LePage's II: The En Banc Third Circuit Revisits 3M's Bundled Discounts and Sees Unlawful "Exclusion" Instead of Above-Cost Pricing

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In *LePage's v. 3M*, 324 F.3d 141 (3d Cir. 2002), the en banc Third Circuit joined a chorus of recent courts of appeals that have sided with plaintiffs in upholding the potential validity of their Section 2 claims.[1] If not reviewed by the Supreme Court—or affected by the outcome of the Court's pending review of the *Trinko* case—*LePage's* may well have the most far-reaching consequences of these recent decisions. It addresses a question of central importance to any firm that possesses a high share of some market: what conduct might be found unlawful under Section 2 of the Sherman Act as the "willful maintenance of monopoly power" or, in the vernacular of most recent cases, be deemed "predatory and exclusionary"?

LePage's answers this question in a way that could be read as sweeping within the ambit of Section 2 virtually any practice that causes harm to competitors. Harking back to the first half of the last century—when bigness bordered on badness[2]—(the decision appears to demand that a jury decide virtually every claim by a plaintiff harmed by the marketplace behavior of a firm with "monopoly" power, and offers those juries precious little guidance for distinguishing between legal competition and unlawful monopoly maintenance.

The type of behavior at issue in *LePage's* magnifies the significance of the case. With inconsequential exceptions, the case was solely about 3M's *pricing* of its products in competition with LePage's.[3] LePage's labored mightily to characterize the case as involving the "exclusionary *structure* of 3M's pricing"—which in part involved "bundled" rebates across multiple product lines—rather than "3M's price levels,"[4] and the court readily agreed that the case did not involve a "predatory pricing claim." 324 F.3d at 151. But there are reasons to question this characterization. For example, LePage's did not attempt to prove that the structure of 3M's pricing made it any harder for LePage's to compete than if 3M had offered equivalent rewards to customers by merely reducing the *level* of its price on the private-label tape with which LePage's competed.

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[1] *E.g.*, MetroNet Servs. Corp. v. US West Communications, 2003 U.S. App. LEXIS 6007 (9th Cir. 2003) (reversing grant of summary judgment against § 2 claim); Law Offices of Curtis V. Trinko, L.L.P. v. Bell Atl. Corp., 305 F.3d 89 (2d Cir. 2002) (reversing district court dismissal of Section 2 claim), *cert. granted*, 123 S. Ct. 1480 (2003); Telecor Communications, Inc. v. Southwestern Bell Tel. Co., 305 F. 3d 1124 (10th Cir. 2002) (affirming § 2 jury verdict); Conwood Co., L.P. v. U.S. Tobacco Co., 290 F.3d 768 (6th Cir. 2002) (affirming § 2 jury verdict), *cert. denied*, 123 S. Ct. 876 (2003);

[2] The court of appeals treats *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) (*Alcoa*), as the beginning of the "modern era" of § 2 jurisprudence, and quotes approvingly from *United States v. Swift*, 286 U.S. 106 (1932).

[3] A significant portion of the court's discussion deals with 3M's alleged "exclusive dealing," but virtually all of the conduct involved the exclusionary effect of the same bundled discounts.

[4] Brief for Appellees/Cross-Appellants at 63 (Mar. 30, 2001) (*LePage's* Brief).

The *LePage's* decision does not doom all firms with monopoly-sized market shares. They can draw some comfort from the fact that the case was decided after a jury had already concluded that 3M had unlawfully maintained its monopoly, and the court of appeals was quite reluctant to override the jury's prerogative to reach that conclusion on an extensive record covering the competitive interactions between 3M and LePage's over the course of several years.[5] They can also hope that the rhetoric of the decision will be applied narrowly, with greatest emphasis given to the court's rejection of the (overbroad) proposition that *Brooke Group* bars all monopolization claims whenever the defendant's prices are above costs.

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Moreover, there are a few concrete steps that potential defendants can take to avoid 3M's fate. They can explicitly limit their marketing programs to above-cost, unstructured discounts offered on single products, and thereby stay within the refuge of predatory pricing law. If they choose to "bundle"—or otherwise get creative in their pricing programs—they can avoid creating a record that their conduct is aimed at annihilating their smaller rivals, so as to avoid the unhappy inference that juries might draw from statements like the one in a 3M document that suggest its actions were intended to "kill" LePage's and its private-label niche. And they can be prepared to defend their pricing structure (or other potentially "injurious" competitive initiatives) by having concrete proof of the procompetitive justifications (a.k.a. "valid business reasons") for decisions to compete in ways that make life relatively more difficult for their rivals.

The Factual and Procedural Context

The factual and procedural context of the case is fairly straightforward. 3M manufactures the "Scotch" brand of tape products, which by the 1990s had come to account for over 90 percent of all sales of transparent tape in the United States. LePage's also makes transparent tape, which it sells to large retailers—like Wal-Mart, Kmart, Staples, Dollar General, CVS, and others—for resale under the retailers' "private labels" instead of the LePage's name. LePage's' private-label business was quite successful. By 1992, LePage's accounted for 88 percent of private-label tape sales in the United States, and those sales were eating into 3M's sales of Scotch-brand tape.

3M reacted in two principal ways. In 1992, 3M began selling its own version of private-label tape, bringing it into head-to-head competition with LePage's for the same large retail accounts.[6] And in 1993, 3M launched a series of marketing programs aimed at encouraging those retailers to acquire more transparent tape—both branded and private-label—from 3M. 3M offered at least three kinds of programs: (1) volume discounts on its private-label tape; (2) rebates (called "brand mix" rebates) based on the customer's total volume of 3M tape purchases, thus encouraging customers to buy both their "Scotch" brand tape needs and their private-label tape from 3M; and (3) other rebates (part of the "executive growth" and "partnership growth" programs) that were calculated based on the customer's purchases from a range of 3M product lines, not just tape. Some of these programs were custom-tailored to specific customers, so that the level of tape purchases needed to earn maximum rebates was close to 100 percent of the customer's total purchases. And there was at least some evidence that 3M told certain customers that they could only earn

[5] *See* 324 F.3d at 146 ("our review of a jury's verdict is limited to determining whether some evidence supports the jury's verdict"); *see also, e.g., id.* at 154, 163.

[6] The court or appeals referred to "considerable evidence in the record that 3M entered the private-label market only to 'kill it.'" *Id.* at 164.

payments by shifting their business from LePage's to 3M.[7] In addition to discount programs, 3M negotiated contracts with two smaller retailers that expressly required them to buy all of their private-label tape from 3M for a period of one year. 324 F.3d at 157.

LePage's apparently did not challenge the first type of discounts,[8] and on that basis it contended that the case did not involve a "predatory pricing" claim. Instead, LePage's argued that 3M's "bundled" rebate programs amounted to a form of exclusive dealing arrangement that foreclosed LePage's from competing on the merits because it did not make branded tape or the other kinds of products included in 3M's programs. According to LePage's, the discounts were payments "conditioned" on exclusivity.[9] All retailers needed to stock 3M's Scotch-brand tape, and so were already paying 3M a substantial amount of money for tape. 3M's bundled rebates acted as a credit against those purchases that customers could earn only if they shifted all or substantially all of their private-label purchases to 3M and away from LePage's.[10]

3M and the dissent pointed out that 3M's rebates involved rather small percentages of 3M's prices on individual products, ranging from 0.2 to 2.0 percent.[11] On the other hand, as LePage's and the majority emphasized, those rebates involved payments of millions of dollars, because 3M's customers bought a lot of 3M products.[12] Eager to earn the maximum amount of 3M rebates, many customers did opt to shift sales away from LePage's. LePage's contended that it could not have matched the economic value of 3M's rebates without offering steep, and likely unprofitable, discounts on its smaller base of private-label tape sales. *Id.* at 161. However, LePage's did not attempt to prove that 3M's rebates were below cost by any measure, even if the entire amount of the dollar savings were allocated to 3M's private-label tape sales. *Id.* at 147 n.5. Nor did LePage's try to demonstrate that 3M's rebates made it impossible for LePage's—or a hypothetical firm that was as efficient as 3M[13]—profitably to lower its tape prices far enough to offer a deal that allowed retailers to save as much or more money than under 3M's programs. *Id.* at 177 (dissent).

3M's strategies were partially successful. By 1997, LePage's share of private-label tape sales had declined from 88 to 67 percent, and its profitability had plunged. *Id.* at 170, 175–76 (dissent); *see also id.* at 161. At that point, LePage's played its antitrust card, challenging 3M's course of conduct under both Section 1 and Section 2 of the Sherman Act, and Section 3 of the Clayton Act. After more than two years of litigation, a jury found in favor of LePage's on its Section 2 monopolization claim.[14] The district court declined to overturn the verdict, and 3M appealed. On appeal, neither market definition nor 3M's status as a monopolist was at issue. 3M did not contest the jury's conclusion that the relevant market consisted of all transparent tape sales—both branded and private-label—in the United States, and that 3M possessed monopoly power in that market.[15] The only significant issue was whether 3M had willfully maintained that power.

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[7] Id. at 154, 158–59; LePage's Brief at 8–12.

[8] *See* LePage's Brief, at 63–64.

[9] *Id.* at 8.

[10] *Id.* at 40–41; *see also, e.g., id.* at 14–15.

[11] 324 F.3d at 170–71 (dissent); *see also* Brief of Appellant Cross-Appellee at 14–15 (Mar. 29, 2001) (3M Brief).

[12] 324 F.3d at 154; LePage's Brief at 45–47.

[13] LePage's apparently conceded that it was less efficient than 3M. 324 F.3d at 177 (dissent).

[14] The jury rejected LePage's Sherman § 1 and Clayton § 3 exclusive dealing claims. The jury found for LePage's on its "attempted maintenance of monopoly power" claim, which the district court and the court of appeals found insufficient as a matter of law to state a § 2 claim. 324 F.3d at 145.

[15] 3M Brief at 9.

The En Banc Court's Decision

At the court of appeals, the case was a war between two diametrically opposed views of how Section 2 of the Sherman Act should be applied in the context of a claim involving price discounts. Initially, a divided Panel of the Third Circuit sided with 3M's view and reversed the district court's judgment.[16] It viewed the case as involving a form of predatory pricing claim, which failed as a matter of law because LePage's made no effort to prove that 3M's prices were below cost—or at least that LePage's was an equally efficient competitor and could not profitably match 3M's discounts. 277 F.3d at 376, 380–81. The Panel dealt with the Third Circuit's 24-year old decision in *SmithKline Corp. v. Eli Lilly & Co.*, 575 F.2d 1056, 1065 (3d Cir. 1978), which had affirmed a finding of Section 2 liability based on a similar bundled discount program, by distinguishing the case. Unlike in *SmithKline*, LePage's had not proven that it could not compete in the face of 3M's rebate programs. 277 F.2d at 378.

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A vehement dissent by Judge Sloviter was followed by an order vacating the Panel decision and setting the case for rehearing en banc. The en banc court reversed field 180 degrees. In an opinion written by Judge Sloviter,[17] the court reached the following conclusions:

- **Brooke Group.** The court swiftly rejected 3M's efforts to have the case treated under the standard applicable to predatory pricing cases. It suggested that *Brooke Group*[18] should not be read as applying to pricing by a monopolist, and may not even stand for the proposition that "a company's pricing action is legal if its prices are not below costs." 324 F.3d at 151. But even if *Brooke Group* did establish a safe harbor for a monopolist's above-cost pricing, the case did not help 3M because LePage's did "not make a predatory pricing claim." *Id.*
- ***The Cavalcade of Supreme Court Precedent.*** To help it chart a course that bypassed the shoals of predatory pricing law, the court recited in detail the evolution of the Supreme Court's Section 2 jurisprudence in the "modern era." In six pages of detailed discussion, the court of appeals marched through the last half-century of cases—from *Alcoa* to *Kodak*[19]—to reach two basic conclusions. First, the court squarely rejected 3M's "legal theory that after *Brooke Group*, no conduct by a monopolist who sells its product above cost—no matter how exclusionary the conduct—can constitute monopolization." 324 F.3d at 147, 152.[20] Second, the court of appeals derived from *Alcoa* and the other Supreme Court precedents the principle that a monopolist willfully maintains its power in violation of Section 2 whenever it deliberately takes any action that "'discourages its customers from doing business with its smaller rival,'"[21] unless the defendant "could explain its actions on the basis of valid business reasons."[22]

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[16] The Panel decision was reported at 277 F.3d 365 (3d Cir. 2002).

[17] Three judges dissented, including both members of the Panel majority.

[18] Brooke Group Ltd v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993).

[19] Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451 (1992).

[20] This characterization was a straw man because 3M's position that it could not be held liable absent a showing that its prices were below cost was limited to the context where "LePage's case was all based upon claims about discount prices and rebates." *3M* Brief at 36, 51. 3M did not seek to establish the broader principle of § 2 jurisprudence that the court rejected.

[21] 324 F.3d at 150 (quoting Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 610 (1985) (citing in turn Lorain Journal Co. v. United States, 342 U.S. 143, 149 (1951)).

[22] 324 F.3d at 151 (citing *Kodak*, 472 U.S. at 483); *see also* 324 F.3d at 152 (referring to the Supreme Court's consistent holdings that a monopolist will violate § 2 if it "engages in exclusionary or predatory conduct without a valid business justification").

- ***Bundled Rebates as Exclusionary Conduct.*** The court of appeals readily found that there was sufficient evidence supporting the jury's determination that 3M's bundled rebates were "exclusionary" and "could reasonably have been viewed as effectuating exclusive dealing arrangements because of the way in which they were structured." *Id.* at 154. The court first characterized 3M's rebates as having provided "powerful incentive[s] . . . to customers to purchase 3M tape rather than LePage's in order not to forgo the maximum rebate 3M offered." On this view of the world, 3M's price reductions amounted to six or seven figure "penalties" for choosing LePage's. *Id.*

Next, the court cited a leading treatise for the proposition that bundled rebates have an "inherent anticompetitive effect," even when they yield "aggregate prices above cost."[23] This characterization was puzzling in light of the treatise's statement—quoted by the court just one paragraph later—that the authors presume that the "anticompetitive case ... is in the minority."[24] In any event, the court of appeals explained that it regarded bundled rebates as anticompetitive because they "may foreclose portions of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer." *Id.* at 155.

Finally, the court turned to *SmithKline* as support for its conclusion that bundled rebates are anticompetitive. The *SmithKline* case addressed the market for cephalosporins, in which Lilly was dominant and SmithKline was an upstart competitor. SmithKline challenged Lilly's multi-line volume rebates, which had led hospitals to "conjoin their purchases" of one of Lilly's cephalosporins (Kefzol) with two others (Keflin and Keflex) that were Lilly's "leading sellers." *Id.* at 156 (quoting *SmithKline*, 575 F.2d at 1061). Kefzol was the private-label tape of its era: "less expensive but otherwise of similar quality" to Lilly's Keflin and Keflex. SmithKline offered its own "cheaper" cephalosporin, Ancef, but Lilly's bundled rebates made it difficult for SmithKline to compete. It would have had to offer discounts on Ancef ranging from 16 to 35 percent in order to provide the same "net dollar amount" as Lilly could provide with a "3% bundled rebate" on its larger volume of cephalosporin sales. 324 F.3d at 156 (quoting *SmithKline*, 575 F.2d at 1062). This bundling was unlawful monopolization because the jury could have found that "the result was [for Lilly] to sell all three products on a non-competitive basis in what would have otherwise been a competitive market for Ancef and Kefzol," and that "SmithKline's prospects for continuing in the cephalosporin market under these conditions [were] poor." *SmithKline*, 575 F.2d at 1065.

- ***"Exclusive Dealing."*** The court of appeals also concluded that 3M's bundled rebates were exclusionary "exclusive dealing practices." 324 F.3d at 159. Even though 3M's payments to retailers were not expressly exclusive, the jury could have found that they were "designed to induce [customers] to award business to 3M to the exclusion of LePage's." *Id.* at 158. The court relied on *Tampa Electric*[25] for the proposition that an arrangement need not contain any "express exclusivity requirement" in order to be treated as exclusive dealing (324 F.3d at 157), and it relied on the D.C. Circuit's *Microsoft* decision[26] for the proposition that exclusive dealing can support a Section 2 violation even if it forecloses substantially less than 100 percent of the market (324 F.3d at 158–59). The court of appeals had no difficulty concluding that the jury could have found that at least some of 3M's customers regarded its bundled dis-

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[23] 324 F.3d at 155 (citing Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law ¶ 749, at 83 (Supp. 2002).

[24] Areeda & Hovenkamp, *supra* note 23.

[25] Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 320, 327 (1961).

[26] United States v. Microsoft Corp., 253 F.3d 34, 69–71 (D.C. Cir.) (en banc), *cert. denied*, 534 U.S. 952 (2001).

counts as amounting to "all-or-nothing" offers that required the customer to give 3M all of its tape business in order to earn the maximum level of rebate. *Id.* at 159.

- ***Anticompetitive Effects.*** The next step in the court of appeals' analysis was its conclusion that there was sufficient evidence for the jury to find that the "long-term effects of 3M's conduct were anticompetitive." *Id.* at 163. It is unclear why the court paused to consider this issue, since it had already said more than once that the jury could have found that 3M's conduct violated Section 2. *Id.* at 159. In any event, the outcome of this step in the court's analysis was not in doubt given the court's earlier conclusion that 3M's actions were exclusionary. The court set a very low threshold for finding anticompetitive effects: whenever a monopolist acts to prevent one or more new or potential competitors from gaining a foothold in the market by exclusionary conduct, "its success in that goal is not only injurious to the potential competitor but also to competition in general." *Id.* To the court of appeals, 3M's success spoke for itself. 3M's rebates hurt LePage's. As the court of appeals explained, the "discount LePage's would have had to provide to match the discounts offered by 3M through its bundled rebates can be measured by the discounts 3M gave or offered." Those discounts were indeed large in dollar terms. Had LePage's matched them, it would have suffered a reduction in earnings "calculated by comparing the discount that LePage's would have been required to provide." *Id.* at 161. "That amount," the court held, "would represent the impact of 3M's bundled rebates on LePage's ability to compete, *and that is what is relevant under § 2 of the Sherman Act*." *Id.* (emphasis added).[27]

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This comment appears to suggest that harm to LePage's was enough to make 3M's conduct "anticompetitive," but the court of appeals also observed that 3M's conduct "harmed competition itself, a *sine qua non* for a § 2 violation." *Id.* at 162. In part this was the obvious consequence of LePage's being 3M's only domestic competitor. The court also cited evidence from 3M's files indicating that 3M desired to do away with the private-label segment altogether so that it could charge higher prices for its premium Scotch-brand tape. *Id.* at 163. That evidence was relevant because "intent is relevant to proving monopolization." *Id.* And the court noted that there was substantial evidence that barriers to entry existed in the transparent tape market. *Id.*

- ***Business Justifications.*** Having found 3M's conduct exclusionary, and, for good measure, anticompetitively so, the court turned to consider whether 3M's actions were "carried out for 'valid business reasons,' the only recognized justification for monopolizing." *Id.* (quoting *Kodak*, 504 U.S. at 483). The court's analysis proceeded in three steps. First, the court rejected the contention that 3M's conduct was justified simply because 3M was acting "in furtherance of its economic interests." *Id.* The court observed that "it can be assumed that a monopolist seeks to further its economic interests and does so when it engages in exclusionary conduct," and stated that this motivation alone is *never* a "valid business reason." *Id.* at 164.

Second, the court considered whether 3M had borne its burden of persuading the jury that its conduct was justified by "actual economic efficiencies" (*id.*) or the "'enhancement of consumer welfare.'" *Id.* at 163 (quoting *Data General Corp. v. Grumman Systems Support Corp.*, 36 F.3d 1147, 1183 (1st Cir. 1994)). The "millions of dollars 3M returned to customers in bundled rebates"

[27] This impact, the court noted, was also "apparent" from the declines in earnings and sales that LePage's realized while 3M's rebate programs were in effect. 324 F.3d at 161.

(*id.* at 164) did not suffice. Instead, 3M apparently was required to show that the bundling of its products achieved real cost savings through, for example, the use of single invoices or single shipments. 3M had not attempted such a showing. *Id.*

Finally, the court noted that there was evidence indicating that the proffered justifications were not the real motivation for 3M's conduct. The jury was entitled to conclude, for example, that 3M had "entered the private-label market only to 'kill it.'" *Id.* (quoting internal 3M document). That, the court held, is "precisely what § 2 prohibits." *Id.*[28]

The Dissent

The dissenting opinion, authored by the same judge (Greenburg, J.) who wrote the vacated opinion for the Panel majority, and joined by two other members of the court, made five principal points:

- The trial record suggested that there were many causes for LePage's' loss of share in the private-label segment other than 3M's discounting practices. *Id.* at 171–73.
- The majority misapplied *SmithKline*, because LePage's did not demonstrate (or even try to prove) that it could not profitably "match the rebates 3M paid to particular customers." *Id.* at 175.
- LePage's should not be allowed to prevail without showing that 3M's pricing was below cost (*Id.* at 173), or at least satisfying the "stricter tests devised by other courts considering bundled rebates" by proving that a single-product competitor that was as efficient as 3M could not profitably match 3M's linked multi-product rebates. *Id.* at 177.
- 3M's conduct was justified by a valid business reason because, unlike in *Aspen Skiing* and other cases, 3M was not acting against its short-run economic interests. *Id.* at 178–79. Instead, it was behaving in a way that "likely increased its sales." *Id.* at 179.
- LePage's' claim that 3M entered into two expressly exclusive contracts was "attenuated" in light of LePage's' ability to retain a "two-thirds share of the private label business," and the two contracts could not have been responsible for the "total drop" in LePage's' business. *Id.* at 180.

The Aftermath

The Third Circuit's Panel decision in *LePage's*, which had overturned the jury verdict against 3M, left the precise standard applicable to Section 2 claims against bundled rebates substantially in doubt. The en banc court's decision to vacate that decision and rehear the case created even more uncertainty and raised a number of interesting questions about how the full court would decide the case.[29] The en banc decision in *LePage's* now provides resounding answers to some of those questions.

In the arena of bundled discounts and other complicated pricing arrangements, there is no doubt that *LePage's* will have significant consequences for the behavior of firms with large market shares. But *LePage's* may cast a longer shadow that influences how litigants and courts approach the difficult task of distinguishing legitimate competition by a monopolist from unlawful

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[28] The majority opinion also addressed and rejected 3M's claims that the court improperly calculated damages and used jury instructions that provided inadequate guidance. 324 F.3d at 164–69.

[29] Many of those questions were considered last May in this publication. *See* David L. Meyer & Raymond A. Atkins, LePage's v. 3M*: Will the Third Circuit Make* Brooke Group *Stick in Assessing the Legality of a Monopolist's Bundled Discount Programs?*," ANTITRUST SOURCE (May 2002), *available at* http://www.abanet.org/antitrust/source/may02/legality.pdf.

"exclusion" in many diverse settings. If that is the case, the decision will be a boon for competitors eager to rein in aggressive competition by their larger rivals.

What Did the Court Decide? *LePage's* weighs in heavily on three key questions that are central, not only to the treatment of bundled discounts and other complex price structures, but to the law of monopolization generally.

1. Price Level vs. Price Structure: When Do Low but Non-Predatory Prices Become "Exclusionary" Prices? The clearest and most significant holding of *LePage's* is that claims against a monopolist's bundled rebates programs should not be analyzed as predatory pricing claims. This means that, under LePage's, plaintiffs need not attempt to prove that the defendant's prices were below costs. The Panel decision's somewhat tentative reliance on *Brooke Group* thus turns out to have been more like a "Post-It" (a.k.a. a "repositionable note")[30] than adhesive tape. The en banc court removed it.

The clearest and most significant holding of **LePage's** *is that claims against a monopolist's bundled rebates programs should not be analyzed as predatory pricing claims.*

This aspect of the court's decision raises two crucial questions. *First*, what kinds of "pricing" will fall outside the ambit of predatory pricing law. The court purports to distinguish between single-product "volume discounts"—which it regarded as "concededly legal" (324 F.3d at 154)—and 3M's rebate programs, which involved more than one product and in many instances multiple product lines. The latter—no matter how far above 3M's costs—are not eligible for analysis under the rubric of "predatory pricing" law for the simple reason that LePage's did not make all of the products that 3M's programs linked.

Less clear is what pricing actions other than simple volume discounts will run afoul of *LePage's*. The apparent rationale of the court's decision—that the plaintiff, no matter how efficient, cannot "match" the defendant's discounts—would seem to cast a fairly wide net capable of snaring many unwary discounters. Programs that link products across multiple markets in which a plaintiff does not compete are certainly at risk if the defendant has monopoly power. But any linkage across products within a single product line appears equally vulnerable under *LePage's*. Many of 3M's offending rebates did not involve products outside the market in which 3M had a monopoly. Instead, they linked 3M's various transparent tape products (Scotch brand and private-label), all of which LePage's alleged and 3M conceded were in the same market as the tape LePage's produced. Because LePage's chose to compete only in one segment of that market—private-label—3M's decision to link its private label prices with purchases of other 3M tape caused those prices to be viewed as potentially "exclusionary" rather than "predatory" under the rubric of *Brooke Group*.[31]

LePage's' lawyers argued that the distinction between 3M's conduct and the kind of pricing amenable to treatment under predatory pricing principles was that 3M's conduct concerned "price structure" rather than merely "price levels."[32] The Third Circuit did not quite endorse that view, but it did not explicitly reject it either. Indeed, a key theme of the court of appeals' decision is that LePage's' ability to match the *value* of 3M's rebate programs was irrelevant; what mattered was LePage's' inability to provide the same kind of program because it lacked 3M's multi-product scope.

On this theory, creative lawyers may well argue that the rationale of *LePage's* should apply to any pricing that is more complicated than a mere reduction in price level and which the plaintiff cannot match tit-for-tat. A wide array of pricing programs may be vulnerable under this approach.

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[30] 3M Brief at 7.

[31] In this regard, *LePage's* is not different from *SmithKline*. *SmithKline* similarly addressed pricing programs that were limited to multiple products within a single market—albeit decades before *Brooke Group*.

[32] LePage's Brief at 63.

"Monopolists" will often have a base of sales that includes many brand-loyal customers, making it impossible for the upstart competitor to "match" the defendant's volume or market share targets. Nor would it be a stretch to argue that, under *LePage's*, single-product volume or market share discounts fall outside the predatory pricing rubric when they are structured so as to "condition" a customer's maximum discount levels on the customer buying so much of the defendant's product that the customer has no interest in the plaintiff's competing product. No less than 3M's rebates, which LePage's argued were conditioned in this way, such programs could be deemed "exclusive dealing" under the rationale of *LePage's*. *See id.* at 159.[33]

This uncertainty about the sweep of *LePage's*' rationale begs a second, more serious question, to which the court does not provide a satisfactory answer. Why should structured discounts be treated differently than unstructured discounts? So far as the record discloses, 3M's rebates were no more harmful to LePage's than an equal number of dollars off of 3M's private-label prices. Stated another way, although LePage's offered evidence that customers were induced to shift their purchases to 3M to take advantage of 3M's rebates, there was no evidence that the structure of 3M's prices, as distinct from their level, mattered to the decisions of these customers.

To be sure, the court emphasized that the multi-product character of 3M's programs allowed it to provide customers with big dollar savings without reducing its prices very much. LePage's would not have been able to provide the same number of dollars without quite significant price reductions, and the court may have inferred that it was truly impossible for any single-product firm—no matter how efficient—to compete on the merits in this environment. But the court of appeals did not require LePage's to offer evidence proving that proposition. And because it did not insist on such proof, the decision could be read as insulating LePage's and similarly-situated competitors from the occasional need to make big price reductions.

One reason the court may have been reluctant to apply predatory pricing principles was its apparent perception that the relationship between 3M's prices and 3M's costs could only be performed on an "aggregate" basis for the entire "bundle" of linked products. *See id.* at 155. If that were so, applying predatory pricing standards probably would give a multi-product monopolist unduly wide latitude to price "above cost" and at the same time undermine effective competition by an efficient single-product rival.[34] But such an approach was not the only way that LePage's might have shown that 3M's prices were predatory. As cautiously suggested in 3M's brief, LePage's might have attempted to demonstrate that 3M's rebates, if allocated to the one 3M product with which LePage's competed, would render 3M's effective price for that product below its costs for that product.[35] Alternatively, LePage's might have attempted to make the showing—suggested in *Ortho*[36]—that a (hypothetical) company that was as efficient as 3M, but which only sold private-

[33] *See also* 324 F.3d at 154 (jury could have viewed the rebates as "effectuating exclusive dealing arrangements because of the way in which they were structured").

[34] This "aggregate" approach for assessing the price-cost relationship in a multi-product setting has led other commentators to conclude that exclusionary rebates should not be analyzed as predatory pricing. Areeda & Hovenkamp, *supra* note 23.

[35] 3M Brief at 43; *see also* Willard K. Tom, David A. Balto & Neil W. Averitt, *Anticompetitive Aspects of Market-Share Discounts and Other Incentives to Exclusive Dealing*, 67 Antitrust L.J. 615, 628–29 (2000) (noting that volume-based incentive discounts can be incentives to exclusivity and can also be viewed "as predatory under the usual cost-based tests" if the discount, when ascribed to the incremental units that generate the discount, results in marginal prices below marginal costs).

[36] Ortho Diagnostic Sys., Inc. v. Abbott Labs., Inc., 920 F. Supp. 455, 467–69 (S.D.N.Y. 1996).

label tape, could not profitably match 3M's rebates by reducing its prices.[37] These two tests appear to be equivalent, because an equally-efficient single-product competitor *could* profitably match 3M's rebates unless and until those rebates became so large that, if allocated entirely to 3M's private-label sales, would bring the effective price for private-label tape below 3M's costs. However, LePage's did not attempt either showing. Nor, for the most part, does the record indicate that it even attempted in the market place to match the dollars available under 3M's discount programs.

The two key factors that the court of appeals discussed in explaining its conclusion that 3M's bundled rebate programs were exclusionary should send a chill down the spine of any firm with a large market share that desires to retain its market position.

Absent any showing that 3M's rebates affected LePage's (much less a hypothetically efficient single-product competitor) differently than a steep but above-cost discount on 3M's own private-label sales, the case became indistinguishable in substance—if not in form—from single-product volume discounts, such as those at issue in *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039 (8th Cir. 2000). *Concord Boat* applied *Brooke Group* to overturn a Section 2 judgment against an alleged monopolist's above-cost market share discount programs that, like the 3M programs in *LePage's*, strongly encouraged but did not compel customers to buy from the defendant instead of the plaintiff. The Eighth Circuit, unlike the Third in *LePage's*, emphasized that above-cost discounting is generally desirable and cannot be controlled without "'courting intolerable risks of chilling legitimate price cutting.'" *Concord Boat*, 207 F.3d at 1061 (quoting *Brooke Group*, 509 U.S. at 223). The court of appeals in *LePage's*, by contrast, did not so much as hint that it regarded the millions in rebates paid by 3M as potentially beneficial to consumers and competition.

2. If It's Not "Predatory" Pricing, What Is the Standard? The court of appeals also had a great deal to say about when conduct by a "monopolist" that does not qualify for treatment as predatory pricing is "exclusionary" under Section 2. On this issue of quite general interest to firms with large market shares—not just those with complex bundled rebate programs—the court of appeals did not offer a neat and tidy "standard" for judging when conduct might be deemed exclusionary. Instead, it took refuge in the jury's verdict and emphasized the breadth of Section 2, quoting the D.C. Circuit's comment that "anticompetitive conduct" comes in "'too many different forms, and is too dependent upon context, for any court or commentator ever to have enumerated all the varieties.'"[38]

The two key factors that the court of appeals discussed in explaining its conclusion that 3M's bundled rebate programs were exclusionary should send a chill down the spine of any firm with a large market share that desires to retain its market position. The first, and apparently independently sufficient, factor was harm to LePage's. 3M's conduct caused LePage's to lose sales because it could not (or chose not to) match the deals 3M was able to offer customers. The court's discussion of the "anticompetitive effect" of 3M's bundled rebates provides the clearest indication that it viewed the harm caused LePage's as sufficient to treat 3M's conduct as exclusionary. That discussion focused on the fact that 3M's payments to customers encouraged them to buy 3M's tape, and LePage's could not match 3M's payments by discounting its own private-label tape without suffering reduced profits because of its more limited base of sales. 324 F.3d at 161–62.

[37] The *Areeda-Hovenkamp* treatise endorses this as the proper test for assessing whether a monopolist's bundled discounts are anticompetitive. Areeda & Hovenkamp, *supra* note 23 ("we would require [LePage's] to show that a hypothetical equally efficient firm making only one of the products subject to the bundled rebate could not have competed successfully"). The treatise criticizes the *LePage's* Panel dissent, which focused on LePage's' inability to compete, as being "overly solicitous of small firms" and "den[ying] customers the benefits of the defendants lower costs." *Id.* at 82. Ironically, the en banc majority (incorrectly) cites the same section of this treatise in support of its view that bundled discounts have an "inherent anticompetitive effect." 324 F.3d at 155.

[38] *Id.* at 152 (quoting Caribbean Broad. Sys. Ltd. v. Cable & Wireless PLC, 148 F.3d 1080, 1087 (D.C. Cir. 1998)).

Equally troubling was the fact that the court did not articulate any threshold for the magnitude of harm required to make conduct exclusionary. In LePage's' case, the company lost a meaningful amount of sales and its profits evaporated, but the evidence does not appear to have shown that LePage's suffered a permanently disabling blow. LePage's was not driven out of business, and it still retained 67 percent of the private-label segment when it filed suit. *Id.* at 170 (dissent). Had LePage's been merely one of many rival sellers of transparent tape, harm to LePage's alone might not have been sufficient to constitute exclusion. But LePage's was one of very few tape manufacturers, and the court emphasized that LePage's' harm was equivalent to harm to "competition in general" because "even the foreclosure of '"one significant competitor"' from the market may lead to higher prices and reduced output.'"[39]

The second key factor in the court's analysis was evidence of 3M's *intent* to do away with LePage's and the entire "lower priced" private-label segment of the tape market. *Id.* at 162–163. As the court noted, the "Supreme Court had made clear that intent is relevant to proving monopolization." *Id.* at 163 (citing *Aspen Skiing*, 472 U.S. at 602).

These two factors, however, would seem to be present in many if not most situations where a "monopoly firm" is able to hold onto its market share in the face of competitive challenges. Presumably the successful monopolist will always have caused competitors to lose share, or never to have gained a foothold, and the roster of potential rivals often will be slim. The monopolist will have been able to do something that takes advantage of its existing position and consumers' preferences that would-be challengers cannot successfully match, causing them to lose sales and profits. And presumably the monopolist will always have desired—i.e., intended—that outcome. To be sure, the factual record will not always lead a court or jury to conclude that the monopoly firm foreclosed competition on the merits through its actions, and so the standard—or lack thereof—of *LePage's* will not always be applied to condemn such firms when they prevail in the market. But the case certainly provides little comfort for potential Section 2 defendants.

The potentially overbroad reach of the court's view of exclusionary conduct under Section 2 is reinforced by its praise of the *Alcoa* case as the first of the "modern era." Although the court of appeals accepts Judge Hand's conclusion that that "a firm does not monopolize if monopoly is "thrust upon it" (*Alcoa*, 148 F.2d at 429), it quickly adds that "'size carries with it an opportunity for abuse that is not to be ignored'" (*id.* at 430 (quoting *Swift*, 286 U.S. at 116)), and emphasizes the portion of Judge Hand's ruling in *Alcoa* that criticized Alcoa's "doubling and redoubling of capacity" (148 F.2d at 431) as an exclusionary practice in violation of Section 2. 324 F.3d at 148. *Alcoa* has been widely criticized as having articulated no coherent standard for distinguishing lawful and unlawful behavior by a monopolist and as suggesting "that a firm with monopoly power might violate Section 2 by pursuing normal commercial conduct that is generally considered procompetitive if the effect of such conduct is to enhance its market position."[40]

3. Will a Strong "Business Justification" Undo the Damage? The court's only recognition that there might be situations in which conduct that harms a competitor, or is intended to do so, should be allowed to survive Section 2 scrutiny is its acknowledgement that monopolists may justify their conduct by proving "valid business reasons." That acknowledgement is a possible silver lining in an otherwise bleak decision for firms with large market shares. On closer examination, however, the silver turns to gray.

[39] 324 F.3d at 159 (quoting Roland Mach. Co. v. Dresser Indus., Inc., 749 F.2d 380, 394 (7th Cir. 1984)).

[40] ABA Section of Antitrust Law, Antitrust Law Developments 247 (5th ed. 2002).

According to the court, a monopolist's desire to hold onto its sales—and win sales from smaller rivals—through aggressive use of above-cost price reductions is not a "valid" justification. As the court stated, "[m]aintaining a monopoly is not the type of valid business reason that will excuse exclusionary conduct." 324 F.3d at 164. Instead, to establish a valid business reason the defendant apparently bears the burden of proving concrete cost savings or other efficiencies of such a magnitude as to outweigh any impact on competitors. In *LePage's*, 3M failed this test because it had merely "allude[d]" to benefits to customers from "single invoices and single shipments," *id.*, and the court saw no evidence of "actual economic efficiencies," much less of cost savings that approached the "millions of dollars 3M returned to customers in bundled rebates." *Id.*

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The court's unwillingness to treat the millions 3M "returned to customers" as having any potentially procompetitive weight in the Section 2 calculus is hard to fathom. Just because 3M's rebates sapped LePage's' sales and profits does not alter the fact that consumers reaped millions in savings. It is no answer to suggest, as the court does, that those rebates "'did not benefit the ultimate consumer'" because many of 3M's retail customers may not have passed them on. *Id.* at 163 (quoting district court opinion). This perspective reflects an unduly narrow view of the consumer welfare purposes of the antitrust laws, which treat 3M's retail customers as consumers to the same extent as the "ultimate consumers" that the court apparently preferred to protect.[41] To the extent that LePage's was harmed by the mere fact that 3M's rebates effectively lowered 3M's price for private-label tape, that harm stemmed from the "very essence of competition"[42] and cannot be regarded as "unjustified"—and thus forming the basis for Section 2 liability—without gutting the law's core procompetitive purposes.[43]

The court's apparent insistence on a tight correlation between the defendant's conduct and "actual economic efficiencies" would have made more sense if the court had framed the question differently. It could have asked, first, whether the way 3M's rebates were structured (e.g., the "linkage" to other products) had an adverse effect on LePage's different from that of an equivalent above-cost reduction in the *level* of private-label tape prices alone, and, second, whether the *incremental* effect was justified by some reason other than the desire to harm LePage's. In that situation, the court would have focused on the pernicious effects, if any, of 3M's pricing structure rather than treating as evil the beneficial effects of the reduction in price levels that went along with that structure.

A more economically justified inquiry of this nature might have been carried out in several ways. The court might have asked whether the structure of 3M's pricing made "business sense" but for its effect of precluding LePage's from profitably matching 3M's rebates. Such an inquiry is similar to that applied by the Supreme Court in *Aspen Skiing*, where the defendant's conduct was found unlawful because the defendant had elected to forgo the short-term benefits of a profitable multimountain ticketing arrangement in favor of "reducing competition . . . over the long run." *Aspen Skiing*, 472 U.S. at 608, 610–11. The federal antitrust agencies have similarly observed that in

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[41] For example, the court's perspective is inconsistent with Supreme Court precedent preventing the offensive or defensive use of "passing on." *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968), generally precludes an antitrust defendant from avoiding an antitrust claim by asserting that its direct customer passed on higher prices to the "ultimate customer," while *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), generally prevents the "ultimate consumer" to whom higher prices were passed on from asserting a claim.

[42] Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 594 (1986).

[43] *See Concord Boat*, 207 F.3d at 1062–63.

cases asserting a duty to assist rivals, "conduct is not 'exclusionary' or 'predatory' would make no economic sense for the defendant but for its tendency to eliminate or lessen competition."[44]

Alternatively, the court might have explicitly attempted to balance the anticompetitive aspects of 3M's price structure (i.e., the exclusionary effects exceeding those of an above-cost single-product discount) against the procompetitive benefits of that pricing structure. Such an inquiry would have been similar to the usual weighing of procompetitive benefits against anticompetitive harms that occurs in applying Section 1's rule of reason, and may have been close to the Section 2 balancing process suggested by the D.C. Circuit in *Microsoft*.[45] It would surely have included the beneficial aspects of the price reductions on the procompetitive side of the calculus.

But the court did neither because it skipped the essential first step of sorting out whether 3M's pricing conduct had any effects beyond those of a per se lawful above-cost single-product price reduction. This placed 3M in an untenable position of having not only to justify its choice of pricing structure but to show that the structure achieved efficiencies equal to the millions in price reductions 3M offered its customers.

And it also placed LePage's' claims before the jury in a context where the court's jury instructions offered precious little guidance for distinguishing lawful price competition by a monopolist form illegal monopolization. The jury was asked whether 3M's conduct tended to "impair the opportunities of its rivals . . . in an unnecessarily restrictive way." 324 F.3d at 167. And it was told that 3M could not be held liable if it engaged in "ordinary competitive behavior " or "the conduct of business that is part of the normal competitive process." Instead, to violate Section 2, 3M's conduct must "represent conduct that has made it very difficult or impossible for competitors to engage in fair competition." *Id.* at 168. These instructions apparently were modeled on the ABA sample jury instructions and those given in *Aspen Skiing*, but they appear to have left the jury at sea in attempting to determine whether the quite obvious pain LePage's suffered as a result of 3M's pricing programs constituted something more than the "normal competitive process" and "fair competition."

The easiest way to avoid direct application of LePage's *is for firms to limit their competitive strategies to above-cost single-product price reductions or unstructured volume discounts.*

What Can Defendants Do to Avoid Condemnation (if They Cannot Avoid the Third Circuit)? The *LePage's* case is a dangerous one for firms with large market shares that are not content to sit back and watch their market position erode. If the Supreme Court leaves the decision intact, the case will provide potential plaintiffs with an important weapon against their more successful, larger rivals. Potential defendants will face potential Section 2 condemnation, and significant treble damages, if their competitive strategies cost rivals sales or profits[46] and a jury can be persuaded that those strategies did not constitute "fair" competition. However, there are a few steps defendants can take to minimize the risks created by *LePage's* even if they cannot avoid having their conduct judged in the Third Circuit.

Strategy One: Stick to Single-Product Volume Discounts. The easiest way to avoid direct application of *LePage's* is for firms to limit their competitive strategies to above-cost single-product price reductions or unstructured volume discounts. Such discounts are "concededly legal" according to the court of appeals. 324 F.3d at 154.

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[44] No. 02-682, Brief for the United States and the Federal Trade Commission as Amici Curiae Supporting Petitioner, *Verizon Communications Inc., v. Law Offices of Curtis V. Trinko, LLP* at 15 (U.S. filed May 2003).

[45] *Microsoft*, 253 F.3d at 58–59.

[46] LePage's was awarded over $65 million in damages, after trebling, based on testimony by LePage's' expert about the profits it would have earned had 3M's conduct not caused LePage's to lose market share and forgo anticipated growth. *See* 324 F.3d at 164–65.

More generally, conduct by defendants with "monopoly" power will be viewed with less hostility if they refrain from establishing any linkages between their "monopoly" product and other products they produce, including products in the same line. As the court of appeals' analysis illustrates, such linkages have an inherent potential to create the impression that rivals are being disadvantaged for reasons unrelated to their ability to compete on the merits in the market at issue.

Strategy Two: Be Prepared to Demonstrate the Efficiencies the Firm's Behavior Achieves. Pursuing Strategy One alone probably will be unsatisfactory in many cases because creating linkages among products often has the potential to enhance efficiency and meet customer demand.[47] Where those motivations spur firms with high market shares to consider offering bundled discount programs, the LePage's decision counsels strongly in favor of taking two key steps first:

- Educate company personnel—including through vigorous antitrust compliance programs—not to devise strategies aimed at preventing rivals from competing on the merits. Also help that personnel understand the importance of perceptions, so that they do not author documents that might be misunderstood as suggesting a desire to do away with competitors or raise prices in the long run, as distinct from a desire to retain or grow business by offering a value proposition that customers prefer. Stated another way, a monopolization case is more likely to go badly if a jury sees documents that say things like "we are doing this to 'kill' our competitors so we can raise prices"; and if such documents already exist it would be good to know about them before a discount program or other strategy achieves that effect.
- Equally important, a firm should be prepared to quantify the efficiency benefits that it expects to flow from the proposed course of action. It would be of tremendous value to be able to show a court (or jury, if it comes to that) a serious quantitative analysis, conducted before a program was initiated, that laid out the rationale for the program and its structural elements. Ideally that analysis would demonstrate that a single-product competitor with comparable costs could profitably match the potential price reductions achieved by the program. Even better—and of particular importance if the first analysis does not reach the desired conclusion—would be a more rigorous analysis that quantifies the specific cost savings or other efficiencies that underlie the design of a "bundled" pricing structure that might have the incidental effect of making life difficult for single-product rivals. ●

[47] Those potential benefits are widely recognized in the law of tying.