

LePage's v. 3M: Five Ingredients in Search of a Monopoly Broth

Ronald W. Davis

By accepting the government's recommendation to deny certiorari¹ in *LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003), *cert. denied*, 124 S. Ct. 2932 (2004), the Supreme Court let stand an en banc Third Circuit back-to-the-future opinion endorsing an expansive and controversial view of the law of monopolization. The appellate court's analytical errors—errors as much of omission as of commission—have given us a precedent that has much potential for mischief.

To illustrate why the decision in *LePage's* creates practical problems, this article explores a not-so-hypothetical hypothetical. First, however, some clarifying thoughts about what this article is and is not about; then, a hard look at those missing ingredients in the Third Circuit's monopoly broth.

Let Me Be Clear

Flawed as it is, *LePage's* has its strong defenders—who tend to praise what they see as the justice of the outcome as between the two litigants, rather than the acuteness of the court's legal analysis.² Thus, in discussing *LePage's* it is important to be clear about whether one is defending the legality of 3M's conduct or defending the court's analysis. So let me make several points, just to be clear.

As an outside observer—I have no dog in this fight—3M's business strategy against *LePage's* seems to have been imprudent. 3M, moreover, should not have assumed that the mere fact that it sold above cost would carry the day in litigation. (That was their story, and they were sticking to it). A litigation victory for the plaintiff should have come as no big surprise. This article does not attempt to prove that the wrong side won the case. Conceivably, the appellate court might have written an analytically sound opinion upholding the jury verdict for *LePage's*. Whether or not that is so is beyond the scope of this article.

This article tells no "narrative" of efficient monopolists engaged in hard, manly competition against inefficient, whiny, smaller competitors.³ One will find no argument here in favor of a simple—or simplistic, if one prefers that word—rule of thumb for deciding bundling cases, such as that bundled discounts and rebates are per se lawful if they are above cost, or if the injured competitor is less efficient, or if the monopolist's plan involves no sacrifice of profits in the short term, or if the monopolist's customers are not "coerced." And no argument is advanced that the legal system owes a duty toward monopolists to create unambiguous rules of per se legality to afford a safe harbor for bundled discount programs or other arguably exclusionary strategies.

■
Ronald W. Davis

is a solo antitrust practitioner in Atlanta, Georgia, and Developments Editor of Antitrust magazine.

¹ Brief for the United States as Amicus Curiae, available at <http://www.usdoj.gov/atr/cases/f203900/203900.pdf>. Denial of certiorari followed soon after the agencies filed their amicus brief recommending that the Court not take the case.

² See PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 749 (Supp. 2004); Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 ANTITRUST L.J. 3 (2004).

³ See Gavil, *supra* note 2, at 34.

It is not my purpose to dispute that strategies employed by monopolists that create, preserve, or extend monopoly power merit careful antitrust scrutiny. No fault is found with those who argue that Supreme Court dicta in cases like *Brooke Group*⁴ and *Trinko*⁵ is too friendly in tone toward monopolists.

All those things said, the en banc Third Circuit court in *LePage's* has served up a monopoly broth with almost no ingredients. And that is a big problem. The Supreme Court's decision to deny certiorari was problematic, but my point is not to quarrel with that decision. It is to illustrate how *LePage's* can create adverse real world effects.

3M's Strategy

In 1992, concerned about the success of LePage's in the private label transparent tape business, 3M adopted an aggressive stance, entering into a series of deals with large buyers like Wal-Mart and Staples. The terms varied from deal to deal, but generally involved bundled rebate programs, where 3M set a customer-specific target growth rate for each of six product lines—including Scotch™ transparent tape and PostIt™ repositionable notes, two strong 3M brands. In these deals customers had to achieve the target growth in *each* line in order to get a rebate. Sometimes the only practical way in which a customer could meet 3M's target was to drop LePage's tape. Very few of these arrangements involved any contractual commitment to exclusivity, and the jury found for the defendant on LePage's claim of unlawful exclusive dealing under Clayton Act Section 3. 324 F.3d at 145.

The en banc Third Circuit court in LePage's has served up a monopoly broth with almost no ingredients.

There was no suggestion that 3M priced below cost. LePage's problem was that if a customer bought any substantial amount of LePage's private label tape, the customer would not meet its 3M "target" in one product line—and the failure to meet the target in one line would, in turn, result in loss of the rebate on *all six* 3M product lines.

The bundled rebates were modest in percentage terms, but significant in dollars, representing up to \$1 million or more per year for large customers.

To meet or beat 3M's bundled discounting, LePage's would have had to cut its price substantially, and this it was unwilling to do. Following the adoption of 3M's new strategy, LePage's share of the overall transparent tape business decreased from 14.4 percent to 9.35 percent. At the time of trial LePage's had been in the red for three years, but it still had two thirds of U.S. private label transparent tape sales. 324 F.3d at 161–62, 170.

The jury found 3M liable for monopolization, with single damages of \$23 million based on lost profits. Reversing an earlier three-judge panel decision, 277 F.3d 365 (3d Cir. 2002), in 2003 the Third Circuit, sitting en banc, affirmed the verdict.

Throughout the litigation 3M clung tenaciously to the position that there is no legal distinction between an above-cost bundled discount and an above-cost unbundled discount—and that, based on *Brooke Group*, no price above cost, bundled or not, can support liability under Sherman Act Section 2. It did not matter, said 3M, that its documents showed an intent to drive LePage's from the market, and perhaps thereafter to raise prices. Nor did it matter whether 3M's scheme was likely to succeed. It did not matter whether barriers to entry were high, and it did not matter if LePage's ultimate demise would leave 3M with 100 percent of a relevant market. Pricing above cost is per se legal. That was 3M's position.

⁴ *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993).

⁵ *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004).

Rising to the bait, the en banc court identified the validity of 3M's per se legality argument as “the most significant legal issue in this case,” 324 F.3d at 147, and rejected it root and branch. The court took inspiration from the spirit of *Alcoa*⁶ and other classic monopolization authorities. *Id.* at 147–51. It found a host of reasons to distinguish—and to dismiss—the Supreme Court's decision in *Brooke Group*: the case was an aberration, *id.* at 151–52; it dealt with simple price cutting, not bundling, *id.* at 151; and, most remarkably—despite Justice Kennedy's high dictum in *Brooke Group* indicating that this Robinson-Patman decision should apply, as well, to the law of monopolization—the Third Circuit allowed as how “nothing in [*Brooke*] suggests that its discussion of the issue is applicable to a monopolist with its unrestrained market power.” *Id.*⁷

The court found that 3M's bundled rebate program illegally denied market share to the plaintiff. *Id.* at 155. Invoking the “monopoly broth” tradition of antitrust jurisprudence, the Third Circuit observed:

The effect of 3M's conduct in strengthening its monopoly position by destroying competition by LePage's in second-tier tape is most apparent when 3M's various activities are considered as a whole. The anti-competitive effect of 3M's exclusive dealing arrangements, whether explicit or inferred, cannot be separated from the effect of its bundled rebates. 3M's bundling of its products via its rebate programs reinforced the exclusionary effect of those programs.

Id. at 162.

Some look kindly on the Third Circuit's approach, believing it to be well within the mainstream of antitrust's traditionally strict scrutiny of the aggressive business practices of monopolists. Others, including myself, view it with alarm.⁸

A Flavorless Monopoly Broth

In *MCI v. AT&T*, 708 F.2d 1081, 1177 (7th Cir. 1983), the court said that “[i]f you really wanted to know what caused the unsavory flavor of the monopoly broth, you would not just audit the chef's books of account; you would also take a look at his recipe.” The Third Circuit's recipe in *LePage's* for Monopoly Broth lacks five key ingredients.

1. Foreclosure by Exclusive Dealing Contracts. A classic monopolist's ploy is to foreclose substantial market share, for a substantial period of time, using a series of parallel exclusive dealing contracts—contracts that put the buyer in breach if it chooses to do business on the merits with a competing seller. But 3M did not do that. Its two exclusive dealing contracts were not material to the case, see 324 F.3d at 157, and the jury found for 3M on the claim of illegal exclusive dealing. *Id.*

Some have argued that the antitrust concept of exclusive dealing should extend to “partial exclusive dealing” arrangements where, for example, a buyer promises to buy a significant percentage (though less than all) of its requirements from a specific seller. Maybe, even, stretching

⁶ *United States v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945).

⁷ This sweeping assertion came as a shock to the antitrust bar, including the federal agencies, see Brief for the United States, *supra* note 1, at 14–15 n.11, not to mention the authors of the chapter on monopolization in both the fourth and fifth editions of ABA ANTITRUST SECTION, ANTITRUST LAW DEVELOPMENTS (4th ed. 1997 & 5th ed. 2002), who relied heavily on *Brooke Group* in describing the black letter law of predation as a Sherman Act Section 2 violation.

⁸ See David L. Meyer, *LePage's II: The Third Circuit Revisits 3M's Bundled Discounts and Sees Unlawful “Exclusion” Instead of Below-Cost Pricing*, ANTITRUST SOURCE, July 2003, available at <http://www.abanet.org/antitrust/source/july03/meyer.pdf>; Joanna Warren, *Comment, LePage's v. 3M: An Antitrust Analysis of Loyalty Rebates*, 79 N.Y.U. L. REV. 1605 (2004); Ronald W. Davis, *LePage's v. 3M: What Will Stick from the Tape Case?*, Discussion Paper Prepared for ABA Antitrust Section Teleseminar on “Buying Loyalty” (June 10, 2003).

a little further, antitrust might label as “exclusive dealing” a situation where the buyer promises nothing, but the seller provides a discount *conditioned* on the buyer’s purchasing, say, 60 percent of its requirements from the discounting seller.⁹

Significantly, however, the en banc majority in *LePage’s* did not seem to think that “exclusive dealing” requires a legally binding promise of exclusivity or a discount conditioned on exclusivity. According to *LePage’s*, all that is needed is an offer that is too good to refuse—an offer so attractive that a buyer chooses to buy from the party making the offer, to the exclusion of other sellers, whose offers are less attractive. The court seemed to ground liability not on a promise elicited from the buyer, or on a condition imposed by the seller, but simply in the seller’s *intent* to make an offer so attractive that it would “exclude” others—as the court put it, “payments to many of the larger customers that were designed to achieve sole-source supplier status.” 324 F.3d at 157.¹⁰

That is what the court said. Did it really *mean* that neither a promise nor a condition is necessary to invoke “exclusive dealing,” only a really, really attractive offer? Enquiring minds want to know. They will not find out by reading the opinion. In a decision that is analytically weak overall, the discussion of exclusivity is the very weakest point.

2. Foreclosure by Tying and De Facto Tying. Like true exclusive dealing, refusal to sell a desired product unless the customer also takes an undesired product—a product it would not otherwise choose on the basis of price, quality, and service alone—is a kind of foreclosure: it artificially interferes with competition on the merits of price and quality. This kind of foreclosure is called tying. 3M did not do that.

A bundled offer that is so much more attractive than the unbundled alternative as to make the unbundled option illusory—in other words, *de facto* tying—may have the same adverse effect on customer freedom of choice as literal tying.¹¹ But *LePage’s* elected not to pursue any claim of literal or *de facto* tying.¹²

I make ice cream. I use the secret Davis family formula, and my ice cream is unusually good. Also, I have learned to produce my ice cream very efficiently and thus I can sell my product at a low price and still make money. But I make and sell only one flavor, vanilla. My competitor down the street sells average tasting ice cream and charges more than I charge. But she sells three flavors, vanilla, strawberry, and chocolate, and she gives a 5 percent discount to customers who buy

⁹ See Willard K. Tom, David A. Balto, & Neal W. Averitt, *Anticompetitive Aspects of Market Share Discounts and Other Incentives to Exclusive Dealing*, 67 ANTITRUST L.J. 615 (2000); see also Richard M. Steuer, *Discounts and Exclusive Dealing*, ANTITRUST, Spring 1993, at 28.

¹⁰ See also *id.* at 158: “*LePage’s* introduced powerful evidence that could have led the jury to believe that rebates and discounts to Kmart, Staples, Sam’s Club, National Office Buyers and ‘UDI’ were designed to induce them to award business to 3M to the exclusion of *LePage’s*.” Again, the court focused on 3M’s intent to gain all the business, not on any contractual promise it may have elicited, or on any gentlemen’s agreement, or even on any specific condition that 3M may have imposed.

¹¹ See generally 1 ABA ANTITRUST SECTION, ANTITRUST LAW DEVELOPMENTS 190–94 (5th ed. 2002). Kenneth Glazer and Brian Henry have argued that liability in a *LePage’s* type of scenario should turn on whether customers were coerced to enter rebate deals. Kenneth L. Glazer & Brian Henry, *Coercive v. Incentivizing Conduct: A Way out of the Section 2 Impasse?* ANTITRUST, Fall 2003, at 45. Compare Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 339 (2002) (buyer consent should not matter). Whatever may be the merits of distinguishing between coerced and willing customers in this context, this is not the distinction I am drawing. Even a customer that willingly and freely binds itself to buy exclusively from a particular seller for a substantial period of time is foreclosed, i.e., may not choose to buy from some other supplier “on the merits” of price and quality, as long as the contractual obligation remains in effect. Simply choosing to buy everything from supplier A on the merits, without such legal foreclosure, is a horse of a very different color.

¹² The narrative portion of the complaint characterized 3M’s bundled rebates as “tying” or “*de facto* tying,” but, inasmuch as 3M never refused to sell any product on an unbundled basis, *LePage’s* dropped the charge of “*per se* illegal” tying, and hung its hat, instead, on the argument that bundling is *analogous* to tying, a position the court accepted. 324 F.3d at 155.

all three as a bundle. She wins some sales from me because some customers prefer one-stop shopping and some like the bundled price. I win some sales from her because some customers only like vanilla, enjoy my secret family recipe, and like my price.

Could I say that I am “foreclosed” from selling to customers who want all three flavors? Could my competitor say that she is “foreclosed” from selling to customers who prefer vanilla ice cream made with my secret formula? Yes to both questions, but only if we speak in a misleadingly imprecise way. In the hypothetical, no one has interfered with a customer’s freedom to choose on the merits. My competitor and I are simply relying on our respective competitive strengths to win sales by making our offerings as attractive as possible.

3. Inability to Compete Effectively. Because its product line was much smaller in scope than 3M’s, LePage’s was literally unable to compete by offering a similar bundled rebate program. At least theoretically, however, LePage’s could have offered an economically equivalent (or superior) counteroffer by cutting the price of its tape by some large amount.¹³ Whether it “could” have done so and made enough money to stay in business is a different question. Justice Greenberg, dissenting from the majority opinion in *LePage’s*, contrasted LePage’s case with that of *SmithKline*¹⁴ in a 1978 bundled discount case:

SmithKline *showed* that it could not compete by explaining how much it would have had to lower prices for both small and big customers to do so. SmithKline ascertained the rebates that Lilly was giving to customers on all three products and calculated how much it would have had to lower the price of its product if the rebates were all attributed to the one competitive product. In contrast, LePage’s did not even attempt to show that it could not compete by calculating the discount that it would have had to provide in order to match the discounts offered by 3M through its bundled rebates, and thus its brief does not point to evidence along such lines. . . . [I]t is critically important to recognize that LePage’s had 67% of the private label business at the time of the trial. Thus, notwithstanding 3M’s rebates, LePage’s was able to retain most of the private label business. In the circumstances, it is ironic that LePage’s complains of 3M’s use of monopoly power as the undisputed fact is that LePage’s, not 3M, was the dominant supplier of private label tape both before and after 3M initiated its rebate programs. Indeed, the record suggests that inasmuch as LePage’s could not make a profit with a 67% share of the private label sales, it must have needed to be essentially the exclusive supplier of such tape for its business to be profitable as it in fact was when it had an 88% share of the private label tape sales business.

324 F.3d at 175–76.

In contrast, the *LePage’s* majority cited *SmithKline* with approval, 324 F.3d at 155–56, but failed to mention that the plaintiff in that case was rendered unable to compete by the defendant’s bundled discount program, or to address the distinction drawn by Judge Greenberg in dissent. The *LePage’s* majority likewise did not deal with another key case, *Ortho Diagnostic Systems, Inc. v. Abbott Laboratories, Inc.*, 920 F. Supp. 455 (S.D.N.Y. 1996), in which

[t]he district court stated that to prevail on a monopolization claim in “a case in which a monopolist (1) faces competition on only part of a complementary group of products, (2) offers the products both as a package and individually, and (3) effectively forces its competitors to absorb the differential between the

¹³ Cutting price would have increased LePage’s sales volume but lowered its profit on each unit. The net result of such a low price strategy *might* have driven LePage’s hopelessly into the red—making a low price strategy totally unrealistic. On the other hand, selling a greater volume of tape at reduced unit profit *might* have been an entirely feasible response for LePage’s. Which of these two different scenarios—a potentially successful low price, high volume strategy, or a low price strategy foredoomed to failure—actually describes the choices LePage’s faced? Based on the information given in the opinion, no one can say.

¹⁴ *SmithKline Corp. v. Eli Lilly & Co.*, 575 F.2d 1056 (3d Cir. 1978).

bundled and unbundled prices of the product in which the monopolist has market power,” the plaintiff must allege and prove “either that (a) the monopolist has priced below its average variable cost or (b) the plaintiff is at least as efficient a producer of the competitive product as the defendant, but that *the defendant’s pricing makes it unprofitable for the plaintiff to continue to produce.*”¹⁵

The majority in *LePage’s* did, however, cite (with approval) the 2002 Hovenkamp *Supplement* to the *Antitrust Law* treatise.¹⁶ The current (2004) *Supplement* to the treatise discusses the en banc decision in *LePage’s*, straining to reconcile the opinion with Professor Hovenkamp’s own, more restrictive view. Hovenkamp paraphrases the court as concluding, “although without offering specific numbers, that an equally efficient rival offering only a single product, tape, could not profitably match the defendant’s discounts.” However, as discussed further below, the discussion in the 2004 *Supplement* advocates a more precise, limited, and nuanced antitrust rule on strategic bundling than any to be derived from the Third Circuit’s decision.¹⁷

To sum up: Would *LePage’s* actually have been able to make an economically attractive counter offer to 3M’s bundled rebate program and still operate profitably? It is unclear.

Did the majority care one way or the other? Clearly it did not. (Otherwise, why would the majority ignore the issue of the plaintiff’s ability or inability to compete, of which the dissent made such a big deal?)

Would it be fair for a future plaintiff to cite *LePage’s* for the proposition that, contrary to *Ortho* and *SmithKline*, it is irrelevant whether or not the plaintiff can match the bundled offer made by the monopolist defendant? Yes, it would.

4. Past Consumer Injury. Often, illegally exclusionary conduct harms both competitors or potential competitors and consumers. Direct purchasers who pay a monopoly overcharge as a result of the exclusion of potential competitors suffer “antitrust injury” and have a claim for damages.¹⁸ A competitor forced to exit a market by illegally predatory or exclusionary means likewise suffers antitrust injury in the form of lost profits.¹⁹ By contrast, unilateral “exclusionary” conduct that has not harmed consumers in the past, and does not threaten (to a legally sufficient degree of probability) to harm them in the future cannot be a basis for liability to a competitor under Sherman Act Section 2. As the Supreme Court said in *Aspen Skiing*,²⁰ “The question *whether Ski Co.’s conduct may properly be characterized as exclusionary cannot be answered by simply considering its effect on [the plaintiff]*. In addition, it is relevant to consider its impact on consumers and whether it has impaired competition in an unnecessarily restrictive way.” 472 U.S. at 605 (emphasis added). In *Aspen Skiing*, liability was based on the plaintiff’s having been “crippled” competitively, in a case where the source of the crippling—the defendant’s deprivation of the plaintiff’s

¹⁵ 324 F.3d at 177 (dissent) (citing 920 F. Supp. at 469) (emphasis added).

¹⁶ 324 F.3d at 155 (citing PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 749 at 83 (Supp. 2002)).

¹⁷ AREEDA & HOVENKAMP, *supra* note 2, at 182–84. Despite its inability to advocate a black letter rule on bundled rebates, the Antitrust Division likewise seems to attribute significance to the ability or inability of a plaintiff to match the offer. In its amicus brief opposing certiorari it wrote that

a bundled rebate or discount can—under certain theoretical assumptions—exclude an equally efficient competitor, if the competitor competes with respect to but one component of the bundle and cannot profitably match the discount aggregated over the other products, even if the post-discount prices for both the bundle as a whole and each of its components are above cost.

Brief for the United States, *supra* note 1, at 13.

¹⁸ See *Hanover Shoe, Inc. v. United Shoe Mach. Corp.*, 392 U.S. 481 (1968).

¹⁹ See, e.g., *Midwest Gas Servs., Inc. v. Indiana Gas Co.*, 317 F.3d 703 (7th Cir. 2003).

²⁰ *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985).

ability to offer a package of skiing experiences—was, at one and the same time, the source of injury to consumers. *Id.* at 606.²¹

In *LePage's* the court found Sherman Act liability without any past consumer injury.²² It neither referred nor alluded to any overcharge paid by a direct or indirect purchaser from 3M, nor did it mention, directly or indirectly, any other way in which purchasers had been deprived of the benefits of competition or suffered any economic loss, as a result of 3M's strategy.²³

5. Future Consumer Injury. Where exclusionary conduct threatens consumer injury and has already injured a competitor, the competitor may seek damages for its past economic injury even though consumers have not yet suffered loss. The leading case is *Brunswick*, which said, “[C]ompetitors may be able to prove antitrust injury before they actually are driven from the market and competition is thereby lessened. Of course, the case for relief will be strongest where competition has been diminished.”²⁴ Thus, a competitor likely to be excluded from a market as a consequence of illegally predatory or exclusionary conduct by a monopolist suffers antitrust injury and may sue for lost profits, where its impending exclusion will likely cause consumer injury. (No one disputes that *LePage's* demise, which would have changed the market from a duopoly to a pure monopoly, would probably have caused consumer injury.)

Even where a competitor is not literally excluded from—compelled to exit—a market, consumer injury may sometimes occur if a smaller competitor is “crippled.” The “wounding” of a competitor might, for example, deprive consumers of innovative new products or increased output that would have occurred, but for the illegal “crippling” behavior. But caution is in order, because “injury” to a competitor occurs whenever a sale is taken away, yet taking sales away is the essence of competition. In *Aspen Skiing* the Supreme Court was careful to link the “crippling” of a competitor with injury to consumers. 472 U.S. at 606. That linkage seems essential in order to prevent smaller competitors from obtaining damages for aggressive competition that benefits consumers—in the short run *and* in the long run.

²¹ See generally 3 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 651d (2d ed. 2002) (urging that “[e]xclusionary conduct requires actual or prospective consumer harm”).

²² Part V of the opinion, headed “Anticompetitive Effect,” expatiated on how much 3M's program hurt *LePage's*, and on evidence of *intent* to earn future monopoly profits. There was no reference to any past injury to competition—only injury to a competitor, the plaintiff. The court did allude several times to the market exit of a third competitor, *Tesa Tuck*. See, e.g., 324 F.2d at 162. The reasons for *Tesa's* exit were not explored, but it is no huge leap to assume that 3M's strategy may have contributed to *Tesa's* market withdrawal. When a market changes from three firms to two firms, it may be easier for the remaining duopolists to coordinate pricing with one another, to the detriment of consumers. If that happened—and there is no suggestion that it did happen—it would have resulted in economic benefit to *LePage's*, not economic loss. In follow-on litigation arising out of the same facts, a class of retail purchasers does claim past damages. *Bradburn Parent/Teacher Stores, Inc. v. 3M*, No. Civ. A. 02-7676, 2004 WL 1842987 (E.D. Pa. Aug. 18, 2004). According to an Associated Press report, Publix Super Markets has filed a similar case. See http://biz.yahoo.com/ap/040917/tape_fight_2.html. The claim seems implausible, but time will tell whether these plaintiffs can prove their case.

²³ The Third Circuit majority found it significant that the lump sum rebate payments in 3M's program were unlikely to be passed on to tape consumers, because the payments did not appear on the invoice. 324 F.3d at 163. That may be right. But economic theory holds that, if the market in which the retailers operate is competitive, then the retailers will compete away these payments in ways that are potentially beneficial to consumers, such as expanding their stores. In *FTC v. H.J. Heinz Co.*, 246 F.3d 708 (D.C. Cir. 2001), the Federal Trade Commission persuaded the D.C. Circuit that competition in offering slotting allowances to retailers is competition protected by the antitrust laws, regardless of the form in which such allowances are passed on. The salient question, in any event, is not whether 3M affirmatively proved that its conduct benefited consumers. Rather, the key issue is whether the plaintiff showed that its lost profits were associated with past, or likely future, consumer injury.

²⁴ *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489 n.14 (1977).

What lessons may we learn from *LePage's* about the showing of likely future consumer injury that a plaintiff in a bundled rebate case must make in order to demonstrate antitrust injury? In answering this question, we have a choice. On the one hand, we may choose to answer based on what we think the court in *LePage's* woulda, shoulda, coulda said—fashioning our answer with a view toward the parties' claims, our intuition as to what the facts really were, and our sense of what the law ought to be. On the other hand, we may answer based on what the court actually said. The former alternative may be described as the mature choice: like the sophisticated courtiers at the emperor's court, we may praise the emperor's new fashions and overlook his nakedness.

Let us begin, however, with the immature alternative, and consider the words that the court used. Two points stand out. First, in the court's exact words: "Had 3M continued with its program it *could* have *eventually* forced *LePage's* out of the market." 324 F.3d at 162 (emphasis added). "Could" and "eventually" do not, however, cut the mustard. If sixteen improbable things happen in the right order, I "could" "eventually" fly to the moon. And any aggressive tactic by a dominant firm "could" "eventually" threaten a smaller rival.

Second, the court was exercised by strong evidence of 3M's intent that its bundling strategy would drive competitors from the market and permit it to recoup monopoly profits. The court alluded to "evidence from which the jury could have determined that 3M intended to force *LePage's* from the market, and then cease or severely curtail its own private-label and second-tier tape lines," which it juxtaposed with snippets of evidence showing "3M's interest in raising prices"—as if a profit-making enterprise's interest in earning profits were surprising or legally relevant—along with evidence that the rebates would generally not be passed along to customers,²⁵ to support its overall conclusion that "there was sufficient evidence for the jury to conclude the long-term effects of 3M's conduct were anticompetitive." 324 F.3d at 163.

It is uncontroversial that intent underlying a business strategy may assist the trier of fact in predicting the likely actual effect of that strategy. By like token, it is uncontroversial that business people often intend to injure their competitors more severely than objective circumstances will permit. For that reason and others, recent case law²⁶ and commentary²⁷ generally recognize that antitrust outcomes should not turn on "bad intent" unaccompanied by likely bad effect.

Nevertheless, based on the words the court employed, a future plaintiff challenging a monopolist's bundled rebate program may fairly cite *LePage's* for the proposition that a smaller and less diverse competitor that loses sales as the result of such a program may recover all its lost profits as single damages where there is a possibility that the plaintiff could eventually be driven from the market, at least where there is evidence of the defendant's intent to achieve such a result and thus to recoup monopoly profits. The hypothetical future plaintiff may legitimately argue that it should win even though there has been no past consumer injury and the probability of future consumer injury is low.

²⁵ Even if rebates are not passed on in the form of lower prices, economic theory dictates that, insofar as the rebate recipients operate in competitive markets, competition will result in their "passing on" the rebates indirectly, in the form of increased advertising, bigger stores, and so forth. Accordingly, while the point remains controversial, the stronger argument is that antitrust protects competition in the provision of rebates and other lump sum payments to commercial intermediaries. See *supra* note 23.

²⁶ *E.g.*, *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396 (7th Cir. 1989).

²⁷ *E.g.*, 3 AREEDA & HOVENKAMP, *supra* note 21, ¶ 601.

Did the court intend for its opinion to be read this way? Who can say? I suspect the court knew it was on shaky ground in respect of consumer injury, and intentionally employed language vague enough so that finding its holding is like nailing Jell-O® to the wall.

Now to what the court woulda, shoulda, coulda said on future consumer injury. In its brief to the Third Circuit LePage's predicted its own "imminent demise."²⁸ Its Supreme Court brief asserted that "[a]t the time of trial, LePage's was barely surviving as a going concern."²⁹ Moreover, the court was aware that LePage's was making a stronger claim than that it might eventually exit the market. The court said, "LePage's claims that it barely was surviving at the time of trial and that it suffered large operating losses from 1996 through 1999." 324 F.3d at 144–45. Thus, one would suppose, the court might properly have written something like this:

Based on the evidence, the jury might reasonably have concluded that LePage's exit from the relevant market was imminent; that 3M's bundled rebate program was a material cause of the plaintiff's likely demise; and that, in light of the high barriers to entry into the relevant market [see 324 F.3d at 162–63], consumers were likely to pay monopoly overcharges as a consequence of LePage's prospective disappearance.

Such a hypothetical finding would have taken care of the future consumer loss/antitrust injury side of the case—and we would have been left to argue only about whether we wish to call 3M's program "exclusionary" or whether we regard it as a legitimate form of competition. As to the latter point, the court might have added language along these lines:

In defense of the strategies that are about to lead to total monopoly on 3M's part, and resulting injury to consumers, 3M has offered wholly unpersuasive—barely colorable, even—purported "business justifications. [See 324 F.3d at 163–64.] Accordingly, we hold that whenever a firm with monopoly power in one or more legally relevant markets employs a bundled rebate or discount program including products over which it has monopoly power, and such a program has led, or is likely to lead, to consumer injury, the firm employing such practices has violated Section 2 of the Sherman Act.

Such a rule would have been controversial on a number of grounds, but it would have been a far cry from a rule permitting liability with no past consumer injury and only the merest possibility that consumer injury "could eventually" result.³⁰

Certiorari Denied

The Antitrust Division and the FTC successfully urged the Supreme Court to deny certiorari. The government had no more success than anyone else in divining the court's holding: it cogently observed that the "court of appeals was unclear as to what aspect of bundled rebates constituted exclusionary conduct," Brief for the United States as Amicus Curiae at 8, and that the court did not explain "what precisely rendered 3M's conduct unlawful." *Id.* at 16. The government recognized that bundled rebates can be procompetitive, *id.* at 12, and that it would be really nice if businesses had some notion about what the rules are. *Id.* at 18. But the Division and the Commission did not buy into 3M's bright line test of per se legality where prices are above cost, *id.* at 14–15,

²⁸ Brief for Appellees/Cross-Appellants, 2002 WL 32157026.

²⁹ Brief for the Respondents in Opposition at 7.

³⁰ Professor Andrew Gavil, who likes *LePage's*, has written "Although LePage's ultimately prevailed as a litigant, it was driven out of the market by 3M, and consumers will continue to suffer the uncompensated consequences of less competition." Gavil, *supra* note 2, at 40. But this report of the firm's death is exaggerated. Its current Web site, http://www.lepages.com/about_us.htm, declares that it is a leading tape producer, and promises a "New Security Tape to Combat Terrorism," thereby illustrating that it is an ill wind indeed that blows nobody good.

nor did it view bundled rebates as invariably procompetitive or benign. *Id.* at 8. And in a case where, in the government's view, both sides were wrong on the legal analysis, the Supreme Court, with little aid from counsel for the parties, was not well positioned to step in and craft its own test. *Id.* at 15–19.

A Not-So-Hypothetical Hypothetical

Some commentators have spoken eloquently of the absence of an identifiable holding by the Third Circuit, and have identified a variety of conflicting specific rules that are consistent with the court's discussion and result³¹ or that might arguably be used to decide the case.³² Others have argued over whether some or all of the bundled rebate should be "allocated" to the tape that competed directly with LePage's, for purposes of a possible predatory pricing analysis³³ (though the plaintiff and the court disclaimed reliance on such a theory). These are good and valid points, and they require no repetition here. Instead, I want to focus on the breathtakingly minimalist nature of the Third Circuit's opinion.

Consider the following hypothetical. It shares some features with the facts in *LePage's* but is different in other respects. (Whether those differences do or do not make legal distinctions is, naturally, the point of the hypothetical.)

Consolidated Gigantic (the company), a large and diversified firm with many high-tech products, asks for an evaluation of the antitrust risks (Robinson-Patman aside) of the following proposed program. The company proposes to negotiate deals with its 20 largest customers (who together account for about 50 percent of its sales and about 50 percent of the buying side of the market in the broad industry in which the company operates). The deals will be negotiated individually and will differ in their details, but will generally be as follows. For each of 15 different "strategic products," the deals will specify an "annual target" for each customer, based, roughly, on the amount purchased by that customer in the preceding year. If the customer buys 10 percent more than its target, it will receive a one percent rebate; for 20 percent growth, a 2 percent rebate; and for 30 percent growth, a 3 percent rebate. (In some cases, adjustments will be necessary. If, for example, 30 percent growth over the prior year would be more than the customer's reasonable requirements, either the "target" will be adjusted downward, or some other modification will be made in the deal.)

Rebates will be payable at the end of the one year contract period. They will be bundled, but the details of the bundling will vary. The company will try to get its large customers to agree that no rebate will be paid unless there is at least 10 percent growth in all 15 categories, but is prepared to modify the requirement through individual negotiation. For example, a deal might provide no rebate unless there is growth of at least 30 percent in one category, 20 percent in two categories, and 10 percent in seven others. It is planned, however, that each of the 20 deals will involve substantial bundling.

In each case the maximum possible rebate will be 3 percent. The company enjoys substantial profits; even if the entire discount were "allocated" to a single category, the price paid would, in almost every possible permutation, be well above variable cost, and, indeed, well above total cost.

Customers that sign these deals will not undertake a contractual commitment to buy any amount at all. In fact, the contracts will recite that no restriction is placed on the customer's ability to buy from any

³¹ *E.g.*, W. Dennis Cross, *What's Up with Section 2?* ANTITRUST, Fall 2003, at 8.

³² Gregory C. Wrobel, *New Clothes for the Emperor: Tailoring Section 2 Standards for Predatory and Exclusionary Conduct*, ANTITRUST, Fall 2003, at 28.

³³ *E.g.*, *Roundtable: Recent Developments in Section 2*, ANTITRUST, Fall 2003, at 15; *see also* Mark R. Patterson, *The Sacrifice of Profits in Non-Price Predation*, ANTITRUST, Fall 2003, at 37; Glazer & Henry, *supra* note 11.

source, without breaching the contract. If a competitor makes a better offer, the customer is entirely free to take it; the only downside is the loss of some or all of the rebate, per the terms of the arrangement. The company anticipates, however, that most customers will increase the amount they buy from the company in many of the 15 categories. In some of them, for some customers, the company may become the sole source of supply.

Of the 15 “strategic products” the company plans to include in its bundled deals, it enjoys, as to two of the categories, a market share higher than 75 percent in a clearly defined relevant product market. In three other categories it also has a greater than 75 percent share, but there is substantial doubt as to whether the market definition should be broadened. Of the remaining ten product lines, it has a high share of market (33–60 percent) in three, while it is one of many competitors in the remaining seven lines. Most or all of the 15 products are “high-tech,” and, generally speaking, barriers to entry may be said to be high in all 15 product lines, though some are perhaps more difficult to enter than others.

Some of the company’s competitors are equally large and diversified; they, for the most part, are offering similar bundled rebate programs. None, however, has exactly the same product lineup as the company, and the company thinks its bundled offer will be seen as attractive by its largest customers. Consequently, it anticipates that the bundled rebate program will result in an increase of some 5–10 percent in sales and profits. It anticipates modest, single digit increases in market share in most categories, including the categories in which it already enjoys a monopolistic share of market. In one or two of the 15 categories, its share is on the decline, but the bundling program, it is hoped, will slow the decline.

The company does not believe that any of its customers will feel “coerced” by its program or will otherwise take offense. On the contrary, a number of the large customers expect, or even demand, that programs such as this should be made available.

The company’s large competitors are mostly doing the same thing, and are unlikely to sue or complain to a government agency. Some of the company’s competitors, however, are smaller or less diversified. The intent of the program is not to “target” any particular competitor or competitors. The company believes that none will be forced to exit from any market or be “competitively crippled” in any meaningful sense, as a consequence of the bundling program.

Relevant business people at the company have not thought deeply about how their smaller competitors are likely to respond, or considered in any detail what degree of difficulty they might have in fighting back by offering economically equivalent alternatives. However, in view of the relatively small percentage size of the discounts, the company’s general understanding is that less diversified competitors can compete effectively by lowering their price, emphasizing the quality of their offerings, or taking other measures. The company thinks the plan will increase its sales and profits regardless of how any particular competitor reacts. Its success is not conditioned on the demise or crippling of any competitors. Nor does the company believe itself to be “investing” in low profits today for the sake of achieving high profits at some future time.

Finally, in response to an inquiry, the company can point to no “efficiency” accruing from its bundled rebate program. There is no saving in production or distribution, and no significant saving in the cost of negotiation, to be had from the program. Its motivation is not to achieve “efficiency” but rather to meet competitive offers, satisfy the needs and expectations of customers, and gain some competitive advantage from the diversity and strength of its product line.

A Plethora of Tests

The hypothetical is complex, but so is life. And I believe the hypothetical describes a much more common scenario than that of *LePage’s*, where the program was “targeted” on a specific competitor, whose demise (if and when it ever occurred) would lead to recoupment of monopoly profits.

Should the program outlined in the hypothetical be condemned as a violation of the Sherman Act? No, it should not, in my opinion. First, there is little, if any, prospect of consumer injury, and some possibility of consumer benefit (as Consolidated Gigantic's customers compete away their lump sum rebates in ways that may indirectly benefit consumers). Indeed, the Antitrust Division's amicus brief in *LePage's* recognized that some bundled discount programs may be procompetitive, and this could well be such a case: there is a good chance that the program is undertaken as a way of competing on price in concentrated markets and is intended to avoid the kind of competitive retaliation that might ensue from simply dropping prices across the board. Second, judicial intervention in such complex and competitively ambiguous circumstances would lead, I am persuaded, not only to indefensible outcomes but to random and completely unpredictable outcomes.

But would Consolidated Gigantic be vulnerable to attack under *LePage's* by a smaller and less diversified competitor that lost a dollar of profit as a consequence of the program? Arguably, it would. Monopoly power and (modest) enhancement of monopoly power are built into the hypothetical. Establishing those elements is a big head start in winning a monopolization case. Consumer injury, present or prospective, is also an essential element, in the view of most cases and commentators—but not, based on the discussion above, in the mind of the Third Circuit.

And what is left? Unlike the facts in *LePage's*, my hypothetical involves no hot documents showing bad intent. But does that really help the defendant? Surely, the plaintiff would argue that absence of hot documents proves only that the defendant was well counseled and clever about what it chose not to write down—and should derive no benefit from its cleverness.

What of “business justification”? Assuming the Third Circuit buys the explanation that the bundled rebate program was, in large measure, an attempt to “cheat” on Consolidated's fellow oligopolists, would that be regarded as a legally sufficient excuse for “exclusionary” conduct? I would not bet the mortgage money on it.

Putting aside “monopoly” and “enhancement of monopoly share” (built into the hypothetical), consumer injury (irrelevant), intent (only counts against the defendant, never for the defendant), and business justification (not accepted as valid), what does that leave? One thing and one thing only: whether to label the business strategy “exclusionary” within the meaning of the Section 2 jurisprudence. For the reasons set forth at some length above, I would not describe the hypothetical program as involving either “exclusive dealing” or “foreclosure.” But the Third Circuit evidently would disagree.³⁴

Fortunately, there is hope because the Third Circuit's position, as I understand it, is an outlier. Space and time do not permit an exhaustive review of the case law and commentary that might have some bearing on the bundled rebate issue, but consider these four alternative approaches.

1. The Ortho Test. This 1996 Southern District of New York opinion set forth a specific test that seems to apply to the hypothetical: Consolidated Gigantic enjoys monopoly power in some markets; it offers products in which it has monopoly power and products in which it does not have monopoly power, both as a package and individually—there is no “tying” in the hypothetical—and it “effectively forces its competitors [with less diverse product lines] to absorb the differential between the bundled and unbundled prices of the product in which [it] has market power.” 920

³⁴ Those who like the *LePage's* approach would have a fallback argument as well: even if the Third Circuit was loose in its “exclusive dealing” and “foreclosure” language, that should not matter, because bundling is inherently unfair to less diverse competitors no matter what name we give it.

F. Supp. at 469. In such a case, under *Ortho* there is liability if “(a) the monopolist has priced below its average variable cost or (b) the plaintiff is at least as efficient a producer of the competitive product as the defendant, but that the defendant’s pricing makes it unprofitable for the plaintiff to continue to produce.” *Id.* In the hypothetical the first test is not met, because price exceeds average variable cost. In the hypothetical, as is typically the case in real life, it is not known whether a specific potential plaintiff “is at least as efficient a producer as the competitor.” But that doesn’t matter, because, as far as one knows, there is no potential plaintiff that will find it unprofitable to continue to produce any of the products in the package.

In the hypothetical the defendant is a monopolist, it has adopted a form of strategic pricing that produces no efficiency, and is intended to, and likely will, gain market share from less diversified competitors, increasing its share of market in properly defined relevant markets in which it enjoys monopoly power—and perhaps in others where the likelihood of increased market share support a dangerous probability of achieving monopoly power. Yet, under *Ortho*, the defendant escapes liability.

2. The SmithKline Test. Although its holding was somewhat more loosely phrased than that of the *Ortho* court, the Third Circuit in *SmithKline* summarized its finding of liability by pointing to the following key factors:

- a defendant with monopoly power in some products and no monopoly power in others,
- linkage of the two categories of products through package pricing so that its competitor in the non-monopoly products is forced to pay rebates equal to the rebates the monopolist gives on its entire package,
- with the result that the less diverse competitor has “poor prospects” for continuing to compete in the non-monopolized product market,
- in a situation with high barriers to entry.

575 F.2d at 1065. Each of these factors is met in the hypothetical except the third—“poor prospects” for continuing in the business—but as Judge Greenberg read *SmithKline*, and as I read it also, failure by the plaintiff to show likely future exit should be enough to defeat recovery. Otherwise, there is no consumer injury, and a competitor should not be able to recover for conduct that lowers prices in the absence of present or prospective consumer injury.

3. The Concord Boat Test. *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039 (8th Cir. 2000), addressed the legality of a structured rebate program where the amount of the rebate was based on “market share,” i.e., percent of a customer’s requirements. The court rejected an argument, similar to 3M’s, that under *Brooke Group* pricing above cost may never be illegal under the Sherman Act. But on the other hand, it said, “If a firm has discounted prices to a level that remains above the firm’s average variable cost, ‘the plaintiff must overcome a strong presumption of legality by showing other factors indicating that the price charged is anticompetitive.’” *Id.* at 1061 (citation omitted). In the hypothetical, it is hard to see how a potential plaintiff might overcome such a “strong presumption of legality.”³⁵

³⁵ The case is not directly on point, inasmuch as the court distinguished (without explaining the rationale for the distinction) cases like *LePage’s*, involving multi-product rebates rather than rebates based on a single product line. It is, however, at least a second cousin to the facts in *LePage’s* and the scenario involved in our hypothetical.

4. The Hovenkamp Test. Addressing *LePage's* in the 2004 *Supplement*, Hovenkamp asserts that the majority's treatment seems consistent with our definition of exclusionary conduct as acts that:

- (1) are reasonably capable of creating, enlarging, or prolonging monopoly power by impairing the opportunities of rivals, and
- (2) that either (2a) do not benefit consumers at all, or (2b) are unnecessary for the particular consumer benefits that the acts produce, or (2c) produce harms disproportionate to the resulting benefits.

¶ 749 at 183. In the hypothetical it is assumed that the rebate program will enlarge or prolong monopoly power, by at least some non-trivial amount. Whether that result is accomplished “by impairing the opportunities of rivals” is a matter of semantics, but, from the context of his discussion, presumably Hovenkamp would think the facts in the hypothetical meet his first test. The application of each of the three alternatives set forth in the second part of the test is likewise open to question. A potential plaintiff would perhaps have the easiest shot at proving the second of the three alternatives: that the rebate program is “unnecessary” to produce “the particular consumer benefit.” Read literally, however, such a test would outlaw any and all bundled pricing by monopolists, because the monopolist could always, at least in theory, have simply lowered the price without bundling. But this cannot be what Hovenkamp intends because he goes on to urge caution in extending *LePage's*, observing, “Indeed, . . . we would be reluctant to extend the doctrine to any situation in which there was at least one competing firm able to match the defendant's discount across all product lines.” *Id.* at 184. Here, the hypothetical assumes that others could match the general scope of the discount program, though no one could duplicate the exact items that Consolidated Gigantic proposes to include in its program. In sum, then, it is doubtful that the company in the hypothetical would be found liable under the Hovenkamp analysis.

Conclusion

Bundled discount and rebate programs are common—increasingly common, I believe. As the Antitrust Division recognized in its brief to the Supreme Court, many are procompetitive. In other cases, the intent and likely effects of the programs seem benign or, at worst, highly ambiguous. Although the outcome in *LePage's* may have been right, the court's analysis was objectionable in several important ways but chiefly in its failure to keep its eye on consumer injury. If future courts avoid that one signal error, most cases will, I believe, be rightly decided.

In his recent article on exclusionary distribution strategies Professor Gavil said that “[t]he real challenge—and the focal point over disagreements about standards under Section 2—are the closer cases, which involve conduct that yields both significant inefficiencies *and* significant efficiencies.”³⁶ Situations of that nature may indeed present challenges to the antitrust court, but I see few of them. Much more often I see scenarios like that in the hypothetical, where there are *insignificant* efficiencies and *insignificant* likelihood of harm, yet there is arguable monopoly power, enhancement of market power, and a business strategy that could, with good lawyering, be made to appear “exclusionary.” To deal with situations of that nature, keep your eye on the consumer injury. ●

³⁶ Gavil, *supra* note 2, at 77.