁷⁵ *Id.* at 11.

¹⁷⁶ *Id.* at 6.

¹⁷⁷ *Id.* at 10 (“[A] price set at or above the average total cost of the alleged predator will not be regarded as ‘unreasonably low’ by the Director, regardless of how much market power is possessed by the alleged predator.”).

¹⁷⁸ *Id.* at 10.

¹⁷⁹ *Id.* at 11.

¹⁸⁰ *Id.*

¹⁸¹ *Id.*

¹⁸² *Consumers Glass Co. Ltd.*, 33 O.R.2d 230-31.

¹⁸³ *Id.*

¹⁸⁴ Two former employees of Portion founded Amhil. *Id.*

¹⁸⁵ *Id.* (“The gist of the allegation against the defendants is that they sold the small plastic lids referred to in the indictment at prices substantially below the total cost of producing and selling those lids, in an effort to drive a new competitor, Amhil Enterprises Ltd., out of business and so out of the lid market.”).

source for small lids in Canada,¹⁸⁶ the trial court found that Portion had not enjoyed monopoly power in the small lid market prior to Amhil's entry.¹⁸⁷ Potential competition from United States manufacturers as well as the ease of entry into the small lid market sometimes effectively checked Portion's ability to raise prices even before Amhil's entry into the market.¹⁸⁸ Portion had previously decided to phase out its presence in the small lid market,¹⁸⁹ but it decided to react aggressively to Amhil's entry into the market and "keep 100% of our customers' business."¹⁹⁰ The trial found that Portion dropped its below the total cost of production not in an effort to drive Amhil from the market, but to minimize its losses and "permit Portion to stay in the lid business until lids could be replaced by more profitable products."¹⁹¹ Eventually Portion exited the market and Amhil became the sole Canadian supplier of small lids.¹⁹²

The major legal issue confronting the trial court was whether Portion had charged an "unreasonably low" price. No less a figure than Donald Turner, co-author of the landmark Areeda-Turner test, testified as an expert witness on behalf of the defendants.¹⁹³ The trial court extensively discussed both the Areeda-Turner test¹⁹⁴ and an alternative proposed by the Crown's expert witness, Douglas Greer, that would focus on a defendant's subjective intent whenever prices fell below average total cost.¹⁹⁵ Although the trial court declined to accept the Areeda-Turner test as a rule of general application in predatory pricing cases,¹⁹⁶ the trial court nonetheless held, consistent with the

¹⁸⁶ *Id.*

¹⁸⁷ *Id.* at 232 ("While prior to August, 1975, Portion was the sole Canadian custom manufacturer of small lids, it did not possess monopoly power over the market for small lids.").

¹⁸⁸ *Id.* at 232 ("[B]ecause of possible competition from the United States and the danger that one or more of its customers might find it more economical to make its own lids, Portion's small lid prices even before a competitor entered the market in August, 1975, were so low that, according to the evidence introduced by the Crown, Portion was not recovering its total cost of production and sale on at least some kinds of small lids that it made.").

¹⁸⁹ *Id.* at 234 ("Portion had decided, again before Amhil had entered the market, to get out of the lid market.").

¹⁹⁰ *Id.* at 237.

¹⁹¹ *Id.* at 245.

¹⁹² *Id.* at 246 ("Portion dropped out of the small and large custom lid market some time in 1979, which means that Amhil was thereafter the sole Canadian supplier of those lids.").

¹⁹³ *See id.* at 247-50.

¹⁹⁴ *See id.*

¹⁹⁵ *See id.* at 250-52.

¹⁹⁶ *Id.* at 253 ("It is not necessary for me to decide whether the Areeda and Turner proposal is an appropriate one for the Court to accept in all predatory pricing cases.").

Areeda-Turner test, that "Portion always sold above its average variable cost of production, and so it was not selling at a price unreasonably low."¹⁹⁷

The average variable cost test used in *Consumers Glass* creates a larger safe haven for pricing policies than the Guidelines use of average total cost for per se legality. The reasoning in *Consumers Glass*, however, appears limited by the trial court's conclusion that one could focus exclusively on average variable costs only in cases, such as the *Consumers Glass*, "where there is no evidence that the accused was not profit maximizing or loss minimizing, and where chronic excess capacity exists, [and] there [is] no suggestion that such price was not also above its average marginal cost."¹⁹⁸ Furthermore, *Consumers Glass* provides no guidance to determine whether prices in any other circumstances, including prices below average variable cost, are unreasonable.

1. THE TOTALITY OF THE CIRCUMSTANCES

In *R. v. Hoffman-La Roche Ltd.*,¹⁹⁹ the Canadian government forced the manufacturer of Valium and Librium to license its patents for these two drugs to competing pharmaceutical companies. *Hoffman-La Roche* reacted to the competition by (1) using various buy one/get one free types of deals to hospitals,²⁰⁰ (2) offering to supply the governments Librium needs for \$1,²⁰¹ and (3) giving Valium to hospitals for free.²⁰² The trial court refused to rely solely on the defendant's subjective intent,²⁰³ economic theory²⁰⁴ or a cost based approach²⁰⁵ to determine the reasonableness of the defendant's prices. Instead, the trial court said, whether "a price is unreasonably low must depend on all the circumstances of the sale."²⁰⁶

¹⁹⁷ *Id.* at 255. One should note that the trial court also stated that if it were to look at intent, it would "still conclude that the accused did not adopt such a price in order to lessen competition or eliminate Amhil as a competitor." *Id.*

¹⁹⁸ *Id.* at 245-55.

¹⁹⁹ *Hoffman-La Roche Ltd.*, 28 O.R.2d 164.

²⁰⁰ *Id.* at 173-74 and 176-77.

²⁰¹ *Id.* at 175-76.

²⁰² *Id.* at 177-80.

²⁰³ *Id.* at 197 ("The reasonableness or unreasonableness of a price is an objective matter, not a subjective one. What is in the seller's mind is not important in deciding whether the price was unreasonable. ... A price may be found unreasonably low even though the seller honestly believed it was not.").

²⁰⁴ *Id.* at 197 ("Economic theory cannot control the legal determination of reasonable, but it is certainly relevant.").

²⁰⁵ *Id.* at 197 ("If Parliament had intended that all sales below cost be considered unreasonable, it could have defined the term in that way. It did not.").

²⁰⁶ *Id.* at 197.

More particularly, the trial court suggested that it should consider four factors in deciding whether a price is unreasonably low.²⁰⁷ The first factor calls for an examination of “the actual difference between production cost and the sale price.”²⁰⁸ Despite the trial court’s reluctance to rely solely on a cost based approach,²⁰⁹ the trial court concluded that if “an article is sold for more than cost, it can never be held to be unreasonable.”²¹⁰ Furthermore, “the greater the reduction below cost, the more likely it is that the price is an unreasonable one.”²¹¹ What is not clear, however, is whether the trial court was referring to average total or variable costs. The trial court further confused the concept of costs by suggesting that “direct costs” should be reduced by “any potential future savings or benefits.”²¹² The second factor requires the court to examine “the length of time during which sales at the questionable prices take place.”²¹³ As one would expect, the “longer the deal lasts, ... the more suspect it would become.”²¹⁴ The third factor considers whether the price cuts are defensive or offensive.²¹⁵ After all, said the trial court, “[c]ompetition is a battle... , and competitors must be allowed to engage in that battle, as long as they do so within reason.”²¹⁶ The trial court framed the fourth factor in economic terms by asking “whether any external or long-term economic benefits will accrue to the seller by reducing its prices below cost.”²¹⁷ In reality, however, the test focuses on the defendant’s subjective intent. Examples of this factor given by the court include price cuts to weather an economic down turn or to remain in a particular market “for prestige reasons.”²¹⁸

The trial court found the various two for one type deals did not constitute unreasonably low prices, at least in part because “some of these sales were below cost and others were not.”²¹⁹ Although the \$1 tenders to the government were below cost,²²⁰ the trial court found that none of the other factors for

²⁰⁷ *Id.* at 200.

²⁰⁸ *Id.*

²⁰⁹ *Id.* at 197 (“If Parliament had intended that all sales below cost be considered unreasonable, it could have defined the term in that way. It did not.”).

²¹⁰ *Id.* at 200.

²¹¹ *Id.* at 201.

²¹² *Id.* at 199.

²¹³ *Id.* at 201.

²¹⁴ *Id.*

²¹⁵ *Id.* at 201 (“[D]efensive price-cutting is viewed differently than offensive price-cutting. A level of prices may be reasonable in the former situation that may not be reasonable in the latter.”).

²¹⁶ *Id.* at 201.

²¹⁷ *Id.*

²¹⁸ *Id.*

²¹⁹ *Id.* at 202.

²²⁰ *Id.* at 203 (“[T]hey were sales below cost.”).

unreasonably low prices were satisfied.²²¹ Therefore, “they were not sales at unreasonably low prices in all of the circumstances.”²²² The free Valium, however, constituted an unreasonably low price.²²³ The trial court was particularly impressed that the plan as originally conceived and executed lasted six months, “which is a substantial amount of time.”²²⁴ The defendant appealed, but the Court of Appeals did not directly address this issue. Nonetheless, the Court of Appeals seemed to uphold the trial court’s opinion on this matter when the Court of Appeals stated its agreement “with the conclusion of the learned trial Judge that viewed in its context the supply of Valium ‘free’ to hospitals constituted engaging in a policy of selling at prices unreasonably low within... the Act.”²²⁵

2. DESIGN, TENDENCY OR EFFECT OF LESSENING COMPETITION OR ELIMINATING A COMPETITOR

The Act only condemns a policy of unreasonably low prices when the policy has the purpose or effect of lessening competition or eliminating a competitor.²²⁶ Analysis of this fourth element under the Guidelines resembles the analysis of whether the prices are unreasonably low. The Guidelines state that the Director will look at a number of issues in assessing the competitive impact:

- (a) Has the pricing behavior had the effect of substantially lessening competition?
- (b) Has it had the effect of eliminating a competitor?
- (c) Does the pricing behavior have the tendency to substantially lessen competition?
- (d) Does it have the tendency to eliminate a competitor?
- (e) Is there evidence that the pricing behavior is or was designed to substantially lessen competition or eliminate a competitor?²²⁷

²²¹ More specifically, the trial court found that established that the \$1 tenders “were made to test the reactions of Roche’s customers and competitors... , there were only three such sales over a relatively short period of time, during a very competitive period.” *Id.* at 203.

²²² *Id.* at 203.

²²³ *Id.*

²²⁴ *Id.*

²²⁵ Hoffman-La Roche Ltd., 33 O.R.2d 694, 710.

²²⁶ Combines Investigation Act, R.S.C., ch. C-34, § 50(1)(c) (1985) (Can.).

²²⁷ Guidelines, *supra* note 144, at 13.

A policy of selling at unreasonably low prices substantially lessens competition if it preserves or adds to market power and "there is little opportunity for competition in the future because entry barriers are maintained or raised."²²⁸ The elimination of a competitor can be shown either by evidence that a "competing firm has gone out of business or is otherwise no longer in a position to constrain the ability of the alleged predator to raise prices."²²⁹

Perhaps not surprisingly given the difference in determining the reasonableness of prices, the trial court in *Hoffman-La Roche* took a different approach to this element than the guidelines. While the guidelines largely ignore the question of the defendant's subjective intent, the trial court in *Hoffman-La Roche* emphasized that "even if there is no *actual* effect or tendency,"²³⁰ the Act is violated so long as "the conduct was *designed* to have the effect or tendency of substantially lessening competition or eliminate a competitor."²³¹ Thus, the trial court went out of its way to establish that *either* the *effect* of the defendant's conduct *or* the defendant's subjective *intent* would satisfy the final element of predatory pricing.

The government did not argue that the defendant's policy of giving Valium away for free had actually resulted in a substantial lessening of competition or eliminated a competitor, and the trial court found it highly unlikely that the government could have prevailed on these grounds.²³² Since the defendant's competitor had survived, the government surely could not have proved that the conduct eliminated a competitor.²³³ The defendant's competitors had temporarily withdrawn from the market while the defendant gave away Valium,²³⁴ but the free Valium had little if any lasting impact on the structure of the market.²³⁵

The trial court, however, found ample evidence that the defendant intended to eliminate competition. The trial court relied on specific statements by defendant's employees such as: "It is our feeling that [free Valium] will not only abort [our competitor's] efforts but serve as a warning to others who seem to be showing an interest in this product."²³⁶ The trial court felt these statements went beyond "the colourful jargon of the market-place"²³⁷ and demonstrated "a purpose of excluding competitors, not just making it

²²⁸ *Id.*

²²⁹ *Id.*

²³⁰ *Hoffman-La Roche*, 28 O.R.2d at 205.

²³¹ *Id.*

²³² *Id.* at 205-06.

²³³ *Id.* at 206.

²³⁴ *Id.* at 205.

²³⁵ *Id.* at 206.

²³⁶ *Hoffman-La Roche*, 28 O.R.2d at 207.

²³⁷ *Id.* at 208.

difficult for them.”²³⁸ The trial court was also struck by the evidence that the defendant “was prepared to lose, and did lose, \$2,600,000 worth of Valium sales to prevent a forecast loss of \$600,000 in sales to [defendant’s main competitor] in that year.”²³⁹ Furthermore, the trial court believed that the “drastic discount” of giving away Valium for free “made no sense economically; the price was not only below cost, it was non-existent.”²⁴⁰ Finally, the trial court pointed out that the defendant was not trying to enter the market, a situation where one could expect substantial price,²⁴¹ but rather to respond to someone else’s entry. The defendant’s price cuts were “so out of line”²⁴² with those of the new entrant, that “their purpose must be suspect.”²⁴³ The Court of Appeals expressly upheld the trial court’s decision on the issue of intent, including the trial court’s use of statements by the defendant’s employees as evidence of defendant’s intent.²⁴⁴

C. Abuse of Dominant Position

For a United States antitrust legal scholar, one of the most intriguing aspects of Canadian law is the attempt to prevent a dominant firm from abusing its position. Under Section 79 of the Act, an abuse of dominant position occurs when:

- (a) one or more persons substantially or completely control, throughout Canada or any area thereof, a class or species of business,
- (b) that person or those persons have engaged in or are engaging in a practice of anti-competitive acts, and
- (c) the practice has had, is having or is likely to have the effect of preventing or lessening competition substantially in a market.²⁴⁵

²³⁸ *Id.*

²³⁹ *Id.* at 210.

²⁴⁰ *Id.* at 211.

²⁴¹ *Id.* at 211 (“One can expect substantial price cuts from a seller who is trying to enter a new market.”).

²⁴² *Id.* at 211.

²⁴³ *See id.* at 211 (“Roche’s response was so outlandish that it demonstrates to me that it was not competing with a competitor, but that it was seeking to eliminate its competitors and to substantially lessen competition.”).

²⁴⁴ Hoffman-La Roche Ltd., 33 O.R.2d 694, 707-09.

²⁴⁵ Combines Investigation Act, R.S.C., ch. C-34, § 79(1) (1985) (Can.); *see also* Kaiser & Nielsen-Jones, *supra* note 131, at 495.

As previously noted, the Act specifically includes certain types of below cost sales within the definition of anticompetitive practices.²⁴⁶ Abuse of dominant position is a civil offense litigated by the Director before the Tribunal.²⁴⁷

The scope of this provision was tested in *Canada (Director of Investigation and Research) v. NutraSweet Co.*²⁴⁸ NutraSweet manufactured and distributed aspartame, an artificial sweetener. Despite that its Canadian use patent for aspartame had expired in 1987, NutraSweet continued to hold "exclusive contracts covering over 90% of Canadian sales."²⁴⁹ The Director argued that NutraSweet had engaged in numerous abusive tactics, including below-cost sales.²⁵⁰

The Tribunal found that NutraSweet used anticompetitive practices, but predatory pricing was not one of them. First, the Tribunal gave a very narrow reading to section 78(i) of the Act. The section specifically defines "selling articles at a price lower than the acquisition cost for the purpose of disciplining or eliminating a rival"²⁵¹ as an anticompetitive act. The Tribunal believed Parliament used the phrase "acquisition cost" to limit the section scope "to situations where articles are purchased for resale."²⁵² The Tribunal further held that "acquisition cost is restricted to the cost of the articles and [does] not [include] the cost of distributing them."²⁵³ Not surprisingly, the Tribunal found NutraSweet's "prices exceeded its acquisition costs by a comfortable margin."²⁵⁴

Although the Tribunal refused to apply Section 78(i) "to manufacturing situations where there is not a purchase and resale of articles,"²⁵⁵ the examples of anticompetitive acts identified in Section 78 of the Act are not meant to be

²⁴⁶ Combines Investigation Act, R.S.C., ch. C-34, § 78(i) (1985) (Can.); Isabel M. Pappé, *The Canadian Competition Act: A Leap Forward*, 22 INT'L LAW. 1071, 1074 (1988) ("[A]nticompetitive practices include a dominant firm or firms selling goods at a price that is lower than the acquisition cost.").

²⁴⁷ See Pappé, *supra* note 246, at 1072-73 (1988); William T. Stanbury, *The New Competition Act and Competition Tribunal Act: "Not with a Bang, But a Whimper"*, 12 CAN. BUS. L.J. 2, 37 (1986).

²⁴⁸ [1990] 32 C.P.R.3d 1 (Competition Tribunal).

²⁴⁹ NutraSweet, 32 C.P.R.3d at 28.

²⁵⁰ For an analysis of the issues other than predatory pricing in *NutraSweet*, see Paul Collins, *The Law and Economics of "Abuse of Dominant Position": An Analysis of NutraSweet*, 49 U. TORONTO FAC. L. REV. 275 (1991).

²⁵¹ Combines Investigation Act, R.S.C., ch. C-34, § 78(i) (1985) (Can.).

²⁵² NutraSweet, 32 C.P.R.3d at 43.

²⁵³ *Id.*

²⁵⁴ *Id.*; Donald N. Thompson, *NutraSweet: The Evolution of Law on Abuse of Dominant Position*, 18 CAN. BUS. L.J. 17, 34 (1991) (The Director's predatory pricing claim "failed because the Tribunal took the position that the language of the statute means that Parliament intended [Section 78(i)] to be applied to distribution (where articles are purchased for resale) and not to manufacturing situations.").

²⁵⁵ NutraSweet, 32 C.P.R.3d at 43.

exclusive.²⁵⁶ Consequently, the Tribunal found that other forms of predatory pricing could constitute predatory pricing.²⁵⁷ Relying heavily on Areeda and Turner's landmark article,²⁵⁸ the Tribunal indicated that only prices below average variable cost could be predatory.²⁵⁹ Although the Tribunal found NutraSweet had "a strong commercial motive to sell below cost,"²⁶⁰ it also found NutraSweet's prices exceeded its average variable cost.²⁶¹ Furthermore, the Tribunal felt even if NutraSweet's prices fell below cost, "it is highly unlikely that [NutraSweet] would be able to recoup from Canadian consumers the foregone profits resulting below-cost pricing."²⁶² Finally, the Tribunal concluded the Director had not asked for an appropriate remedy and refused to decide whether NutraSweet had engaged in predatory pricing.²⁶³

D. Summary and Critique

Consistency has not been the hallmark of predatory pricing law in Canada, and several commentators have criticized the current state of the law. After conducting an extensive examination of Canadian case law,²⁶⁴ McFetridge and

²⁵⁶ Combines Investigation Act, R.S.C., ch. C-34, § 78 ("For the purposes of section 79, 'anticompetitive acts,' *without restricting the generality of the term*, includes any of the following acts."); Hunter & Blakney, *supra* note 133, at 69 (Section 78 "is illustrative and not exhaustive of the restrictive and exclusionary activities the Act is aimed at preventing."); Grover & Kwinter, *supra* note 137, at 288 ("[T]he Act provides a non-exhaustive list of nine examples that the tribunal may have regard to in considering whether a dominant firm has abused its market position.").

²⁵⁷ NutraSweet, 32 C.P.R.3d at 43-44 ("The tribunal [sic] is satisfied that the term 'anti-competitive act' ... is broad enough to cover other predatory pricing.").

²⁵⁸ Areeda & Turner, *supra* note 38.

²⁵⁹ NutraSweet, 32 C.P.R. (3d) at 44.

²⁶⁰ *Id.* at 45; *cf.* Grover & Kwinter, *supra* note 137, at 289 (1987) (Since each of the nine anticompetitive acts listed in Section 78 refer "to some purpose, object, or design [to lessen competition or eliminate a competitor,] an element of intent must be demonstrated in respect to all forms of conduct alleged to constitute an anti-competitive practice."); Bruce C. McDonald, *Abuse of Dominant Position: A New Monopoly Law for Canada*, 32 ANTITRUST BULL. 795, 812 (1987).

²⁶¹ NutraSweet, 32 C.P.R.3d at 45. At different, the Tribunal vacillated between average *variable* and average *total* cost as the appropriate threshold. In reliance on Areeda and Turner, average variable cost was used as a proxy for the more accurate (but more difficult to ascertain) marginal cost. *Id.* at 44. The Tribunal stated that when a was producing at full capacity, average total cost "is obviously the better proxy." *Id.* There was some evidence that NutraSweet operated at capacity, but the decision does not state whether NutraSweet's prices exceeded average total cost.

²⁶² *Id.* at 45.

²⁶³ *Id.* at 45 (The Director "did not ask for any remedy concerning prices other than that they be forbidden to fall below 'acquisition cost,' a concept that we have found to be irrelevant to this case. Therefore a specific finding on selling below cost is not required in respect of any potential remedy.").

²⁶⁴ Donald G. McFetridge & Stanley Wong, *Predatory Pricing in Canada: The Law and the Economics*, 63 CAN. B. REV. 685 (1985).

Wong found the courts did not apply consistent tests for what constituted "unreasonably low prices" or "lessened competition."²⁶⁵ Although they recommend adoption of the Areeda-Turner test,²⁶⁶ McFetridge and Wong shared Chicago's skepticism about the existence of predatory pricing²⁶⁷ and expressed their own doubt "that the development of a workable jurisprudence in the area of abuse of dominant position is a reasonable prospect."²⁶⁸

More recently, Hunter and Hutton examined Canadian predatory pricing law, including the 1992 Guidelines.²⁶⁹ They generally welcomed the Guidelines as an "attempt to clarify the [Bureau of Competition Policy's] approach"²⁷⁰ to predatory pricing, and they believed that the Guidelines will prove "helpful to business people who suspect that their own or other's aggressive pricing policies may be illegal."²⁷¹ Nonetheless, Hunter and Hutton concluded that the Guidelines "fall short of their goals of providing practical business advice and an economically sound framework for legal analysis."²⁷² Their economic criticisms stemmed from their belief that, consistent with Chicago interpretations of United States antitrust law, "the underlying purpose of the Act [is] to enhance the efficiency of the Canadian economy by promoting competitive markets."²⁷³ Consequently, Hunter and Hutton criticized the Guidelines for failing "to distinguish between barriers which result from the greater efficiency of the incumbent firm and those which are

²⁶⁵ *Id.* at 699 (The cases "do not make it clear what is the test for determining if prices are 'unreasonably low,' or when the policy will, in general terms, be held to have lessened or been designed to lessen competition."); *see also* Warner, *supra* note 151, at 861 ("The meaning of 'unreasonably low' continues to baffle both courts and commentators.").

²⁶⁶ McFetridge & Wong, *supra* note 264, at 732 ("In our view the Areeda-Turner test is the least costly of these tests [for unreasonably low prices] in that it entails a low probability of convicting innocent behavior and requires relatively little in the way of information gathering, interpretation and enforcement effort.").

²⁶⁷ *Id.* at 733 ("If the leading [Canadian] cases are presumably the most glaring examples of predatory pricing to come to the attention of the government, then the inescapable conclusion is that the [predatory pricing law] is not needed.").

²⁶⁸ *Id.* at 733.

²⁶⁹ Lawson A.W. Hunter, Q.C. & Susan M. Hutton, *Is the Price Right?: Comments on the Predatory Pricing Enforcement Guidelines and Price Discrimination Enforcement Guidelines of the Bureau of Competition Policy*, 38 MCGILL L.J. 830 (1993).

²⁷⁰ *Id.* at 833.

²⁷¹ *Id.*

²⁷² *Id.*

²⁷³ *Id.* at 832. Hunter and Hutton's strong Chicago bias is seen throughout their work. For example, on the issue of predatory intent, they claim that "there is no real distinction between pro- and anti-competitive intent, and intent is of no practical use as an evaluative criterion in predatory pricing." *Id.* at 845. Furthermore, they argue that "'predatory' pricing is expected and welcome in a competitive market." *Id.* at 846.

due to outside influences or strategic firm behavior."²⁷⁴ Not surprisingly, they were also critical of the use of intent to determine whether prices are unreasonably low.²⁷⁵

These criticisms may go too far. First, as to consistency and predictability, the commentators are correct that the current state of the law fails to define the appropriate measure of cost. Nonetheless, the consistent thread throughout the case law, the Guidelines, and the *NutraSweet* decision is that prices above cost are legal *per se*. At a minimum, this means that a business cannot be held liable for predatory pricing so long as its price exceeds its average total cost.²⁷⁶ Furthermore, this is information within the control of the business, so that a business may easily determine whether its pricing policy is placing itself at risk. To be sure, the safe harbor of total costs may cause some overly cautious firms to avoid making legal price cuts. Yet these must be extraordinarily cautious firms, since none of the Canadian approaches to predatory pricing condemn below cost pricing *per se*. For example, as McFetridge and Wong concede, the criminal offense still requires "that there be a planned and *deliberate* course of actual selling for a sufficient length of time."²⁷⁷ Similarly, the objection of to use of intent ignores that the alleged predator's intent is only one element of the predatory pricing case.²⁷⁸

The economic criticisms all share a similar problem in that they are based on the erroneous premise that the Act's sole purpose is to promote economic efficiency. As noted *supra*, the Act expressly a variety of other goals including such as "to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy."²⁷⁹ This multiplicity of goals is also reflected in the statutory offenses themselves.

²⁷⁴ *Id.* at 863. "Only the later possibly pose a threat to efficient *competition*, as opposed to inefficient *competitors*." *Id.* (emphasis in the original).

²⁷⁵ *Id.* at 864 ("In our view, the intent of the alleged predator is irrelevant for the purpose of determining if its prices are unreasonably low. ... We lament the inclusion of intent analysis of whether the prices are 'unreasonably low.'") Commenting on the role of intent to prove abuse dominant position, one commentator objected that it is "notoriously difficult to distill a corporate intent from a variety of internal memoranda and other communications by employees expressing personal views in the course of the decision-making process within the corporation." Bruce C. McDonald, *supra* note 260, at 813. This same commentator also objected that intent had no bearing on what he believed to be the critical issue, whether the conduct lessened competition. *Id.* at 814.

²⁷⁶ Referring specifically to Section 50(1)(c), one commentator observed that a "sale above 'cost' cannot be an anti-competitive act." Grover & Kwinter, *supra* note 137, at 294. This is, of course, explicitly stated in Section 78(i) definition predatory pricing.

²⁷⁷ McFetridge & Wong, *supra* note 264, at 699 (emphasis added).

²⁷⁸ In an abuse of dominant position case, for example, the Director must also fill the "tall order" of showing that the defendant or defendants "have substantial or complete control of the market [and] have the effects of substantially lessening competition." Stanbury, *supra* note 247, at 34.

²⁷⁹ Combines Investigation Act, R.S.C., ch. C-34, § 1.1 (1985) (Can.).

Section 50(1)(c) prohibits unreasonably low prices that have “the effect or tendency of substantially lessening competition or eliminating a competitor . . . , or designed to have such effect.”²⁸⁰ Similarly, Section 78(i) prohibits below cost pricing “for the purpose or disciplining or eliminating a competitor.”²⁸¹ The language of “design” in Section 50(1)(c) and “purpose” in Section 78(i) requires an examination of subjective intent regardless of economic effects. Furthermore, even if one equates “competition” with economic efficiency as adherents of the Chicago School do, Sections 50(1)(b) and 78(i) both require examination of the conduct’s impact on *competitors*. The Act provides no basis for the courts or the Tribunal to let economic efficiency override these other goals.

IV. COMPARISON OF PREDATORY PRICING LAW IN THE UNITED STATES AND CANADA

Perhaps the best way to understand the differences and similarities between predatory law in Canada and the United States is to look at how the law of each country would treat particular cases. Predatory pricing law in the United States begins requires an analysis of two factors: whether the cost of the goods sold exceed their price and whether the seller had a reasonable prospect of recouping the loss through future sales at supracompetitive prices. The government’s case in *Consumers Glass* probably would have failed under both prongs. Although the defendant’s prices fell below average total cost,²⁸² the found that the defendant’s prices always exceeded average variable cost.²⁸³ Given the ease with which firms could enter and exit the market in question,²⁸⁴ the defendant could have no hope of recoupment.

The government succeeded in establishing below-cost pricing in *Hoffman-La Roche*, but recoupment requires a lessening of competition and the trial court expressed deep skepticism that the government could have proven this.²⁸⁵ The underlying facts support the dubious prospects for recoupment. Although the defendant held patents for products in question, the Canadian federal government required the defendant to license its patents to its competitors for a relatively small royalty.²⁸⁶ According to the trial court, this

²⁸⁰ Combines Investigation Act, R.S.C., ch. C-34, § 50(1)(c) (1985) (Can.).

²⁸¹ Combines Investigation Act, R.S.C., ch. C-34, § 78(i) (1985) (Can.).

²⁸² *Consumers Glass*, 33 O.R.2d at 254.

²⁸³ *Id.* at 255.

²⁸⁴ *Id.* at 232.

²⁸⁵ *Hoffman-La Roche*, 28 O.R.2d at 205-06.

²⁸⁶ *Id.* at 171.

created “an atmosphere of vigorous competition.”²⁸⁷ Consequently, any attempt by the defendant to recoup its losses by raising prices above competitive levels would have triggered entry into the market by other pharmaceutical firms.

In *NutraSweet*, the Tribunal did find high barriers to entry²⁸⁸ which might support a conclusion that recoupment was feasible. Nonetheless, the Tribunal expressed some skepticism as to whether the defendant engaged in below-cost pricing.²⁸⁹ Given the hostility to predatory pricing claims under the current state of the law in the United States, it seems unlikely that a court would interpret the ambiguous facts regarding costs in *NutraSweet* to support the government’s case. In short, it seems likely that the defendants in all three major cases would have prevailed under the law in the United States. This is a reversal of the outcome only in the *Hoffman-La Roche* case.

Application of Canadian law to the facts in *Brooke Group* reveals a sharper contrast between the different approaches of the two countries. This is so even though one must concede that it appears unlikely the abuse of dominant position would apply to the defendant in *Brooke Group*. The *NutraSweet* decision indicates that the Tribunal will not apply Section 78(i) to manufacturing situations.²⁹⁰ Even if the Tribunal would to treat below-cost pricing by a manufacturer as an anticompetitive act, abuse of dominant position requires that the defendant “substantially or completely” controls “a class or species of business” in Canada.²⁹¹ In the antitrust parlance of the United States, the defendant must have market or monopoly power.²⁹² Of the six firms with a significant presence in the United States market, the defendant in *Brooke Group* ranked a “distant third, its market share never exceeding 12 [percent].”²⁹³ By contrast, the two largest firms had a combined market share of 68 percent.²⁹⁴ Assuming that firms held similar shares of the Canadian market, it does not seem plausible that the defendant could exercise monopoly power.²⁹⁵

²⁸⁷ *Id.* at 172.

²⁸⁸ *NutraSweet*, 32 C.P.R.3d at 27.

²⁸⁹ *Id.* at 44-45.

²⁹⁰ See Thompson, *supra* note 254, at 34.

²⁹¹ Combines Investigation Act, R.S.C., ch. C-34, § 79(1)(a) (1985) (Can.).

²⁹² See *NutraSweet*, 32 C.P.R.3d at 28 ([T]he Tribunal accepted the respondent’s argument that “control” under Section 79 meant “market power” which “is generally accepted to mean an ability to set prices above competitive levels for a considerable period.”); McDonald, *supra* note 260, at 801 (“The question of ‘control’ ... is a question of market power.”).

²⁹³ 509 U.S. at 213.

²⁹⁴ *Id.* at 213 (“R.J. Reynolds and Philip Morris, the two industry leaders, enjoyed respective market shares of about 28 [percent] and 40 [percent].”).

²⁹⁵ The repealed definition of “monopoly” under the old Combines Investigation Act contained

The defendant's lack of a dominant position does not affect a predatory pricing claim under the criminal provisions of the Act. Indeed, it would appear that the defendant's conduct in *Brooke Group* would have satisfied all the elements under Section 50(1)(c). First, it almost goes without saying that the defendant in *Brooke Group*, a cigarette manufacturer, was engaged in a business, i.e., the business of manufacturing cigarettes.²⁹⁶ Second, the defendant's conduct constituted a policy of selling the articles in question, i.e., the cigarettes. For eighteen months, the defendant sold its generic cigarettes at prices below its costs.²⁹⁷ Moreover, the conduct was no accident.²⁹⁸ Not only did the defendant repeatedly adjust its wholesale discounts,²⁹⁹ the trial court in *Brooke Group* found that the "corporate planning documents written by top executives" of the defendant's buttressed the plaintiff's description of the conduct.³⁰⁰ In short, the defendant engaged in a deliberate program of pricing in the market for a significant period of time.³⁰¹ With respect to the third element of the criminal offense, unreasonably low prices, *Brooke Group* found "sufficient evidence" that the defendant's prices "were below its costs."³⁰² If one assumes that by "costs" *Brooke Group* meant average variable costs, then the defendant's prices clearly fell outside the safe harbor

almost the same language as "control" provision of Section 79 of the current Act, and the court in *Consumers Glass Co. Ltd.*, 29 C.P.R.2d 1 indicated that a firms who jointly coordinated their activities might have sufficient control over a market to constitute a shared monopoly. However, the Tribunal has tendered to interpret the current Act narrowly. *See Canada (Director of Investigation and Research) v. NutraSweet Co.*, 32 C.P.R.3d 1 (Holding that the express predatory pricing provisions under abuse of dominant position were limited to purchases for resale.); *Canada (Director of Investigation and Research) v. Warner Music Canada Ltd.*, [1997] 78 C.P.R.3d 321 (Holding that the Act's prohibition of refusals to deal did not extend to copyright licenses.). Consequently, it seems unlikely that the Tribunal would aggressively interpret the definition of "control." *But see Stanbury, supra* note 247, at 31 ("The Department of Consumer and Corporate Affairs in its clause-by-clause analysis of Bill C-29, which used the same language [as Section 79 of the Act], argued that substantial control is not intended to mean virtual or complete control. Rather, such a degree of control refers to sufficient market power to influence price by jointly restricting output."); *McDonald, supra* note 260, at 802-06 (Outlining the possible elements necessary to prove joint dominance.).

²⁹⁶ *See* 509 U.S. at 212-213.

²⁹⁷ *See id.* at 231.

²⁹⁸ *Cf. Hoffman-La Roche*, 28 O.R.2d at 193 ("It is not enough for a violation of this section to sell a few articles accidentally at an unreasonably low price.").

²⁹⁹ *See* 509 U.S. at 215-217.

³⁰⁰ *Liggett Group, Inc. v. Brown & Williamson Tobacco Corp.*, 748 F. Supp. 344, 354 (M.D.N.C. 1990).

³⁰¹ *Cf. Guidelines, supra* note 144, at ii ("[A] policy of selling" requires evidence "that the prices are part of deliberate corporate program of pricing in the market and that they are in effect for a significant duration of time."); *Hoffman-La Roche*, 28 O.R.2d at 193 ("[T]he selling must be as a result of a conscious decision to do so [and] the selling must be continuing or repeated sales.").

³⁰² 509 U.S. at 231.

of above cost pricing under all the approaches to unreasonably low prices. Although *Consumers Glass* established that prices above average variable cost cannot constitute unreasonably low prices, the case does not give any guidance when, as in *Brooke Group*, prices fall below cost.

Hoffman-La Roche, on the other hand, required examination of three additional factors. First, as to the length of time, *Hoffman-La Roche* indicated that six months of below cost pricing favored a conclusion of unreasonableness. The defendant in *Brooke Group* engaged in below cost pricing for eighteen months. Second, *Hoffman-La Roche* indicated that the court must consider "the circumstances of the sale."³⁰³ The facts in *Brooke Group* are subject to interpretation on this point. The defendant in *Brooke Group* could characterize its price cuts as a defensive reaction to the plaintiff's low cost generics, and unlike the defendant in *Hoffman-La Roche*, it did not drop its prices to zero. Alternatively, and also unlike the *Hoffman-La Roche* defendant, the *Brooke Group* defendant could argue that it used below cost pricing to enter a market. Nonetheless, the considerable evidence existed that the defendant in *Brooke Group* dropped its generic below its costs not to gain a foothold in that market but rather to punish the plaintiff for creating the generic market in the first place.³⁰⁴

Finally, no external or long term economic benefits as defined by the trial court in *Hoffman-La Roche* accrued the benefit of the *Brooke Group* defendant.³⁰⁵ *Brooke Group* gives no indication price cuts were necessary to stave bankruptcy, and almost by definition, the defendant's prices in the generic market could do little to garner prestige.³⁰⁶ On balance, therefore, it would seem that the defendant in *Brooke Group* charged unreasonably low prices under the *Hoffman-La Roche* standard.

As previously noted, the Guidelines' analysis of prices below costs deviates substantially from the *Hoffman-La Roche* standard. First, the Guidelines look for evidence of sufficient market power to recoup its losses from a successful predatory pricing campaign, the very ground on which the plaintiff's case foundered in *Brooke Group*. The Guidelines suggest the alleged predator must have at least a 35 percent market share to exercise the

³⁰³ *Hoffman-La Roche*, 28 O.R.2d at 201.

³⁰⁴ See 509 U.S. at 231 (Noting that a reasonable jury could conclude that the defendant "envisioned or intended [the] anticompetitive course of events" alleged by the plaintiff.).

³⁰⁵ The defendant, to be sure, did subsequently enjoy the benefits of an end to vigorous price competition in the generic market and a reduction in competition in the branded market from generics. Nonetheless, *Brooke Group* concluded that this had nothing to do with defendant's below cost pricing. Furthermore, for a reduction in competition to constitute a long-term benefit would stand competition law on its head.

³⁰⁶ See *Hoffman-La Roche*, 28 O.R.2d at 201.

requisite market share.³⁰⁷ The *Brooke Group* defendant only had an 11.4 percent market share.³⁰⁸ Nonetheless, “[a] conclusive finding depends on the assessment of the conditions of entry into an industry.”³⁰⁹ Although *Brooke Group* largely ignored conditions of entry into the cigarette market, critics of *Brooke Group* point out the cigarette industry has a history of strategic behavior which the Guidelines might treat as a barrier to entry.³¹⁰ Finally, given the conflicting inferences drawn from the defendant’s low market share and the history of strategic behavior in the industry, the Guidelines would look to more subjective factors, including evidence of predatory intent.³¹¹ On this point, it should again be noted that *Brooke Group* found that a reasonable jury could conclude that the defendant had predatory intent.³¹²

The final element seeks to determine whether the defendant either caused or intended to cause substantial lessening of competition or the elimination of a competitor. *Brooke Group* specifically held the plaintiff “has failed to demonstrate competitive injury.”³¹³ Although the Guidelines focus primarily on the competitive impact prong of this element,³¹⁴ both the Guidelines and *Hoffman-La Roche* make it clear that testimonial and documentary evidence of subjective intent will suffice.³¹⁵ It bears repetition that the *Brooke Group* did find sufficient evidence of predatory intent,³¹⁶ the trial court in *Brooke Group* described the evidence of subjective predatory intent as “more voluminous and detailed than any other reported case.”³¹⁷ More specifically, the evidence showed not only that the defendant “wanted to injure [the plaintiff], it also details an extensive plan to slow the growth of the generic cigarette segment.”³¹⁸

In short, application of the Canadian competition law to the facts outlined in *Brooke Group* suggest a result entirely the opposite of that reached by the United States Supreme Court. The key to this outcome is that Canadian competition law would consider evidence of two things that *Brooke Group*

³⁰⁷ Guidelines, *supra* note 144, at 6.

³⁰⁸ See 509 U.S. at 214.

³⁰⁹ Guidelines, *supra* note 144, at 7.

³¹⁰ *Id.* at 10.

³¹¹ See *id.*

³¹² See 509 U.S. at 231.

³¹³ *Id.*

³¹⁴ See Guidelines, *supra* note 144, at 12-13.

³¹⁵ See *id.* at 13; *Hoffman-La Roche*, 28 O.R.2d at 205-13.

³¹⁶ See 509 U.S. at 231.

³¹⁷ *Liggett Group, Inc. v. Brown & Williamson Tobacco Corp.*, 748 F. Supp. 344, 354 (M.D.N.C.

1990).

³¹⁸ *Id.*

treated as irrelevant, the history of strategic behavior in the cigarette industry and the evidence of the defendant's subjective intent.

V. CONCLUSION

Without question, predatory pricing law in the United States and Canada have much in common. Both countries, for example, limit predatory pricing to sales below cost. Furthermore, neither country has developed and applied a consistent measure of cost. These and other similarities notwithstanding, significant differences exist between the Canadian and United States approaches to predatory pricing.

Although *NutraSweet* indicates recoupment plays a role in assessing the predatory nature of low prices, the overall approach taken by the Tribunal, including its reference to predatory intent as both plausible and relevant, strongly suggest that recoupment does not play the central role in Canadian law the way it does in United States law. In this respect, Canadian law seems much closer to the approach used by state below-cost sales statutes, than it does to the dominant federal antitrust law.³¹⁹

Second, Canadian predatory pricing law does offer a distinct alternative to the Chicago approach. Although efficiency and recoupment concerns are not rejected in the Canadian approach, issues of intent and protection of competitors play an explicit role in the evaluation of pricing conduct. Indeed, the Competition Act expressly states that one of its purposes is "to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the Canadian economy."³²⁰ Thus, those who seek an alternative path for United States antitrust law may well find it in Canadian jurisprudence.

³¹⁹ See, Norman W. Hawker, *Wal-Mart and the Divergence of State and Federal Predatory Pricing Law*, 15 J. PUB. POL'Y & MARKETING 141 (1996).

³²⁰ Combines Investigation Act, R.S.C., ch. C-34, § 1.1 (1985) (Can.).