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ARTICLES

PREDATORY PRICING AND RECOUPMENT

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Predatory pricing is a two-step strategy for securing monopoly profits. During the first step—the predation stage—a firm charges a price below its costs in the hope of driving its competitors out of the market by forcing them to sell at a loss as well. If it succeeds, the firm can proceed to the second step—the recoupment stage. After it has the market to itself, the now-dominant firm charges a monopoly price in an effort to recoup the losses it sustained in the predation stage and to earn a steady stream of monopoly profits into the future.

Predatory pricing violates section 2 of the Sherman Act, which prohibits the use of anticompetitive conduct to acquire or maintain monopoly power. Predatory pricing is one form of anticompetitive conduct. Many judges and scholars, however, believe that predatory pricing does not occur because the two-step strategy combines significant up-front costs with a low probability of success. This skepticism has led courts to impose a recoupment element for section 2 predatory pricing claims. The recoupment element requires an antitrust plaintiff bringing a predatory pricing claim to prove that the defendant will be able to acquire monopoly power and to charge a monopoly price for long enough to make the whole scheme profitable. Antitrust liability becomes a function of the defendant's profitability.

This Article discusses the evolution of and rationale for the recoupment requirement. It shows how recoupment analysis by courts is often flawed, largely because judges incorrectly assume that market entry, which can prevent recoupment, is easy. This Article then illustrates the many ways in which recoupment can occur, including recoupment in other markets and recoupment through cartel or oligopoly pricing. Despite these various modes of recoupment, federal courts have sometimes structured the recoupment requirement in a way that is literally impossible to satisfy. This Article advocates more fine-tuned recoupment analysis.

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After exploring the judicial misapplication of the recoupment requirement, this Article challenges the underlying premises of the element by showing how predatory pricing can hurt consumers and competition even if a firm engaged in predatory pricing is unable to eventually recoup its losses. Ultimately, the recoupment requirement does not distinguish between anticompetitive and benign (or beneficial) conduct. This Article concludes by explaining how eliminating the recoupment requirement in predatory pricing litigation would better serve the purposes of antitrust law.

INTRODUCTION

Antitrust law condemns conduct and agreements that unreasonably restrain trade. The goal of antitrust law is to protect competition in the marketplace. Beginning with the Supreme Court's opinion breaking up Standard Oil over a century ago, antitrust law has been concerned with predatory pricing. In its most basic form, predatory pricing is a two-step strategy for securing monopoly profits. During the predation phase, the firm charges a price below its costs in the hopes that its competitors will be unwilling or unable to sustain the losses they would incur if they matched the below-cost price and will exit the market. After the rivals are vanquished, the post-predation phase begins. With the market to itself, the dominant firm charges a monopoly price with the goal of recouping the losses it sustained during the predation phase and then earning a steady stream of excess profits into the future.[1] If executed successfully, this two-stage process can secure the predatory firm more money than it would get by vying for customers in a competitive marketplace. While no federal statute explicitly condemns predatory pricing, pricing below cost implicates several antitrust causes of action. First and foremost, predatory pricing may violate section 2 of the Sherman Act, which prohibits mo-

1. Transamerica Computer Co. v. IBM, 698 F.2d 1377, 1384 (9th Cir. 1983) ("Predatory pricing occurs when a company that controls a substantial market share lowers its prices to drive out competition so that it can charge monopoly prices, and reap monopoly profits, at a later time.").

nopolization and attempted monopolization[2]—that is, a dominant firm's use of anticompetitive conduct to acquire or maintain monopoly power in a relevant market.[3] Predatory pricing qualifies as a form of anticompetitive conduct. Second, predatory pricing can implicate section 1 of the Sherman Act when it is pursued jointly through an agreement among competitors. Section 1 of the Sherman Act condemns agreements that unreasonably restrain trade and, in theory, predatory pricing conspiracies violate section 1.[4] Third, predatory pricing can also violate the Robinson-Patman Act. The Robinson-Patman Act condemns certain forms of price discrimination, such as when a firm charges a profitable price in one geographic market and a predatory price in another geographic market, using the profits from the first market to subsidize predation in the second.[5] Most predatory pricing litigation is brought under section 2 of the Sherman Act, which is the focus of this Article.

Predatory pricing has long been a controversial cause of action in antitrust. Many judges and scholars believe that successful predatory pricing simply does not occur because price predation is a high-risk strategy that entails significant up-front costs and a low likelihood of sustained profitability.[6] This skepticism has led courts to impose a recoupment element for section 2 predatory pricing claims. The recoupment element requires a predatory pricing plaintiff to prove that the defendant will be able to acquire monopoly power and charge a monopoly price long enough to make the whole scheme profitable.

Since its creation in the 1980s, the recoupment requirement has been little scrutinized, which is surprising given that this lone element

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2. 15 U.S.C. § 2 (2012) ("Every person who shall monopolize, or attempt to monopolize, . . . any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony . . . .").

3. E.g., United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966) (defining monopolization). Section 2 also condemns attempted monopolization when a firm with a significant market share and a specific intent to monopolize engages in anticompetitive conduct with a dangerous probability of monopolizing a relevant market. Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 454 (1993) (articulating required elements of attempt to monopolize).

4. 15 U.S.C. § 1 ("Every contract, combination . . . , or conspiracy, in restraint of trade . . . is declared to be illegal.").

5. 15 U.S.C. § 13(a) ("It shall be unlawful for any person engaged in commerce . . . to discriminate in price between different purchasers of commodities of like grade and quality . . . where the effect of such discrimination may be substantially to lessen competition . . . ."); United States v. Nat'l Dairy Prods. Corp., 372 U.S. 29, 33–34 (1963) ("The 1936 enactment of the Robinson-Patman Act was . . . aimed at a specific weapon of the monopolist—predatory pricing.").

6. See Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986) ("[T]here is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful."); Bathke v. Casey's Gen. Stores, Inc., 64 F.3d 340, 343 (8th Cir. 1995) ("[T]he Supreme Court has urged great caution and a skeptical eye when dealing with unfair [predatory] pricing claims.").

has effectively eliminated the viability of predatory pricing claims. After presenting the origins of the recoupment requirement, this Article explains why the recoupment element is both unnecessary and counterproductive. To appreciate why the recoupment requirement is superfluous, it is instructive to compare two scenarios: predatory pricing with recoupment and predatory pricing without recoupment. In Scenario 1, Firm *A* makes widgets and has two competitors. The average variable cost of making the product is $10 per unit. In an effort to eliminate its two competitors, Firm *A* reduces its price to $9 per unit. The two competitors remain in the market for two years before exiting the market entirely. During this time, Firm *A* sells two million units of product and racks up losses of approximately $2 million. After the competitors exit the market, Firm *A* begins charging a monopoly price, $11 per unit, and continues to sell one million units each year for three years until a new firm enters the market and bids the price back down to $10 per unit. Assume a discount rate of zero for simplicity, and the price predation seems like a profit-maximizing strategy. During the monopoly period, Firm *A* earns $3 million in monopoly profits. Firm *A* will have recouped its $2 million investment in predatory pricing in the first two years and received an additional $1 million in monopoly profits during the third year.

In Scenario 2, all of the facts remain the same with one exception: Firm *A* reduces its price to $8 per unit. This means that its losses during the predation period total $4 million. After its competitors exit the market, Firm *A* will again earn $3 million in monopoly profits until a new rival enters the market and restores the competitive price. Firm *A* will not recoup its investment in predation and will instead lose $1 million despite its monopoly position for two years.

In both scenarios, Firm *A* acquires monopoly power through predatory pricing. The competitors suffer the same antitrust injury and consumers in the post-predation period have paid the same monopoly overcharges. Yet because of the recoupment requirement, Firm *A* has only violated section 2 of the Sherman Act in Scenario 1, not Scenario 2. This makes little sense because in both scenarios, Firm *A* has engaged in predatory pricing and has imposed the same injuries on its competitors and consumers. The failure to profit from anticompetitive conduct should not immunize that conduct from liability.

Part I of this Article discusses the evolution of and rationale for this recoupment requirement. It explains how courts imposed the recoupment requirement in section 2 litigation through a misapplication of a section 1 case. Courts and commentators have justified the recoupment requirement as necessary to reduce the risk of an innocent firm being held liable for predatory pricing. Further, they argue that predatory pricing harms neither consumers nor competition unless the predator recoups its investment in below-cost pricing.

Part II examines the recoupment requirement in operation. It explains how federal courts are often too quick to conclude that a defendant could not recoup its investment in an alleged predatory pricing scheme. Part II examines the many ways that recoupment is possible—ways that federal judges often fail to appreciate. In some cases, courts have structured the recoupment requirement in a way that is literally impossible to satisfy. The recoupment requirement has made it exceedingly difficult for predatory pricing claims to survive summary judgment. If the recoupment requirement is to serve its intended function, judges need to recognize the many ways that below-cost pricing can be profitable.

Part III challenges the underlying premises of the recoupment requirement. It shows how predatory pricing can hurt consumers and competition even without recoupment. In particular, consumers who purchase during the post-predation period when prices are supracompetitive suffer antitrust injury regardless of the monopolist's profitability. Part III also examines the inefficiency inherent in price predation.

Part IV advocates eliminating the recoupment requirement for monopolization claims based on predatory pricing. The primary justification for the recoupment requirement is to reduce the risk of false positives. Part IV explains how other screens for false positives are better than the recoupment element. It then shows how the recoupment requirement can create false negatives in antitrust litigation and explores the costs of this form of judicial error. Finally, it explains why the profitability of anticompetitive conduct is generally irrelevant in antitrust jurisprudence.

I. THE RECOUPMENT REQUIREMENT IN PREDATORY PRICING JURISPRUDENCE

A. *The Evolution of the Recoupment Requirement*

The Supreme Court first recognized predatory pricing as an antitrust violation in *Standard Oil Co. v. United States.*[7] In the following decades, antitrust plaintiffs enjoyed a high success rate in predatory pricing cases.[8] Early courts did not require plaintiffs to prove that the defendant either recouped its investment in below-cost pricing or had a reasonable

7. E.g., Christopher R. Leslie, Revisiting the Revisionist History of *Standard Oil*, 85 S. Cal. L. Rev. 573, 573 (2012) [hereinafter Leslie, *Standard Oil*] (discussing Supreme Court's condemnation of Standard Oil's anticompetitive conduct, including predatory pricing).

8. See, e.g., Patrick Bolton, Joseph F. Brodley & Michael H. Riordan, Predatory Pricing: Strategic Theory and Legal Policy, 88 Geo. L.J. 2239, 2250 (2000) [hereinafter Bolton, Brodley & Riordan, Predatory Pricing] (noting, prior to Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993), "[p]laintiffs won most litigated cases"); James D. Hurwitz & William E. Kovacic, Judicial Analysis of Predation: The Emerging Trends, 35 Vand. L. Rev. 63, 140–45 (1982) (observing higher degree of plaintiff success in pre-*Brooke Group* era of predatory pricing cases).

probability of doing so.[9] Judicial and scholarly attention focused more on the appropriate measurement of cost for predatory pricing claims. In a famous article, Professors Phillip Areeda and Donald Turner proposed a legal test based on average variable cost (AVC) being used as a proxy for marginal cost.[10] Under this test, a price below AVC was presumed to be predatory while a price above AVC was presumed lawful. As courts adopted variations of the Areeda-Turner test, plaintiffs' success rates fell.[11]

The Supreme Court revisited the predatory pricing debate with its opinion in *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*[12] In *Matsushita,* American manufacturers of consumer electronics products brought a claim under section 1 of the Sherman Act, asserting that Japanese manufacturers of consumer electronics had conspired to charge predatorily low prices in the American market in order to drive American firms out of business.[13] According to the complaint, after the Japanese firms had the American market to themselves, they would operate as a cartel in America, as they were doing in Japan.[14] The Third Circuit held that plaintiffs had presented sufficient evidence to survive summary judgment.[15] The Supreme Court reversed in a 5-4 opinion.[16]

The *Matsushita* majority expressed skepticism about the rationality of predatory pricing conspiracies. The plaintiffs' theory assumed that the defendants had collectively agreed to sustain losses for several years, and the Court reasoned that for this "investment to be rational, the conspirators must have a reasonable expectation of recovering, in the form of later monopoly profits, more than the losses suffered."[17] The majority believed that recoupment was unlikely given that the predation would have to eliminate the American manufacturers from the market in order for the conspirators to be able to raise their prices, but this subsequent increase in price would encourage the eliminated manufacturers (or new

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9. See Timothy J. Trujillo, Note, Predatory Pricing Standards Under Recent Supreme Court Decisions and Their Failure to Recognize Strategic Behavior as a Barrier to Entry, 19 J. Corp. L. 809, 813 (1994) (noting in earlier period "[b]elow cost pricing plus anticompetitive intent appeared to be all that was necessary" to stake a claim).

10. Phillip Areeda & Donald F. Turner, Predatory Pricing and Related Practices Under Section 2 of the Sherman Act, 88 Harv. L. Rev. 697, 716–17 (1975) [hereinafter Areeda & Turner, Predatory Pricing].

11. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2250–51, 2253.

12. 475 U.S. 574 (1986).

13. Id. at 577–78 (discussing plaintiffs' theory of case).

14. Id. at 584 (discussing respondents' allegations of planned future cartelization in United States).

15. Id. at 580.

16. Id. at 582.

17. Id. at 588–89.

ones) to reenter the market during the post-predation period.[18] The Court claimed the existence of "a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful."[19] These commentators had argued that a single monopolist would be unlikely to recoup the losses associated with predatory pricing.[20] The Court noted that the *Matsushita* defendants would have to recoup through cartel pricing, which was even less likely given the inherent instability of cartels.[21] Asserting a low likelihood of recoupment, the Court held that the plaintiff's theory of the case made "no practical sense"[22] and absent "evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently," the defendants were entitled to summary judgment.[23] At its heart, the *Matsushita* opinion establishes a summary judgment standard for section 1 cases. If an alleged conspiracy appears irrational to the reviewing judge, the plaintiff must present more evidence to survive summary judgment.

Matsushita was a section 1 case, involving an alleged conspiracy to restrain trade, and not a section 2 case; it involved no allegations of unilateral anticompetitive conduct. *Matsushita*'s reasoning, nevertheless, wound its way into section 2 jurisprudence. In *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.* (*Rose Acre*), the Seventh Circuit considered a case against a single seller accused of engaging in below-cost pricing in violation of section 2 of the Sherman Act as well as the Robinson-Patman

18. Id. at 589 (citing Robert H. Bork, The Antitrust Paradox 145 (1978); John S. McGee, Predatory Pricing Revisited, 23 J.L. & Econ. 289, 295–97 (1980)).

19. Id.; see also Cargill, Inc. v. Monfort of Colo., 479 U.S. 104, 121–22 n.17 (1986) ("Although the commentators disagree as to whether it is ever rational for a firm to engage in such conduct, it is plain that the obstacles to the successful execution of a strategy of predation are manifold, and that the disincentives to engage in such a strategy are accordingly numerous.").

20. Robert H. Bork, The Antitrust Paradox 149–55 (1978) [hereinafter Bork, Paradox]; Areeda & Turner, Predatory Pricing, supra note 10, at 699; John S. McGee, Predatory Price Cutting: The *Standard Oil (N.J.)* Case, 1 J.L. & Econ. 137 (1958) [hereinafter McGee, *Standard Oil*]; John S. McGee, Predatory Pricing Revisited, 23 J.L. & Econ. 289, 292–94 (1980) [hereinafter McGee, Revisited].

21. 475 U.S. at 590–92. Cartels are inherently unstable for two related reasons. First, every member of the cartel has a strong incentive to cheat by charging less than the cartel price and stealing sales away from its cartel partners. See Christopher R. Leslie, Cartels, Agency Costs, and Finding Virtue in Faithless Agents, 49 Wm. & Mary L. Rev. 1621, 1629–30 (2008) (describing opportunities to maximize profit by cheating). Second, cartels often suffer from significant coordination problems as the conspirators negotiate price, production limits, market allocation, and enforcement mechanisms. See Herbert Hovenkamp & Christopher R. Leslie, The Firm as Cartel Manager, 64 Vand. L. Rev. 813, 825–34 (2011) (discussing coordination problems faced by prospective cartels).

22. *Matsushita*, 475 U.S. at 597.

23. Id. at 588 (quoting Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752, 764 (1984)); see also Instructional Sys. Dev. Corp. v. Aetna Cas. & Sur. Co., 817 F.2d 639, 646 (10th Cir. 1987) ("The [*Matsushita*] Court held that under these circumstances, the plaintiffs had failed to create a fact issue on the existence of a section 1 conspiracy.").

Act.[24] Writing for the court, Judge Frank Easterbrook asserted that *Matsushita*'s "holding [was] that recoupment would be so unlikely that antitrust inquiry could not be justified."[25] He further cited *Matsushita* as standing for the proposition that "[b]ecause unsuccessful predation is unprofitable, it is bootless for the legal system to intervene."[26] This misrepresents the Supreme Court's holding: *Matsushita* did not hold that unprofitable predation is immune from antitrust liability. Rather, the Court held that the unlikelihood of recoupment meant that a jury in a section 1 case could not infer the presence of a conspiracy absent compelling evidence of an agreement.[27] *Matsushita* had nothing to do with the standards for determining a section 2 violation. Judge Easterbrook never acknowledged that *Matsushita* was a section 1 case about the level of evidence an antitrust plaintiff needs to survive summary judgment, not a section 2 case on the elements necessary for liability.

Judge Easterbrook incorrectly asserted that the *Matsushita* Court adopted a recoupment requirement for all predatory pricing cases.[28] Although the *Matsushita* Court itself noted that its observations about the difficulties of recoupment "apply even to predatory pricing by a single firm seeking monopoly power,"[29] Judge Easterbrook converted *Matsushita*'s observation about the difficulty of recoupment into a requirement that plaintiffs must prove recoupment in section 2 predatory pricing cases. The *Rose Acre* opinion held: "The investment must be recouped. If a monopoly price later is impossible, then the sequence is unprofitable and we may infer that the low price now is not predatory."[30] By sleight of hand, Judge Easterbrook held that if there is no likelihood of recoupment, then there must not be any pricing below cost. Thus, a plaintiff's failure to prove probability of recoupment entitled the defendant to summary judgment.

Rose Acre was flawed, but prescient. The Supreme Court next considered predatory pricing in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*[31] When Liggett found its share of the American tobacco market in decline, it began making and marketing low-priced generic cigarettes.[32] This action both took sales away from branded-cigarette manufacturers and constrained their ability to raise price.[33] In reaction, Brown &

24. 881 F.2d 1396, 1399 (7th Cir. 1989).

25. Id. at 1401.

26. Id. (citing *Matsushita*, 475 U.S. at 595).

27. *Matsushita*, 475 U.S. at 597–98.

28. *Rose Acre*, 881 F.2d at 1401 ("Only if market structure makes recoupment feasible need a court inquire into the relation between price and cost.").

29. *Matsushita*, 475 U.S. at 590 (emphasis omitted).

30. *Rose Acre*, 881 F.2d at 1401.

31. 509 U.S. 209 (1993).

32. Id. at 214.

33. Id.

Williamson (B&W) began making generic cigarettes and undercutting Liggett's price in that market.[34] Liggett brought suit under the Robinson-Patman Act, claiming that B&W was engaging in illegal predatory pricing.[35] Liggett did not claim that B&W was attempting to monopolize the market for generic cigarettes. Instead, Liggett claimed that B&W's predatory pricing was designed to pressure Liggett to "raise its list prices on generic cigarettes, so that the percentage price difference between generic and branded cigarettes would narrow.... The resulting reduction in the list price gap... would restrain the growth of the economy segment and preserve Brown & Williamson's supracompetitive profits on its branded cigarettes."[36] According to Liggett's theory, B&W would recoup its losses through oligopoly pricing[37] in the branded cigarette market after the price of generic cigarettes rose and stopped constraining price increases in branded cigarettes.[38] The district court overturned a jury verdict in favor of Liggett. The Fourth Circuit affirmed.[39]

The Supreme Court used *Brooke Group* as a vehicle for imposing a recoupment requirement in section 2 predatory pricing cases. The Court began by noting that although Liggett had brought its claim under the Robinson-Patman Act, the Court's opinion would apply equally to predatory pricing claims brought pursuant to section 2 of the Sherman Act.[40] Despite the different nomenclature,[41] the Court reasoned that "the essence of the claim under either statute is the same: A business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market."[42] Thus, the Court held that whether the plaintiff

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34. Id. at 215.

35. Id. at 216.

36. Id. at 217.

37. Oligopoly pricing occurs when competitors in a concentrated market tacitly raise their prices above competitive levels without explicitly communicating or fixing prices. Although the alleged recoupment mechanism involved multiple sellers, in contrast to the conspiracy allegations of *Matsushita*, *Brooke Group* involved one defendant accused of price predation.

38. *Brooke Group*, 509 U.S. at 212.

39. Liggett Grp., Inc. v. Brown & Williamson Tobacco Corp., 964 F.2d 335, 342 (4th Cir. 1992), aff'd sub nom. *Brooke Group*, 509 U.S. 209.

40. *Brooke Group*, 509 U.S. at 222. The Court explained that the two antitrust provisions address the same problem because "primary-line competitive injury under the Robinson-Patman Act is of the same general character as the injury inflicted by predatory pricing schemes actionable under § 2 of the Sherman Act." Id. at 221.

41. Id. at 222 ("[W]e interpret § 2 of the Sherman Act to condemn predatory pricing when it poses 'a dangerous probability of actual monopolization,' whereas the Robinson-Patman Act requires only that there be 'a reasonable possibility' of substantial injury to competition . . . ." (citation omitted) (quoting Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 455 (1993); Falls City Indus., Inc. v. Vanco Beverage, Inc., 460 U.S. 428, 434 (1983))).

42. Id.

"alleges predatory pricing under § 2 of the Sherman Act or . . . under the Robinson-Patman Act, two prerequisites to recovery remain the same."[43] First, the plaintiff must establish that the defendant charged prices that were "below an appropriate measure of its . . . costs."[44] Second, the plaintiff must establish recoupment by showing several steps, beginning with a showing that the "below-cost pricing [is] capable, as a threshold matter, of producing the intended effects on the firm's rivals, whether driving them from the market, or . . . causing them to raise their prices to supracompetitive levels within a disciplined oligopoly."[45] If the target of the predation does not succumb, then the predator will not be able to enter the recoupment phase of the strategy.[46] Assuming the defendant drives its rivals from the market, the predator must then be able to raise price in a sustained manner.[47] The underlying premise of the predatory pricing claim is that the defendant is attempting to vanquish rivals through below-cost pricing in order to recoup the losses through monopoly pricing later.[48] The *Brooke Group* majority opinion noted that "[r]ecoupment is the ultimate object of an unlawful predatory pricing scheme; it is the means by which a predator profits from predation."[49] The Court converted the defendant's aspirations into the plaintiff's burden. In order to satisfy the recoupment element, the *Brooke Group* majority held:

> The plaintiff must demonstrate that there is a likelihood that the predatory scheme alleged would cause a rise in prices above a competitive level that would be sufficient to compensate for the amounts expended on the predation, including the time value of the money invested in it. As we have observed on a prior occasion, "[i]n order to recoup their losses, [predators] must obtain enough market power to set higher than competitive prices, and then must sustain those prices long enough to earn in excess profits what they earlier gave up in below-cost prices."[50]

After *Brooke Group*, the recoupment requirement became an established element for predatory pricing claims brought under section 2 of

43. Id.

44. Id.

45. Id. at 225.

46. See id. ("The inquiry is whether, given the aggregate losses caused by the below-cost pricing, the intended target would likely succumb.").

47. Id. at 225–26.

48. See Areeda & Turner, Predatory Pricing, supra note 10, at 698 ("[T]he classically-feared case of predation has been the deliberate sacrifice of present revenues for the purpose of driving rivals out of the market and then recouping the losses through higher profits earned in the absence of competition.").

49. *Brooke Group*, 509 U.S. at 224.

50. Id. at 225–26 (alterations in *Brooke Group*) (quoting Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 590–91 (1986)).

the Sherman Act.[51] This created a unique burden for antitrust plaintiffs making predatory pricing claims. In general, section 2 requires the plaintiff to prove that the defendant acquired or maintained monopoly power through anticompetitive conduct. In predatory pricing cases, the recoupment requirement imposes an additional element that the monopolist generated sufficient monopoly profits to exceed its investment in anticompetitive conduct.

B. *The Rationale Behind the Recoupment Requirement*

Courts and commentators have provided several related justifications for imposing a recoupment element in section 2 predatory pricing claims. First, the recoupment requirement is defended as a method of minimizing the risk of false positives. Second, several judges and scholars have argued that attempts at predatory pricing inflict no anticompetitive harm in the absence of recoupment. Third, the recoupment requirement is justified as an effective filter that lets judges avoid the more complicated issues of intent and price-cost relationships.

1. *The Risk of False Positives.* — A false positive exists if a defendant is found liable when, in fact, it has not violated the law. The section 2 cause of action for predatory pricing creates the risk of false positives because an efficient firm that can lower its cost of production and then pass those savings on to consumers should be rewarded with a higher market share, not punished with an antitrust lawsuit. When an inefficient firm loses sales to a competing firm that charges a lower price, the firm with diminishing market share may be tempted to accuse its rival of pricing below cost.[52] Because inefficient rivals may take advantage of a legal standard

51. See, e.g., Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 900 (9th Cir. 2008) ("As the Supreme Court explained in *Brooke Group*, a plaintiff in a single product predatory pricing case must establish that the defendant priced below cost and that there was a probability the defendant could recoup the losses it suffered during the predation period."); Stearns Airport Equip. Co. v. FMC Corp., 170 F.3d 518, 528 (5th Cir. 1999) (explaining "[t]o succeed, such a [predatory pricing] claim must demonstrate . . . that the alleged monopolist has a reasonable chance of recouping the losses through below-cost pricing" (citing *Brooke Group*, 509 U.S. at 222–24)); Nat'l Parcel Servs., Inc. v. J.B. Hunt Logistics, Inc., 150 F.3d 970, 971 (8th Cir. 1998) ("[P]laintiff must prove . . . 'that the competitor had . . . a dangerous probability of recouping its investment in below-cost prices.'" (quoting *Brooke Group*, 509 U.S. at 222–24)); Coastal Fuels of P.R., Inc. v. Caribbean Petrol. Corp., 79 F.3d 182, 191 (1st Cir. 1996) ("[T]he plaintiff must show that the predator stands some chance of recouping his losses.").

52. See William J. Baumol & Janusz A. Ordover, Use of Antitrust to Subvert Competition, 28 J.L. & Econ. 247, 255 (1985) (claiming less efficient firms "advocate their [own] costing approach . . . to limit the price-cutting opportunities" of rivals made more efficient through "legitimate sources of superiority"); Michael L. Denger & John A. Herfort, Predatory Pricing Claims After *Brooke Group*, 62 Antitrust L.J. 541, 541 (1994) (noting difficulty of distinguishing between legitimate and predatory low pricing may encourage false antitrust allegations by competitors).

for predatory pricing that is either too vague or too liberal,[53] courts must be able to distinguish between beneficial, procompetitive price cuts and predatory, anticompetitive price cuts. Courts may find it difficult to make this distinction because, as the Supreme Court has noted, "the mechanism by which a firm engages in predatory pricing—lowering prices—is the same mechanism by which a firm stimulates competition."[54] If judges are not careful, predatory pricing "can easily be confused with merely low prices which benefit customers."[55]

Courts in antitrust cases endeavor to reduce the number of false positives because false positives punish innocent firms and can distort business decisions. A false positive in predatory pricing litigation—when a defendant is found liable for illegal monopolization through predatory pricing when it has in fact been charging a price above cost—means that an efficient firm is penalized for engaging in beneficial conduct.[56] If antitrust law were to improperly condemn harmless or beneficial price reductions, "[r]isk averse firms in particular might avoid legitimate pricing strategies out of fear of prosecution or litigation."[57] Ironically, an overly broad predatory pricing regime could "'chill the very behavior the antitrust laws seek to promote.'"[58] In theory, this could prevent markets from operating efficiently.[59] Ultimately, consumers are made worse off as the

53. See Peter C. Carstensen, Predatory Pricing in the Courts: Reflection on Two Decisions, 61 Notre Dame L. Rev. 928, 938 (1986) (arguing inefficient competitors can make anticompetitive use of vague predatory pricing standards).

54. Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 122 n.17 (1986); see also Vollrath Co. v. Sammi Corp., 9 F.3d 1455, 1460 (9th Cir. 1993) ("Economic reality is that, generally, price reduction is the very essence of competition. Thus, care must be taken in drawing the line between pricing that enhances competition and predatory pricing that is designed to eliminate competition.").

55. Tri-State Rubbish, Inc. v. Waste Mgmt., Inc., 998 F.2d 1073, 1080 (1st Cir. 1993).

56. See, e.g., Dial A Car, Inc. v. Transp., Inc., 82 F.3d 484, 487 (D.C. Cir. 1996) ("Predatory pricing claims, because they are premised on a temporary increase in competition, inherently ask the court to penalize potentially beneficial conduct.").

57. Joseph F. Brodley & George A. Hay, Predatory Pricing: Competing Economic Theories and the Evolution of Legal Standards, 66 Cornell L. Rev. 738, 790 (1981).

58. Bayou Bottling, Inc. v. Dr Pepper Co., 725 F.2d 300, 305 (5th Cir. 1984) (quoting Ne. Tel. Co. v. AT&T, 651 F.2d 76, 88 (2d Cir. 1981)); see also United States v. AMR Corp., 335 F.3d 1109, 1114 (10th Cir. 2003) ("Chicago scholars argued that lowering prices could only be pro-competitive and any prohibition on such conduct could ultimately deter firms from engaging in conduct that is socially beneficial." (citing Richard J. Pierce, Jr., Is Post-Chicago Ready for the Courtroom? A Response to Professor Brennan, 69 Geo. Wash. L. Rev. 1103, 1106 (2001))); Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1197 (3d Cir. 1995) (noting "danger of chilling competition" through "[e]rroneous jury verdicts for plaintiffs in predatory pricing cases").

59. Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 231 (1st Cir. 1983) ("[A] legal precedent or rule of law that prevents a firm from unilaterally cutting its prices risks interference with one of the Sherman Act's most basic objectives: the low price levels that one would find in well-functioning competitive markets.").

fear of predatory pricing liability keeps prices artificially higher than they otherwise would be.[60]

Courts have justified the recoupment requirement as reducing false positives. Federal judges have surmised that the Supreme Court created the recoupment requirement "to distinguish aggressive but competitive price cutting (assumed to be good for competition and consumers) from predatory, anti-competitive price cutting (assumed to be ultimately bad for consumers and competition)."[61] If judges can accurately use a firm's inability to recoup as a proxy for whether the defendant firm would have undertaken a strategy of pricing below cost, the argument goes, this could reduce false positives. As the Fifth Circuit explained, "[i]f there is no likelihood of recoupment, it would seem improbable that a scheme would be launched. Given the high error cost of finding companies liable for cutting prices to the consumer, the court should thus refuse to infer predation."[62] Thus, in the name of stopping false positives, Judge Easterbrook's supposition in *Rose Acre* has triumphed: If the judge does not believe that recoupment is likely, then the defendant must not have priced below its cost.[63]

2. *No Anticompetitive Harm Absent Recoupment.* — Courts also justify the recoupment requirement by arguing that absent recoupment, pricing below cost harms neither consumers nor competition. For example, courts have reasoned that "[p]redatory pricing is only harmful when the predator succeeds in recouping the losses it suffered by its earlier below-cost pricing."[64] Most courts treat an attempt at predatory pricing as beneficial to consumers and as having no anticompetitive consequences so long as it fails to generate a net profit for the predator.

60. See Morgan v. Ponder, 892 F.2d 1355, 1358–59 (8th Cir. 1989) ("Indeed, there is a real danger in mislabeling such practices as predatory, because consumers generally benefit from the low prices resulting from aggressive price competition.").

61. Wheeling-Pittsburgh Steel Corp. v. Mitsui & Co., 35 F. Supp. 2d 597, 602–03 (S.D. Ohio 1999); see also Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224 (1993) ("Without [recoupment], predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced."); Mathias v. Daily News, L.P., 152 F. Supp. 2d 465, 473 (S.D.N.Y. 2001) ("Absent the reasonable possibility of success in such recoupment, below-cost pricing cannot be anticompetitive because a failed predatory pricing scheme only results in lower aggregate prices for the consumer, again, a pro-competitive outcome."); Chris Sagers, "Rarely Tried, and . . . Rarely Successful": Theoretically Impossible Price Predation Among the Airlines, 74 J. Air L. & Com. 919, 928 n.44 (2009) (noting common view of commentators that predatory pricing "will ordinarily be very hard to distinguish from legitimate price competition, and will impose no social harm unless recoupment succeeds").

62. Stearns Airport Equip. Co. v. FMC Corp., 170 F.3d 518, 528 (5th Cir. 1999).

63. A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1401 (7th Cir. 1989) (noting "[o]nly if market structure makes recoupment feasible need a court inquire into the relation between price and cost").

64. W. Parcel Express v. UPS, 65 F. Supp. 2d 1052, 1063 (N.D. Cal. 1998).

a. *No Consumer Harm.* — Predatory pricing is a two-stage strategy. During the predation stage, the predator cuts price below cost in order to drive competitors from the market or to compel them to succumb to its demands—be they to raise price or reduce certain sales. During the recoupment stage, the predator acts like a monopolist: raising price, reducing output, and converting consumer surplus into producer surplus. The conventional wisdom holds that consumers benefit during the predation stage and are harmed only during the recoupment stage.

Several courts have reasoned that price predators who fail to recoup create a boon for consumers. For example, in *Rose Acre*, Judge Easterbrook wrote, "Price less than cost today, followed by the competitive price tomorrow, bestows a gift on consumers. Because antitrust laws are designed for the benefit of consumers, not competitors, a gift of this kind is not actionable."[65] The Supreme Court echoed this rationale in *Brooke Group* when it opined that without recoupment, "predatory pricing produces lower aggregate prices in the market, and consumer welfare is enhanced."[66] Courts have thus reasoned that, absent recoupment, antitrust law should embrace the gift of below-cost prices for consumers, not condemn it.[67]

b. *No Competitive Harm.* — During the predation stage—before recoupment is attempted—the predator's rivals could be injured in one of two ways. If they match the predator's price, they may incur losses on each sale made. If they decline to match the loss-inducing price, they may lose sales as consumers take advantage of the below-cost pricing by the predator. Even a more efficient competitor can find itself losing sales and money to a price predator.

Despite this injury to efficient rivals, courts and commentators argue that in the absence of recoupment, no anticompetitive harm takes place. Some commentators have suggested that the predator's competitors "suffer no antitrust injury until they are actually driven from the market."[68] Even when rivals leave the market, however, courts hold that the preda-

65. *Rose Acre*, 881 F.2d at 1401 (citations omitted).

66. *Brooke Group*, 509 U.S. at 224; see also Atl. Richfield Co. v. USA Petrol. Co., 495 U.S. 328, 340 (1990) ("Low prices benefit consumers regardless of how those prices are set . . . ."); Michael L. Freedman, Note, Predatory Pricing After *Brook Group*: Economic Goals Prevail [sic], 58 Alb. L. Rev. 243, 253 (1994) ("Without the possibility of recoupment, below-cost pricing results in enhanced consumer welfare and will not be discouraged by the courts." (citing *Brooke Group*, 509 U.S. at 224–25)).

67. See, e.g., Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1200 (3d Cir. 1995) ("Such futile below-cost pricing effectively bestows a gift on consumers, and the Sherman Act does not condemn such inadvertent charity.").

68. Am. Bar Ass'n Section of Antitrust Law, Proving Antitrust Damages: Legal and Economic Issues 27 (2d ed. 2010).

tion does not have antitrust consequences absent recoupment.[69] Courts make a distinction between injury to competitors and injury to competition, with only the latter being an antitrust concern.[70] For example, the majority in *Brooke Group* opined that even though "below-cost pricing may impose painful losses on its target," this "is of no moment to the antitrust laws if competition is not injured."[71] The injury to competition is decoupled from the elimination of competitors and is instead tethered to the probability of recoupment.[72] For example, the Tenth Circuit held that "[w]ithout a dangerous probability of recoupment, competition remains unharmed even if individual competitors suffer."[73] In short, the prevailing view is that in the absence of recoupment, predatory pricing "has no anticompetitive consequences."[74]

3. *Recoupment as Efficient Filter.* — The third justification for the recoupment requirement involves the administrability of antitrust rules. Like all elements of a cause of action, the recoupment requirement operates as a screen to distinguish beneficial or benign conduct from harmful conduct.[75] The supporters of the recoupment requirement argue that this element is particularly useful because it saves courts from having to examine other elements of a predatory pricing claim. According to this line of thinking, if the alleged predation seems unprofitable, then a ra-

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69. See, e.g., Wallace v. IBM, 467 F.3d 1104, 1106 (7th Cir. 2006) ("When exit does not occur, or recoupment is improbable even if some producers give up the market, there is no antitrust problem.").

70. See Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 488 (1977) ("[A]ntitrust laws . . . were enacted for 'the protection of *competition*, not *competitors* . . . .'" (quoting Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962))); see also Rebel Oil Co. v. Atl. Richfield Co., 51 F.3d 1421, 1433 (9th Cir. 1995) ("Though rivals may suffer financial losses or be eliminated as a result of the below-cost pricing, injury to rivals at this stage of the predatory scheme is of no concern to the antitrust laws.").

71. *Brooke Group*, 509 U.S. at 224.

72. See *Advo*, 51 F.3d at 1200 ("Predatory pricing schemes that fail at the recoupment stage may injure specific competitors . . . but do not injure competition (*i.e.* they do not injure consumers) and so produce no antitrust injury." (citing *Brunswick Corp.*, 429 U.S. at 487–90)).

73. United States v. AMR Corp., 335 F.3d 1109, 1115 (10th Cir. 2003); see also Kelly J. Fox, Note, *Brooke Group, Ltd. v. Brown & Williamson Tobacco Corp.*: Taking the Predator out of Predatory Pricing, 23 Cap. U. L. Rev. 581, 590 (1994) ("The recoupment analysis focuses upon the premise that no antitrust injury to competition occurs unless there exists a high likelihood that the alleged predatory firm will recoup the expenses and lost profits expended during the period of predation." (citing Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986))).

74. M. Steven Wagle, Predatory Pricing, A Case Study: *Matsushita Electric Industries Co. v. Zenith Radio Corporation* [sic], 22 Creighton L. Rev. 89, 119 (1988).

75. See 3A Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law ¶ 726a, at 57–58 (3d ed. 2008) ("[T]he substantive evil that antitrust reprehends is not the injury to rivals, but the subsequent injury to consumers. The recoupment requirement enables the tribunal to determine whether a particular price cut is calculated to injure only rivals, or consumers as well.").

tional firm would not have attempted it, so it must not have happened.[76] For example, in *Rose Acre*, Judge Easterbrook justified the recoupment requirement in large part as a way to avoid having to evaluate the pricing-below-cost element.[77] Judge Easterbrook asserted that if the only reason for a firm to engage in below-cost pricing is to recoup the investment later, then it must follow that if there is no likelihood of recoupment, the firm must not be pricing below cost.[78] Other courts have followed suit.[79]

Recoupment was not seen as merely another element, equal to all others. Instead, recoupment was elevated to a threshold element: The plaintiff's failure to prove probability of recoupment eliminated the need to consider either the appropriate measure of cost or whether the defendant actually priced below that measure.[80] This view was justified on the grounds that recoupment is an easier element to apply than the price-below-cost element.[81]

Courts and commentators also praise the recoupment requirement as a convenient filter to avoid all inquiries into intent in predatory pricing cases. Some jurisdictions treat predatory intent as an element of the

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76. See, e.g., Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc., 824 F.2d 582, 599 (8th Cir. 1987) ("Therefore, '[a]ccepting rational economic conduct as the standard for predation,' we assume that predatory conduct will be undertaken only when success is plausible." (alteration in *Lomar*) (quoting Henry v. Chloride, Inc., 809 F.2d 1334, 1345 (8th Cir. 1987))); Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2263 ("The recoupment requirement was designed to screen out cases where predation appeared unprofitable and hence irrational.").

77. See A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1401 (7th Cir. 1989) ("It is much easier to determine from the structure of the market that recoupment is improbable than it is to find the cost a particular producer experiences . . . . Market structure offers a way to cut the inquiry off at the pass . . . .").

78. Id.

79. See, e.g., Irvin Indus., Inc. v. Goodyear Aerospace Corp., 974 F.2d 241, 244 (2d Cir. 1992) ("Moreover, if the market structure renders recoupment of profits lost during the price cut phase difficult or risky, it may be unlikely that the seller's price cut is predatory.").

80. See 3A Areeda & Hovenkamp, supra note 75, ¶ 725b, at 50–51 ("Some have suggested that the recoupment requirement 'trumps' or takes precedence over the requirement of prices below cost . . . .").

81. See, e.g., Aaron S. Edlin & Joseph Farrell, The *American Airlines* Case: A Chance to Clarify Predation Policy, *in* The Antitrust Revolution: Economics, Competition, and Policy 502, 518 (John E. Kwoka, Jr. & Lawrence J. White eds., 4th ed. 2004) [hereinafter Antitrust Revolution, 4th ed.] ("Judge Frank Easterbrook suggested in *Rose Acre* . . . that sacrifice is not worth even looking for if recoupment seems very unlikely. He argues that it is often easier to see that market structure makes recoupment unlikely than to decide if there was a sacrifice."); Jessica L. Goldstein, Note, Single Firm Predatory Pricing in Antitrust Law: The *Rose Acre* Recoupment Test and the Search for an Appropriate Judicial Standard, 91 Colum. L. Rev. 1757, 1781 (1991) ("Judge Easterbrook, in supporting his use of recoupment ability as the appropriate judicial 'filter' for predatory pricing claims, asserts that determining whether recoupment is possible is easier than determining a business' costs.").

predatory pricing offense.[82] When the charge of predatory pricing is brought in the form of an attempted monopolization claim, the plaintiff must prove a specific intent to monopolize. Although many antitrust violations include some variation of an intent requirement, the intent element is nevertheless often disparaged as difficult to apply and interpret in the context of predatory pricing.[83] In *Rose Acre*, Judge Easterbrook argued that "unless recoupment lies in store even the most vicious intent is harmless to the competitive system."[84] Because recoupment is seen as the only way in which predatory pricing could inflict antitrust injury, any inquiry into predatory intent is considered superfluous and "irrelevant" if recoupment is unlikely.[85]

In short, the recoupment requirement lets courts avoid inquiries into both price and intent.[86] This is seen as increasing the efficiency of antitrust litigation. As one commentator explained, the recoupment element is "a filter to reduce the timely and expensive discovery and litigation associated with predatory pricing claims. If the recoupment analysis proves futile, there would be no need to inquire into the cost/price analysis or predatory intent of the parties, as these would not lead to competitive injury."[87]

82. See infra Part IV.A.3 (surveying jurisdictional variations on predatory intent element).

83. See, e.g., Morgan v. Ponder, 892 F.2d 1355, 1359 (8th Cir. 1989) (noting "futility in attempting to discern predatory conduct solely through evidence of a defendant's 'predatory intent'").

84. A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1401 (7th Cir. 1989).

85. Page I. Austin, Predatory Pricing Law Since *Matsushita*, 58 Antitrust L.J. 895, 899 (1990) ("If recoupment is impossible, then the defendant's state of mind also becomes irrelevant."); John B. Schulte, Note, Predatory Pricing: The Retreat from Subjective Intent Analysis and the Move Toward a Likelihood of Recoupment Inquiry, 24 Suffolk U. L. Rev. 975, 1007 (1990) ("Also, if recoupment is stressed at the outset, the need to search for intent, assuming arguendo intent was relevant, may become meaningless; if recoupment is impossible, intent is irrelevant."); William L. Worden, Case Note, Antitrust: Predatory Pricing, 40 Drake L. Rev. 657, 668 (1991) ("Making recoupment an initial hurdle avoids questions of cost and intent, because if a price below cost is lawful when it cannot lead to monopoly, then the defendant's intent is irrelevant."); see also supra Part I.B.2.b (discussing general assumption of no competitive harm absent recoupment).

86. Schulte, supra note 85, at 1007–08 ("Determining from the structural characteristics of the relevant market whether eventual recoupment is possible is easier to determine than either attaching significance to evidence of intent or discovering the pertinent product cost and price-cost relation for an alleged predator.").

87. Fox, supra note 73, at 604 (citing *Rose Acre*, 881 F.2d at 1400); see also Schulte, supra note 85, at 1007 ("Such an initial analysis will also shorten the time and reduce the complication of antitrust litigation.").

C. *Summary*

The importation of the recoupment requirement into predatory pricing law results from courts confusing the evidentiary standards for section 1 claims with the substantive elements of section 2 claims. The *Matsushita* Court explored recoupment in the context of section 1 litigation as evidence of whether the alleged conspiracy—to charge a predatory price—was plausible.[88] The Justices wrestled with the sole question of whether there was sufficient evidence of an agreement among the Japanese manufacturers.[89] In the context of section 1 concerted predatory pricing claims, if there is no likelihood of recoupment then courts are less likely to infer the existence of an agreement among competitors to engage in predatory pricing.[90] Unfortunately, subsequent courts applied the *Matsushita* standard for section 1 conspiracy cases to summary judgment motions in section 2 predatory pricing litigation.[91] This approach is flawed because section 2 predatory pricing claims are not predicated on the presence of an agreement. In order to prevail on a section 2 monopolization claim, the plaintiff need only show that the defendant has monopoly power in a relevant market and acquired (or maintained) that power through anticompetitive conduct.[92] Thus, while the likelihood of recoupment changes how much weight to give ambiguous evidence of an agreement in section 1 cases, this issue should be irrelevant in section 2 cases.

II. COURTS ROUTINELY ERR IN APPLYING THE RECOUPMENT REQUIREMENT

Courts often reject predatory pricing claims because the plaintiff failed to prove a probability of recoupment to the court's satisfaction.[93] Unfortunately, in many of these cases, the court incorrectly analyzed the issue of recoupment. This Part exposes mistakes that courts make and explores the myriad ways in which predators recoup their investments in below-cost pricing.

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88. Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 590–91 (1986) (treating perceived low likelihood of recoupment as evidence suggesting lack of conspiracy).

89. Id.

90. Id.

91. See, e.g., C.B. Trucking, Inc. v. Waste Mgmt., Inc., 944 F. Supp. 66, 69 (D. Mass. 1996) (granting summary judgment motion on predatory pricing claims based in part upon failure to meet "heightened pleading requirements of *Matsushita*").

92. United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966). Private plaintiffs must also show that they have suffered antitrust injury. See infra Part IV.A.4 (discussing causal antitrust injury).

93. See infra note 265 (discussing line of cases articulating necessity of "dangerous probability" of recoupment).

A. *Judicial Misperceptions in Analyzing Recoupment*

Judicial decisions finding no probability of recoupment are often riddled with unfounded assumptions and misunderstandings of how markets work. This section examines three mistakes that judges make in predatory pricing cases: assuming easy entry into markets; misunderstanding capital markets; and distorting the timing issues related to recoupment.

1. *Entry Assumptions.* — In applying the *Brooke Group* dicta that if entry is easy then recoupment is implausible,[94] lower courts are too quick to assume that market entry is, in fact, easy. For example, in *Stearns Airport Equipment Co. v. FMC Corp.*, the Fifth Circuit affirmed summary judgment against a predatory pricing plaintiff, reasoning that recoupment was unlikely because foreign suppliers could enter the market.[95] To reach this conclusion, the court derided the plaintiff because the "only specific barriers to foreign entry mentioned" were "transportation costs, manufacturing costs, and the demonstrated ability of the dominant firm to charge supracompetitive prices."[96] The court failed to recognize that these are—or suggest—barriers to entry. The court rejected transportation costs as a barrier to entry for foreign producers because domestic producers also face shipping costs.[97] The court dismissed "the historical lack of success foreign firms have had in the domestic market," which the plaintiff argued suggested the presence of entry barriers, as "irrelevant."[98] Furthermore, the court discounted the plaintiff's argument for failing to prove the existence of "*unusual* barriers to entry in the . . . [relevant] market."[99] The court never explained why a barrier to entry must be "unusual" in order to support the possibility of recoupment. The court ultimately reasoned that the antitrust plaintiff proved too much because "[n]ew entrants to a market will always face these kinds of entry costs."[100] In other words, according to the Fifth Circuit, because barriers to entry always exist, such barriers do not exist as a matter of antitrust law.

But ubiquity is not a reason to deny something's existence; rather, it is a reason to take it seriously. The court concluded that "it would not

94. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 226 (1993) ("[W]here new entry is easy . . . summary disposition of the case is appropriate.").

95. 170 F.3d 518, 536 (5th Cir. 1999).

96. Id. at 530 (internal quotation marks omitted).

97. Id. at 530–31. The court also noted that the defendant shipped its product abroad. Id. at 520.

98. Id. at 530; see also Avishalom Tor, The Fable of Entry: Bounded Rationality, Market Discipline, and Legal Policy, 101 Mich. L. Rev. 482, 554 (2002) (arguing courts should consider "lack of entrant penetration into the market, the absence of large-scale entry, and the absence of innovative entry" when evaluating ease of entry in predation cases).

99. *Stearns*, 170 F.3d at 531 (emphasis added).

100. Id.

seem unreasonable to assume" that entry would occur once the defendant began to raise price in the post-predation period.[101] This is completely inappropriate because at the summary judgment stage all evidence, including that relating to the existence of barriers to entry, should be read in favor of the nonmovant, the antitrust plaintiff. In essence, the Fifth Circuit simply assumed away the probability of recoupment. Courts assume that if entry appears easy, then any attempt at recoupment is "doomed to failure."[102] For example, in *Advo*, the Third Circuit declared that it would be easy to enter the market for assembling and distributing advertising circulars.[103] The Third Circuit asserted that "[a]ny attempt to earn back the foregone profits by charging monopoly prices on distribution of circular advertising . . . merely will lead to a wave of new entrants who will drive prices down to competitive levels."[104] But the facts showed that Advo charged a monopoly price for years before entry occurred.[105] Thus, while entry was theoretically easy, it was actually more complicated.

Some commentators argue that recoupment is unlikely because rivals who exit the market in response to below-cost pricing will reenter when the monopolist raises price in the post-predation period.[106] There are, however, many markets which, once exited, are relatively difficult to reenter. For example, reentry did not occur in the airline industry when a dominant carrier raised price after defeating an upstart airline with predatory pricing.[107] Similarly, grocery stores driven from the market in response to predatory pricing would have to incur significant costs in order to reopen, including "the cost of rehiring employees or rebuilding the loyalty of angry customers."[108] In many industries, "[s]alvaged equipment, dispersed labor force and management, discontinued advertising, and unmaintained reputation can only be replaced or re-adapted to their

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101. Id.

102. Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1200 (3d Cir. 1995).

103. Id. ("The inputs required are readily available: a small cadre of experienced managers; a sales force; computerized address lists available from a variety of vendors; and a large number of low-skill employees to stuff circulars into packets, and then either to stuff them into newspapers or hang them on doorknobs.").

104. Id. at 1203 (citation omitted).

105. Id. at 1201.

106. See, e.g., Bork, Paradox, supra note 20, at 151–52 (discussing possibility of predation victim avoiding losses by closing operations until reentry is feasible); Frank H. Easterbrook, The Limits of Antitrust, 63 Tex. L. Rev. 1, 27 (1984) (discussing likelihood of competition from "resurgent firms"); McGee, *Standard Oil*, supra note 20, at 140 (asserting possibility of reentry).

107. See Paul Stephen Dempsey, Predatory Practices & Monopolization in the Airline Industry: A Case Study of Minneapolis/St. Paul, 29 Transp. L.J. 129, 159–60 (2002) (discussing Northwest Airlines's predatory dominance in Minneapolis/St. Paul market and absence of reentry by airlines chased out of market).

108. Richard Craswell & Mark R. Fratrik, Predatory Pricing Theory Applied: The Case of Supermarkets vs. Warehouse Stores, 36 Case W. Res. L. Rev. 1, 33 (1985).

former uses at substantial costs. Such costs constitute re-entry barriers."[109] In short, reentry is not as easy as some courts would make it out to be.

Even when entry (or reentry) seems theoretically easy, it may not occur for several reasons. First, the higher post-predation price need not necessarily induce entry because the successful predator can employ limit pricing. Limit pricing refers to setting "price at a level just below that which a prospective entrant to the market would need to charge in order to sustain a successful entry."[110] In theory, the supracompetitive price can be set at a level that allows recoupment to occur at a reasonable pace without provoking entry, which would drive the price down.[111] In this manner, a dominant firm may use predatory pricing to drive out a competitor and charge a supracompetitive price that is too small to attract new entrants, yet high enough to recoup its losses and then some.

Second, monopoly prices need not attract entry. Even if a monopoly price would allow a new entrant to recover the start-up costs, the would-be entrant could calculate that its entry into the market would depress the price and its actual rate of return would be insufficient to recover its entry costs in a timely manner.[112] Consequently, a dominant firm could charge a monopoly price without inviting entry if potential entrants believed that the price would fall upon their entry and that that lower price would make entry insufficiently profitable.

Finally, even if entry does occur, it need not prevent recoupment. For example, the entry may be too small to compel the dominant firm to reduce price.[113] Professor Avishalom Tor has argued that "mere evidence of entry should not be sufficient to reject predatory pricing claims out of hand. Instead, the courts should focus on the success of entrants in penetrating the market as a better indicator of the short-term competitive threat such entrants pose for allegedly predatory incumbents."[114] A new entrant may enjoy the price umbrella created by the monopolist, taking a small slice of the market while also charging the monopoly price. This

109. Wagle, supra note 74, at 96 (citing Janusz A. Ordover & Robert D. Willig, An Economic Definition of Predation: Pricing and Product Innovation, 91 Yale L.J. 8, 11–12 (1981)).

110. Phototron Corp. v. Eastman Kodak Co., 842 F.2d 95, 101 (5th Cir. 1988).

111. See Carstensen, supra note 53, at 962–63 (showing how more "modest" markup during recoupment phase of predatory pricing "may make new entry far less attractive given the significant short-run costs that any new competition would have to incur").

112. See, e.g., Kelco Disposal, Inc. v. Browning-Ferris Indus., 845 F.2d 404, 408 (2d Cir. 1988) (noting low rate of return could lead firms to "think twice" about reentry despite relative ease of reentry), aff'd, 492 U.S. 257 (1989).

113. See Tor, supra note 98, at 559 n.319 (describing FTC v. Cardinal Health, Inc., 12 F. Supp. 2d 34, 54–58 (D.D.C. 1998), as case finding "where larger-scale entry was unlikely to occur within the time frame set by the guideline, the existing potential for expansion by small 'fringe' firms was not sufficient to achieve the required impact on price").

114. Id. at 553 (emphasis omitted).

would reduce the monopolist's revenue, but not dramatically so, and possibly not enough to prevent recoupment.

2. *Courts Misunderstand Capital Markets.* — Some courts and commentators argue that recoupment is improbable because the targets of price predation can readily secure financing to withstand the below-cost pricing during the predation period or to reenter the market during the recoupment period.[115] They argue that the targets of price predation can receive financing to compete against deep-pocketed predators.[116]

Capital markets, however, are imperfect.[117] Venture capitalists may avoid markets dominated by a price predator.[118] Price predation can deplete the target's funds available to meet loan commitments.[119] Banks and venture capitalists may be unable to determine whether the target is suffering losses due to temporary predation or more durable inefficiencies.[120] Either way, predation can discourage financing by creating uncertainty.[121] Indeed, some predators intend to send a message to their rivals'

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115. See, e.g., W. Parcel Express v. UPS, 65 F. Supp. 2d 1052, 1062 (N.D. Cal. 1998) (finding capital costs not barrier to entry in predatory pricing case); AD/SAT, a Div. of Skylight, Inc. v. Assoc. Press, 920 F. Supp. 1287, 1304 (S.D.N.Y. 1996) (holding "cost of capital should not be considered in determining whether [defendant] has priced below average variable cost"); Caller-Times Publ'g Co. v. Triad Commc'ns, Inc., 826 S.W.2d 576, 593 n.24 (Tex. 1992) (Doggett, J., dissenting) (criticizing majority for failing to recognize imperfections in capital markets and "lack of available credit arguably could serve as a barrier to entry"); see also Keith N. Hylton, Antitrust Law: Economic Theory and Common Law Evolution 223 (2003) ("If it is clear that in terms of economic fundamentals, the rival can compete against the monopolist, then the rival should be able to borrow funds that would allow it to withstand a lengthy predatory campaign."); James A. Dalton & Louis Esposito, Predatory Price Cutting and *Standard Oil*: A Re-examination of the Trial Record, 22 Res. L. & Econ. 155, 158 (2007) [hereinafter Dalton & Esposito, Re-examination] (noting McGee's argument that capital markets would supply "efficient prey" with necessary funds to withstand predation).

116. See George A. Hay, The Economics of Predatory Pricing, 51 Antitrust L.J. 361, 363–64 (1982).

117. See Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2286 (explaining capital market imperfections); see also Richard T. Rapp, Predatory Pricing Analysis: A Practical Synthesis, 59 Antitrust L.J. 595, 597–98 (1991) (explaining relevance of capital market imperfections to market dominance).

118. See Carstensen, supra note 53, at 966 (arguing venture capitalists will not enter market "unless the potential reward is great enough to outweigh additional risk" presented by predator).

119. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2287.

120. See id. at 2248 ("[B]anks observe the [fall in profits], but cannot tell whether it is caused by predation or inefficient performance . . . ."); see also John E. Kwoka, Jr. & Lawrence J. White, The Economic and Legal Context, *in* Antitrust Revolution, 4th ed., supra note 81, at 172, 181 [hereinafter Kwoka & White, Economic and Legal Context] (arguing many instances of alleged predation are simply hard competition from stronger firms).

121. See Brodley & Hay, supra note 57, at 746 n.15 ("Financers do not know with certainty if the new entrant will progress down the textbook curve that illustrates declining costs as cumulative output increases. Thus, they may balk at underwriting large short run

bankers not to fund them.[122] Furthermore, even if the target has access to capital, the losses imposed by predation may cause lenders to charge a premium.[123] The losses inflicted by price predation cause lenders to tighten their terms,[124] hobbling the rival's ability to compete on the merits. Insufficient access to outside capital can deny a target the means to withstand predation, even if it has the will.[125] Despite the widespread academic awareness of capital market imperfection, courts do not consider the issue when asserting that targets can get money to survive predation or to reenter the market later.[126]

3. *Courts Confuse Timing Issues.* — Courts have made the recoupment requirement too difficult to satisfy by improperly analyzing the issue of duration. By assuming that the length of both the predation and the recoupment periods must be substantial,[127] courts put plaintiffs in an impossible bind. Courts require predatory pricing plaintiffs to prove that "'the extent and duration of the alleged predation'" were sufficient to drive all rivals from the market.[128] If the extent of predation is relatively little, then courts hold that recoupment is "impossible" because a low

losses."); James A. Dalton & Louis Esposito, *Standard Oil* and Predatory Pricing: Myth Paralleling Fact, 38 Rev. Indus. Org. 245, 251 (2011) ("Uncertainty about the costs of the potential entrant relative to the dominant firm as well as uncertainty about the incumbent firm's reaction to entry diminishes the resolve of the potential entrant, as well as the willingness of the capital markets to supply funds.").

122. See Patrick Bolton, Joseph F. Brodley & Michael H. Riordan, Predatory Pricing: Response to Critique and Further Elaboration, 89 Geo. L.J. 2495, 2509 (2001) [hereinafter Bolton, Brodley & Riordan, Response] (discussing example of Sacramento cable market).

123. See Kwoka & White, Economic and Legal Context, supra note 120, at 181 (noting lenders charge premiums to smaller firms because of favoritism toward larger firms, or because larger firms disrupt smaller rivals' business prospects).

124. See Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2287 ("Finally, lower earnings may cause lenders to believe wrongly that the firm's profits are likely to be lower or riskier in the future and therefore to stiffen their lending terms.").

125. See Jonathan B. Baker, Predatory Pricing After *Brooke Group*: An Economic Perspective, 62 Antitrust L.J. 585, 591 n.27 (1994) (arguing predator has advantage in price war when target lacks access to capital).

126. See id. at 597 ("Although it was obliged to interpret the record in the light most favorable to Liggett, the [*Brooke Group*] Court did not investigate the possibility of a capital market imperfection hobbling Liggett's access to financing relative to that of Brown & Williamson.").

127. See, e.g., Vollrath Co. v. Sammi Corp., 9 F.3d 1455, 1460 (9th Cir. 1993) ("[I]n order for the business entity to eliminate competition by pricing below cost, it must forego short-term profits long enough to drive competitors from the market and then maintain monopoly power long enough to recoup the losses and realize additional gain.").

128. Stearns Airport Equip. Co. v. FMC Corp., 170 F.3d 518, 529 (5th Cir. 1999) (quoting Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 225 (1993)).

amount of below-cost pricing will be insufficient to drive competitors from the market.[129]

In addition to requiring a lengthy period of predation, courts assume that the duration of recoupment must be similar to the duration of predation. For example, in *Matsushita*, the Supreme Court opined that "because the alleged losses have accrued over the course of two decades, the conspirators could well require a correspondingly long time to recoup."[130] The Court then concluded that recoupment was too improbable because it would take too long.[131] The Court's duration assumption is flawed. The monopoly profit margin in the recoupment period may often be higher than the loss margin during the predation period. For example, after Northwest Airlines drove its rival, Kiwi International Airlines, from the market by matching the upstart's $69 fare on the Minneapolis-Detroit route, Northwest Airlines raised its fares to $467.[132] Similarly, a predator could reduce prices by ten percent below cost during the predation phase and then charge a monopoly price that is 400 percent above cost during the recoupment phase. If that were to happen, recoupment would take significantly less time than predation.

Courts have essentially created a Catch-22 regarding the duration of predation in which the antitrust plaintiff simply cannot succeed. If the predation lasts for a relatively short time, then the court will conclude that there is no exclusionary effect; if the predation lasts for a relatively long time, then the court will conclude that the predator cannot recoup as a matter of law.[133] In theory, there is a sweet spot in which the duration

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129. See Taylor Publ'g Co. v. Jostens, Inc., 216 F.3d 465, 478–79 (5th Cir. 2000) (finding insufficient predation when only two-fifths of one percent of customers were lost over two-year period); *Stearns*, 170 F.3d at 529 (holding underpricing in five bids over four-year period would not eliminate competitors from market); see also Denger & Herfort, supra note 52, at 552 ("[I]f challenged below-cost pricing is not sustained long enough to exclude or drive rivals out of the market or alter their pricing behavior appreciably, then it is not likely to create the type of competitive dangers that the prohibition against predatory pricing was designed to avert.").

130. Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 592 (1986).

131. See id. at 592–93 ("If the losses have been substantial—as would likely be necessary in order to drive out the competition—petitioners would most likely have to sustain their cartel for years simply to break even." (footnote omitted)).

132. Dempsey, supra note 107, at 159.

133. See William H. Jordan, Comment, Predatory Pricing After *Brooke Group*: The Problem of State "Sales Below Cost" Statutes, 44 Emory L.J. 267, 299 (1995) ("If the below-cost pricing is merely a short-term promotion, then it cannot drive competitors from the market. On the other hand, a firm which prices its products below cost for an extended period of time may never be able to recoup its losses . . . ."). The Court created a bind where there is no duration of below-cost pricing that leads to antitrust liability:

> The Court also failed to address how long predatory pricing must exist for it to be actionable. If the below-cost pricing is merely a short-term promotion, then it cannot drive competitors from the market. On the other hand, a firm which prices its products below cost for an extended period of time may never be able to recoup its losses even if it should succeed in driving its rivals from the market.

of predation is neither too short nor too long and recoupment is hence possible, but the courts have given no indication of where this middle ground resides.[134]

B. *Courts Fail to Appreciate How Recoupment Actually Occurs*

Courts are quick to dismiss the probability of recoupment because they look for recoupment through a narrow lens and often not in the correct places. Because static analysis of the recoupment issue leads to false conclusions of no recoupment,[135] this section employs dynamic analysis to demonstrate how predators recoup their investments in below-cost pricing. While most observers may agree that the ability to recoup makes predatory pricing rational,[136] not everyone recognizes the many forms that recoupment may take.

1. *Recoupment in Another Product Market.* — In rejecting predatory pricing claims, some courts either assert or assume that any recoupment must take place in the specific market in which the below-cost pricing occurred.[137] Courts apparently do not appreciate the prospect of recoupment in another market.[138] The source of this misconception may reside

Id.

134. For example, the Fifth Circuit rejected a predatory pricing claim because it was "unlikely that [the defendant] would be able to control prices for any meaningful period, because other competitors easily c[ould] enter the market," but the court did not attempt to define this "meaningful period." C.A.T. Indus. Disposal, Inc. v. Browning-Ferris Indus., Inc., 884 F.2d 209, 211 (5th Cir. 1989) (per curiam).

135. See Louis Kaplow, Extension of Monopoly Power Through Leverage, 85 Colum. L. Rev. 515, 527–28 (1985) ("Static analysis—determining whether the firm profited immediately by its price cut—would produce the misleading conclusion that predation was never profitable. One could only discover the potential profitability of this strategy by taking into account the dynamic effect on the firm's market position.").

136. See, e.g., Baker, supra note 125, at 593–99 (noting Chicago and post-Chicago schools "differ on the plausibility of certain potential mechanisms for recoupment, not on the necessity of recoupment").

137. See, e.g., Clark v. Flow Measurement, Inc., 948 F. Supp. 519, 526 (D.S.C. 1996) (finding relevant market for Sherman Act analysis to be monopolized market); Edlin & Farrell, supra note 81, at 519 (noting court in airline price predation case "was reluctant to consider recoupment in other markets"); see also McGahee v. N. Propane Gas Co., 858 F.2d 1487, 1498 (11th Cir. 1988) (discussing requirement that business "'must . . . recoup its losses in the particular communities where their commodities are sold below cost . . . by raising the price of the same class of commodities'" (quoting S. Rep. No. 63-698, at 3 (1914))).

138. See 3A Areeda & Hovenkamp, supra note 75, ¶ 724, at 39 ("There may be cases where a predator who makes more than one product or operates in more than one region selects only one for below-cost pricing but reaps recoupment benefits in all. . . . The courts have not dealt adequately with this problem."); Trujillo, supra note 9, at 825 ("The . . . recoupment analysis in *Matsushita*, *Cargill*, and *Brooke* refers to recoupment only in the market in which the predation actually occurs. Thus, the Court's analyses and test . . . ignore the possibility that successful predation could occur because the dominant firm can spread its gains from predation over several markets." (footnote omitted)).

in the Chicago School's assumption that if recoupment cannot happen in a single-product market, then it necessarily cannot occur in a multi-product scenario.[139] This section explains how recoupment can happen in markets for complements, substitutes, and replacement goods.

a. *Recoupment in Complementary Product Market.* — Recoupment can take place in a complementary product market. If a firm sells two complementary products, *A* and *B*, and has market power in *B*, but not *A*, it may profitably engage in predatory pricing in *A* while recouping in the market for *B*. In complementary product markets, a reduction in the price of one good will generally increase demand for the other.[140] If the firm is charging a supracompetitive price for product *B*, then an increase in demand for *B* will increase the firm's profits. The firm can accomplish this by charging a below-cost price for product *A*, which has the effect of potentially vanquishing other suppliers of *A* while increasing the profits earned in the market for *B*. In this manner, the predatory pricing in *A* can be both exclusionary and cost-effective.[141]

Recoupment can also happen in a product market in which predation has not occurred when a firm monopolizes one market, but makes its profits in another market. The *Microsoft* case provides an example of this dynamic.[142] Microsoft possessed monopoly power over operating systems, but worried that browser technology (namely, Netscape's Navigator browser) might evolve in a manner that would make consumers and application developers less dependent on Microsoft's operating system.[143] Microsoft created its own browser, Internet Explorer (IE), and sought to dominate the browser market in order to prevent browser technology from advancing and undermining Microsoft's monopoly over operating systems.[144]

139. See McGee, Revisited, supra note 20, at 326 ("I said very little about multiple-product firms. If we cannot get the principles straight for single-product firms, there is no sense in going further.").

140. If consumers are willing to pay $100 for the bundle of *A* and *B* when each costs $50, then if the price of *A* declines to $45, consumers should be willing to pay $55 for *B*.

141. See Edlin & Farrell, supra note 81, at 509 (observing "'sacrifice' in one product can be immediately recouped (often quite legitimately) because it boosts profits in a complementary product").

142. United States v. Microsoft Corp., 253 F.3d 34, 68 (D.C. Cir. 2001) (per curiam) (describing government's argument that Microsoft priced Internet browser below cost to preserve monopoly on operating systems).

143. See United States v. Microsoft Corp., 84 F. Supp. 2d 9, 29 (D.D.C. 1999) (discussing Microsoft's fear that Netscape's success in browser market could enable development of alternative platform for applications development), rev'd in part, 253 F.3d 34.

144. Id. at 43.

Microsoft's conduct can be seen as a form of predatory pricing.[145] Microsoft's development and marketing of IE cost Microsoft well over $100 million per year, but Microsoft gave away this product for free.[146] Microsoft itself referred to its browser as a "no-revenue product."[147] Giving away a product for free constitutes predatory pricing under any reasonable definition of "appropriate measure of cost."[148] Even Robert Bork—not generally a friend of antitrust plaintiffs—described Microsoft's conduct as a species of predatory pricing.[149]

Microsoft did not recoup in the market in which the predation occurred—browsers—but it did recoup elsewhere. Microsoft had no intention of earning profits in the browser market.[150] Microsoft's goal was to stop Netscape from encroaching upon the operating systems market.[151] Microsoft engaged in below-cost pricing in order to—in its own words—"cut off Netscape's air supply."[152] By engaging in predatory pricing in browsers, Microsoft succeeded in driving Netscape from the market and eliminated the threat that browser technology posed to Microsoft's monopoly on operating systems.[153] As Robert Bork explained,

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145. The D.C. Circuit did not evaluate *Microsoft* as a predatory pricing case. 253 F.3d at 68 (declining to consider liability for predatory pricing because plaintiffs did not press issue on appeal). The facts of the case, however, illustrate how recoupment from below-cost pricing can occur in adjacent markets. See *Microsoft*, 84 F. Supp. 2d at 28 (stating Microsoft "operated to reinforce monopoly power" in the operating system market by entering the browser market).

146. Daniel L. Rubinfeld, Maintenance of Monopoly: *U.S. v. Microsoft*, *in* Antitrust Revolution, 4th ed., supra note 81, at 476, 489.

147. Id.

148. See Am. Bar Ass'n Section of Antitrust Law, Handbook on the Antitrust Aspects of Standards Setting 87 (2004) ("In the standard-setting context, a number of commentators have suggested that, by bundling its browser product (Internet Explorer) with its operating system product, Microsoft essentially 'gave its browser away for free' and thereby engaged in predatory pricing." (quoting Steven C. Salop & R. Craig Romaine, Preserving Monopoly: Economic Analysis, Legal Standards, and Microsoft, 7 Geo. Mason L. Rev. 617, 638–39 (1999)) (citing Thomas A. Piraino, Jr., Identifying Monopolists' Illegal Conduct Under the Sherman Act, 75 N.Y.U. L. Rev. 809, 873–74 (2000))).

149. See Robert Bork, High-Stakes Antitrust: The Last Hurrah?, *in* High-Stakes Antitrust 45, 54 (Robert W. Hahn ed., 2003) [hereinafter Bork, Last Hurrah] ("Microsoft's campaign resembled price-cutting predation in that it gave price and other concessions (translatable into price) to those vendors it demanded stop dealing with Netscape and Sun, and it also had to increase its output of browsers and JVMs [Java Virtual Machines].").

150. See Rubinfeld, supra note 146, at 490 ("[T]he Government introduced . . . documents showing that [Microsoft's] zero (or negative) price for its browser was not considered a way to earn competitive ancillary revenues.").

151. Bork, Last Hurrah, supra note 149, at 50 (noting Steve Ballmer of Microsoft stated Microsoft had to expand into "Netscape's territory lest Netscape encroach on [its] operating systems territory").

152. Rubinfeld, supra note 146, at 489–90 (quoting deposition testimony of witness Steven McGeady) (internal quotation marks omitted).

153. Bork, Last Hurrah, supra note 149, at 50–51.

> Microsoft was defending monopoly profits that made the expense of predation worthwhile. Even after the sacrificed fixed costs of developing the Internet Explorer, the company was earning supracompetitive returns on the monopoly it was defending, while Netscape, forced to distribute its Navigator free, had no income in that market to cover its fixed costs. Understandably, Netscape gave up a contest it could not win.[154]

In sum, Microsoft's losses in the browser market were recouped in the market for operating systems.[155] This example shows how a firm may engage in predatory pricing in one market in order to sustain a profitable monopoly in another market.[156] If courts focus exclusively on the market in which the price predation occurred, they may fail to detect the recoupment.

b. *Recoupment in Substitute Product Market.* — Recoupment can also take place in the market for a substitute product. For example, in *Brooke Group*, the cigarette manufacturer Liggett had sued its rival (B&W) for predatory pricing in the market for generic cigarettes. According to Liggett's theory of the case, Liggett had sold low-priced generic cigarettes, which reduced the ability of makers of branded cigarettes to raise their prices. As a result, B&W suffered significant decreases in its profits. B&W needed to slow the sales growth of—and increase the price of—generic cigarettes in order to slow or reverse its decline in profits for branded cigarettes.[157] In response to the threat posed by Liggett's low-

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154. Id. at 55.

155. See Rubinfeld, supra note 146, at 490 ("From the Government's perspective, the preservation of Microsoft's OS monopoly alone would permit recoupment."); Steven C. Salop & R. Craig Romaine, Preserving Monopoly: Economic Analysis, Legal Standards, and Microsoft, 7 Geo. Mason L. Rev. 617, 639 (1999) (discussing plausibility of recoupment for Microsoft).

156. Network effects also played a role in the recoupment strategy. Network effects can reinforce a monopoly but cannot protect it forever. In this instance, Microsoft had monopoly power over the market for operating systems, secured in part through the network effects. United States v. Microsoft Corp., 253 F.3d 34, 49 (D.C. Cir. 2001) (per curiam). The network effects alone were insufficient to guarantee Microsoft's monopoly position. So it engaged in a series of anticompetitive acts in order to undermine firms and products that represented potential long-term threats to Microsoft's operating system. The network effects, in turn, facilitated recoupment. See Salop & Romaine, supra note 155, at 639 (describing how network effects could make price predation profitable for Microsoft); see also Mark A. Lemley & David McGowan, Could Java Change Everything? The Competitive Propriety of a Proprietary Standard, 43 Antitrust Bull. 715, 725 (1998) (noting investments in predation are more likely to be recouped in market with network effects). In short, the *Microsoft* case shows how a dominant firm in a market that exhibits network effects may engage in predatory pricing in order to prevent a rival's (superior) product from becoming the industry standard.

157. Brief for the Petitioner, Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993) (No. 92-466), 1992 WL 541265, at *17 ("Its unilateral investment in below-average-variable-cost pricing turned out to be $14.9 million, which is far less than the $350 million that it estimated it would forego by 1988 unless the growth of generics were slowed down." (citation omitted)).

priced generics, B&W entered the market for generic cigarettes and priced below cost, while tacitly communicating the message to Liggett that if Liggett would raise the prices of its generic cigarettes, so would B&W.[158] If Liggett succumbed to this pressure, B&W—along with the other tobacco firms—would be able to raise the price of branded cigarettes.[159] According to Liggett, B&W would recoup its losses from the generic cigarette market in the oligopolized market for branded cigarettes.[160] Thus, while the predation happens in one market (generic cigarettes), the recoupment takes place in another (branded cigarettes).[161]

In their argument to the Supreme Court, the defendants in *Brooke Group* tried to focus the Court's attention on the market for generic cigarettes, instead of the market for branded cigarettes where the true profits from the alleged predatory pricing scheme occurred.[162] Their strategy worked. The Supreme Court did not appreciate how recoupment can happen in another market.[163] The Court affirmed reversal of a jury verdict in Liggett's favor despite the fact that Liggett did, in fact, raise its prices as B&W had dictated.[164] Even after B&W's entry into the generics market increased the percentage of the overall cigarette market belonging to generics, the average price of all cigarette sales increased significantly post-predation.[165] This allowed B&W to recoup its losses in generic cigarettes through supracompetitive pricing in branded cigarettes.[166]

Brooke Group illustrates the principle that recoupment can take place in the market for higher-priced substitutes. Ultimately, the Supreme Court failed to recognize this possibility despite the fact that there is no legal reason the predicted recoupment must take place in the precise

158. See supra notes 31–49 and accompanying text (discussing *Brooke Group*).

159. See supra notes 31–49 and accompanying text.

160. See supra notes 31–49 and accompanying text.

161. Although I have characterized the recoupment as taking place in another market, the parties in *Brooke Group* stipulated that branded and generic cigarettes were segments of one market for cigarettes, not separate markets. Baker, supra note 125, at 595.

162. Respondent's Brief on the Merits, *Brooke Group*, 509 U.S. 209 (No. 92-466), 1993 WL 445371, at *18–*20.

163. See Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2258 ("In *Brooke*, the Court omitted from its analysis any consideration of strategic factors such as possible gains from . . . other cigarette markets . . . .").

164. Professor Areeda noted that Liggett indeed raised prices in his argument before the Court. See Oral Argument at 10:56, *Brooke Group*, 509 U.S. 209 (No. 92-466), available at http://www.oyez.org/cases/1990-1999/1992/1992_92_466#argument (on file with the *Columbia Law Review*) ("[T]he losses, as B&W predicted, induced Liggett to raise its consumer prices, its list prices.").

165. See id. at 15:27 ("[F]rom the date when B&W entered the . . . generic business, to the close . . . of the record, the price of regular-brand cigarettes rose 67 percent[] [and] [t]he price of all generics rose 74 percent.").

166. Id. at 12:25 ("[P]rices are supracompetitive. And the maintenance of those supracompetitive prices on regular-brand product, was, in fact, the object of the predatory scheme.").

market in which the below-cost pricing occurred.[167]

c. *Recoupment in Replacement Product Markets.* — Courts also fail to appreciate how recoupment for a predatory-pricing scheme can occur in the market for replacement goods. In this variation of predatory pricing, the monopolist charges a price below cost for original equipment, but charges a supracompetitive price for replacement or additional items. As a result, the losses from early predatory sales are recouped through high-priced subsequent sales.

The market for spark plugs illustrates this strategy. In *Stitt Spark Plug Co. v. Champion Spark Plug Co.*, the plaintiff brought a predatory pricing claim, arguing that the dominant firm in the market for spark plugs sold its product below cost in the original-equipment market in order to create brand name recognition that it could exploit in the market for replacement spark plugs.[168] The plaintiff explained that by monopolizing the market for spark plugs used in original equipment (i.e., in new cars), the dominant spark plug manufacturer—Champion—could manipulate consumer preference in the market for replacements.[169] Although the products Champion sold in the original equipment and replacement markets were identical, Champion could and did sell those identical spark plugs for a higher price in the replacement market.[170] The Supreme Court had recognized this dynamic in the spark plug market in *Ford Motor Co. v. United States*, when it observed that spark plug makers

> furnished the auto manufacturers with OE [original equipment] plugs at cost or less, about six cents a plug, and they continued to sell at that price even when their costs increased threefold. The independents sought to recover their losses on OE sales by profitable sales in the *aftermarket* where the requirement of each vehicle during its lifetime is about five replacement plug sets. By custom and practice among mechanics, the *aftermarket* plug is usually the same brand as the OE plug.[171]

Employing this strategy, Champion could take losses in the primary market, knowing it could recoup these losses in the replacement market.[172] The Fifth Circuit in *Stitt Spark Plug* improperly rejected the preda-

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167. See Edlin & Farrell, supra note 81, at 519 (noting none of the "reasons for a recoupment test suggests that recoupment must be in the same antitrust market as the sacrifice").

168. 840 F.2d 1253 (5th Cir. 1988).

169. Id. at 1254–55 ("[E]ngine owners tend to purchase replacement plugs of the same brand as the plugs that came with the engine originally.").

170. Id. at 1255 ("Champion sells spark plugs to original equipment manufacturers at prices well below the price of replacement plugs . . . .").

171. 405 U.S. 562, 565 (1972); see also *Stitt Spark Plug*, 840 F.2d at 1256 ("Champion is accused of cutting prices in one market—original equipment—in order to capture concurrent gains in another market—replacement equipment.").

172. See Joel B. Dirlam & Alfred E. Kahn, Fair Competition: The Law and Economics of Antitrust Policy 144, 217–18 (1954) (discussing below-cost pricing in spark plugs).

tory pricing claim by defining the two markets—originals and replacements—as one market in which no predation had occurred. The court held, "When Champion sets the prices for original-equipment plugs, the expected return includes not only the price paid by the original-equipment manufacturer, but also the replacement purchases that probably will follow. Hence, any meaningful comparison of price and cost must encompass Champion's sales to both markets."[173] In other words, because Champion was recouping in the second replacement market, it must not have been pricing predatorily in the original-equipment market.[174]

The Fifth Circuit created a Catch-22 that makes predatory pricing claims impossible to prove. Under the court's approach, because Champion was recouping its investment in below-cost pricing, it was not engaging in predatory pricing. Conversely, if Champion were not recouping its investment in below-cost pricing, *Brooke Group* holds that Champion did not engage in illegal predatory pricing. The recoupment requirement here operates to prevent all claims of price predation. Here, a monopolist was utilizing below-cost pricing in order to maintain its dominant market position for reasons unrelated to efficiency. This would seem to be quintessential monopoly conduct.[175] Yet *Stitt Spark Plug* illustrates the phenomenon that if there is recoupment, as a matter of law there is no predatory pricing.

Courts have applied this same analysis to predatory pricing of equipment, coupled with supracompetitive pricing of spare parts. For example, in *Kentmaster Manufacturing Co. v. Jarvis Products Corp.*, the defendant allegedly maintained its eighty percent market share in slaughterhouse equipment by providing it at little or no cost to customers, while charging highly profitable prices for spare and replacement parts.[176] Like the *Stitt Spark Plug* court, the Ninth Circuit in *Kentmaster* reasoned that the predatorily priced equipment and profitably priced spare parts "necessarily constitute a single product."[177] The Ninth Circuit

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173. *Stitt Spark Plug*, 840 F.2d at 1256.

174. It should be entirely irrelevant whether Champion was engaging in predatory pricing in both markets. It should be enough that it was engaging in predatory pricing in one market and recouping in another.

175. It may be tempting to argue that challengers could copy Champion's strategy of below-cost pricing on the original equipment followed by supracompetitive pricing on replacements. See *Stitt Spark Plug*, 840 F.2d at 1256 ("No action of Champion prevented Stitt from also pricing its product to original-equipment manufacturers with an expectation of return from the replacement market."); Dirlam & Kahn, supra note 172, at 219 (suggesting new entrants into markets could emulate practice of using below-cost pricing for original-equipment market and recoup losses in other markets). However, the entrant would have to be able to sustain losses for years until consumers needed replacements. This waiting period constitutes a barrier to entry unrelated to efficiency or product quality.

176. 146 F.3d 691, 693 (9th Cir. 1998), amended by 164 F.3d 1243 (9th Cir. 1999).

177. Id. at 695.

held that the plaintiff's theory of recoupment "is a straightforward admission that the total price of the single unit, [equipment plus spare parts], is not predatory."[178] Ultimately, the Ninth Circuit affirmed summary judgment for the defendant on the predatory pricing claim by discounting the initial predatory sale of equipment and using the fact of recoupment—a necessary element of a predatory pricing claim—to hold that no predation occurred.[179]

The Sixth Circuit employed similar reasoning for cases in which an initial product or service is given away for free. Ohio Bell Telephone Company published a telephone directory (the "white pages") and through its subsidiary, Ameritech Publishing, Inc. (API), also sold telephone listings for business directories (the "yellow pages"). Ohio Bell and API entered into a contract that required API to offer one yellow-page listing free to each business telephone subscriber and provided for simultaneous delivery of the white pages and the yellow pages to the subscriber. The plaintiff, Directory Sales Management Corporation (DSM), sold a competing business directory. DSM alleged that Ohio Bell was engaging in predatory pricing by giving away one yellow-page listing for free and recouping that loss by charging a supracompetitive price for additional listings in its yellow pages. The Sixth Circuit rejected the predatory pricing claim reasoning that because API "has never sold first listings," it did "not compete in the sale of first listings."[180] The court reasoned, "Predatory pricing requires that the Defendants sell a product at a price below cost. . . . The fallacy in DSM's argument is that the Defendants do not sell first listings, they sell subsequent listings."[181] This sets up a paradox: If below-cost sales are priced so low that the product is free, then there is no sale, and predatory pricing is not implicated. The court missed the point: DSM would have liked to sell so-called "first listings" but could not enter this market because its primary competitor was giving the product away. The defendants' strategy of pricing the first listing below cost was profitable because that first free listing locked in customers by creating path dependence, including coordinated billing and delivery of all directories, and the defendant could recoup its investment through sales of subsequent high-priced listings.[182]

178. Id. at 694.

179. Id. at 696 (Pregerson, J., dissenting) ("Here, the initial 'sale' took place when Jarvis delivered its equipment to Kentmaster's customers either for free or at below-cost prices. At that point, Jarvis's prices were predatory. Unlike the majority, I do not believe that the complaint's allegations about recoupment change this fact.").

180. Directory Sales Mgmt. Corp. v. Ohio Bell Tel. Co., 833 F.2d 606, 613 (6th Cir. 1987). The court approved the district court's holding that "no hidden charge exists for the first listing." Id. at 610. This demonstrates that the first listing was provided at below cost.

181. Id. at 613.

182. The court also employed the single-market analysis used by the *Kentmaster* court, reasoning that "the first listing is not a separate product or market for the purposes of

The markets for spark plugs, slaughterhouse equipment, and telephone directories illustrate both the economics of recoupment and courts' inability to appreciate this reality.[183] In the context of replacement product markets, courts have defined markets in a way that puts predatory pricing beyond the reach of antitrust law because either (1) the plaintiffs cannot show recoupment and, thus, there is no predatory pricing claim, or (2) the plaintiffs can show recoupment and this, according to the above opinions, proves that the price was not predatory.

2. *Recoupment in Another Geographic Market.* — Recoupment can also occur in geographic markets other than the one in which the predatory pricing took place. A firm that operates in many markets may price below cost in just one or a few of those markets in order to acquire a reputation for price predation.[184] Predatory pricing in one market serves as a warning shot for rivals in other markets. As Professors Areeda and Hovenkamp note, "the predation may 'signal' other incumbents what awaits their price competition or signal outsiders what awaits their entry. The predatory behavior can deter future competition *before* it occurs."[185] In this manner, the exclusionary effects of the predation are not limited to the specific target of a particular episode of predation. This reputational effect can also limit the expansion of existing competitors.[186]

A firm that operates in several geographic markets could overtly price below cost in one market in order to purchase a reputation for price aggression that it can employ in every market in which it competes. Jonathan Baker has explained:

> Suppose a chain store faces a non-chain rival in each of a large number of towns. The chain cuts its prices drastically in a few towns. When the chain's rivals in those towns either exit or begin to compete less aggressively with the chain, the price war ends and high prices are restored. In addition, the chain store's rivals in all the other towns, in which the chain did not cut

predatory pricing, and that to demonstrate predatory pricing DSM would have to show that the Defendants' overall charges for advertising space in their yellow pages are priced below cost." Id. at 614.

183. See also Int'l Travel Arrangers v. NWA, Inc., 991 F.2d 1389, 1396 (8th Cir. 1993) ("To evaluate [defendant's] pricing structure fairly, it was necessary to consider not just its lowest prices, but all of its prices for the routes involved, for that is the only basis upon which the relationship between [defendant's] charges and costs could be determined.").

184. See, e.g., United States v. AMR Corp., 335 F.3d 1109, 1114 (10th Cir. 2003) ("Under the government's theory, American attempted to monopolize the four city-pair routes in question in order to develop a reputation as an exceedingly aggressive competitor and set an example to all potential competitors."); id. at 1115 ("Post-Chicago economists have theorized that price predation is not only plausible, but profitable, especially in a multi-market context where predation can occur in one market and recoupment can occur rapidly in other markets.").

185. 3A Areeda & Hovenkamp, supra note 75, ¶ 726, at 80.

186. See Craswell & Fratrik, supra note 108, at 42 ("[Predation] may be designed to mislead the warehouse store into cancelling plans to expand into neighboring markets.").

> prices, also respond by avoiding aggressive competition with the chain. As a result, prices also increase in the towns in which predation did not occur.
>
> In this hypothetical example of price predation with multimarket recoupment, the firm developed a reputation as a predator by reducing price in a small number of markets. It in effect engaged in selective predation. The rivals in the markets in which predation occurred may have ended up crippled or destroyed, as the traditional predatory pricing story would have it. But rivals competing against the predator in markets in which predation did not occur were not injured directly. Most of the victimized rivals never experienced a price war but were merely intimidated by the threat of a price war into engaging in less aggressive behavior than they would otherwise have found most profitable.[187]

These effects in other markets can make predatory pricing profitable even if recoupment does not take place in the precise market in which the below-cost pricing occurred.[188]

In deciding the recoupment issue, courts are not generally amenable to proof of recoupment through reputational effects in other markets.[189] Some courts have recognized the reputational benefits of predatory pricing in theory, but have nonetheless rejected recoupment-through-reputation arguments. For example, in *Advo, Inc. v. Philadelphia Newspapers, Inc.*, the Third Circuit acknowledged the theoretical possibility of reputational effects deterring entry after a predator raises price, but it discounted the argument, asserting that "[p]otential competitors will realize that at some point the predatory firm will be unable or unwilling to charge below-cost prices and absorb further losses, since nobody's pockets are bottomless."[190] The court disposed of the reputational effects argument by *assuming* entry. But some dominant firms try to acquire a reputation for aggression in an effort to provide notice to all would-be entrants that entry will be greeted with predation.[191]

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187. Baker, supra note 125, at 590–91 (footnotes omitted).

188. See Steven F. Benz, Note, Below-Cost Sales and the Buying of Market Share, 42 Stan. L. Rev. 695, 741 (1990) ("Long-term sales at, or below, cost, from a protected home market . . . to a low-price geographic market may benefit producers [under a variety of scenarios].").

189. See 3A Areeda & Hovenkamp, supra note 75, ¶ 727, at 97 (highlighting cases where courts declined to consider reputational effects).

190. 51 F.3d 1191, 1202 (3d Cir. 1995); see also Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2260 (noting in Traffic Scan Network, Inc. v. Winston, No. 92-2243, 1995 WL 317307 (E.D. La. May 24, 1995), "district court rejected a reputation effect argument not because it was implausible, but because market conditions would have prevented such an effect").

191. See Dempsey, supra note 107, at 164 ("Any time that a low fare carrier attempted to enter Northwest's monopoly markets, Northwest engaged in a predatory

The reputational effect for a predatory firm in multiple markets makes long-term recoupment possible for below-cost pricing that otherwise appears unprofitable. Even if the predator fails to recoup in the specific market where it charged a price below cost, the signaling effect can outweigh the losses associated with predatory pricing.[192] For example, in the early telephone era, Bell engaged in predatory pricing in Madison, Wisconsin, which allowed it to drive its local competitors from the market and to signal to the broader market its willingness to price below cost.[193] Although Bell was probably unable to recoup its Madison-based losses in the Madison market, its strategy was nonetheless profitable because Bell could now recoup in other markets.[194] Professors Bolton, Brodley, and Riordan have explained that having openly engaged in below-cost pricing in Madison (and a few other markets), "Bell, while maintaining low prices in Madison for several years, was able to raise prices to a supracompetitive level in many other markets without inducing significant entry."[195]

The cumulative effects of a reputation for predation can be significant. The reputation itself "serves as a barrier to entry, allowing the predator to increase prices in the recoupment market."[196] The reputation for predation can also deter venture capitalists and other lenders from financing entry into any market dominated by the predator.[197] And the reputational effects can deter reentry into any market from which the predator has driven rivals and subsequently raised price in order to recoup its investment.[198]

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response designed to drive the low fare choice from the market, and to serve as a painful example to any other potential competitor.").

192. See Brodley & Hay, supra note 57, at 742–43 ("If other entrants are aware of this threat, the return from predation, spread across many markets and extended over time, could amply exceed the losses sustained in the demonstration effect market."); Rapp, supra note 117, at 602 ("Under these conditions repeated predatory episodes pay off in total even though the defeat of a single rival in any one of them would cost the predator more than it would return in extra profits."); Oliver E. Williamson, Predatory Pricing: A Strategic and Welfare Analysis, 87 Yale L.J. 284, 287 (1977) ("If by responding aggressively to a current threat of entry a dominant firm can give a 'signal' that it intends to react vigorously to entry in later time periods or different geographical regions, discounted future gains may more than offset sacrifices of current profit.").

193. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2309–10.

194. Id.

195. Id. at 2310 (footnote omitted).

196. Id. at 2301.

197. See id. (finding financiers may be discouraged from backing future rivals that may exit or fail to enter markets dominated by predator); see also supra notes 117–126 and accompanying text (discussing predatory pricing and venture capitalists).

198. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2302 ("Reputation effects enhance the profitability of financial predation by making entry or reentry less likely. Future potential entrants observing the failure of the current entrant can only be more cautious in contemplating entry, whether or not they recognize the

A predator's participation in multiple geographic markets can be particularly important to a predatory pricing scheme because the supracompetitive profits earned in another market can fund the below-cost pricing in the market in which predation is taking place. Historically, Congress has been concerned with this possibility.[199] The Supreme Court has noted that "Congress by the Clayton Act and Robinson-Patman Act barred the use of interstate business to destroy local business" through programs in which "profits made in interstate activities would underwrite the losses of local price-cutting campaigns."[200] Nevertheless, firms that engage in below-cost pricing in one market often finance the predation through cross-subsidization across geographic markets. Examples include airlines,[201] tobacco companies,[202] grocery stores,[203] bread companies,[204] and dairy companies.[205]

This ability to fund predation from another market's profits in turn gives the predator visible staying power, which increases the credibility of its predatory threat.[206] The reputational effects of price predation inure to the predator itself and not to any particular product or geographic market. Thus, below-cost pricing in one product in one region can produce entry-deterring effects in other product markets and in other locations.[207] Furthermore, because the losses associated with limited predatory pricing can be recouped in multiple markets,[208] the amount recouped in each individual market need not be particularly great. Given this reputational dynamic across markets, the recoupment inquiry should

predatory nature of the price cutting."); id. at 2265 ("[T]he incumbent's past reputation as a predator deters future entry or reentry.").

199. See McGahee v. N. Propane Gas Co., 858 F.2d 1487, 1498 (11th Cir. 1988) (discussing legislative intent behind Clayton Act and Robinson-Patman Act to curb predatory pricing); Jordan, supra note 133, at 275 (examining legislative intent behind Robinson-Patman Act).

200. Moore v. Mead's Fine Bread Co., 348 U.S. 115, 119–20 (1954).

201. Dempsey, supra note 107, at 152.

202. Malcolm R. Burns, Outside Intervention in Monopolistic Price Warfare: The Case of the "Plug War" and the Union Tobacco Company, 56 Bus. Hist. Rev. 33, 35–36 (1982).

203. Dirlam & Kahn, supra note 172, at 215.

204. *Moore*, 348 U.S. at 118; Estes Kefauver, In a Few Hands: Monopoly Power in America 139, 154–55 (1965).

205. United States v. Nat'l Dairy Prods. Corp., 372 U.S. 29, 34 (1963).

206. See Dirlam & Kahn, supra note 172, at 142 (discussing dangers from firms operating in multiple markets).

207. See supra notes 192–205 and accompanying text (discussing recoupment across geographic markets).

208. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2248 ("In reputation effect predation . . . a predator reduces price in one market to induce the prey to believe that the predator will cut price in its other markets or in the predatory market itself at a later time, thereby enabling multimarket recoupment of predatory losses.").

not be limited to the individual market in which the predation took place.[209]

3. *Targeted Cuts and Fighting Brands.* — The argument that firms cannot recoup the losses associated with predatory pricing is often based on the assumption that the predator must reduce its price below cost on all of its sales. Robert Bork and John McGee argued that predatory pricing is not rational—and therefore does not occur—because the predator presumably has a greater market share; thus, when the price of the product falls below cost, the predator will suffer proportionately greater losses than the prey.[210] According to this argument, as the predator succeeds in acquiring more market share, its relative losses increase as well.[211] These scholars assume that the dominant firm must cut price across all units of its product, driving up losses and making recoupment all but inconceivable.

Predatory pricing, though, need not require a dominant firm to charge a predatorily low price to all of its customers. The history of price predation shows that predators do not indiscriminately reduce price below costs for all of their sales. Their strategies are more shrewd than that. First, predators engage in targeted price cuts.[212] For example, Standard Oil targeted its price cuts to its rivals' customers.[213] Professors Dalton and Esposito have explained:

> Standard also employed a sophisticated and extensive intelligence network. Its employees identified the shipments and customer destinations of wholesalers of competing refiners using information obtained from agents of the railroads, retailers of refined oil products, and other employees of Standard. Standard maintained this information in an elaborate card cata-

209. See Kwoka & White, Economic and Legal Context, supra note 120, at 181 ("Even if 'irrational' when considered in isolation, such conduct may create a reputation for aggressive response that discourages any other competitors from initiating action. The value of that reputation justifies the expenditure in the initially targeted market.").

210. Bork, Paradox, supra note 20, at 149 ("Losses during a price war will be proportionally higher for the predator because he faces the necessity of expanding his output at ever higher costs . . . ."); McGee, Revisited, supra note 20, at 296 ("It will also cost the predator more than it costs his prey and probably an increasing amount of money as well.").

211. Bork, Paradox, supra note 20, at 149; McGee, Revisited, supra note 20, at 296.

212. John E. Kwoka, Jr. & Lawrence J. White, The Economic and Legal Context, *in* The Antitrust Revolution: Economics, Competition, and Policy, 166, 173–174 (John E. Kwoka, Jr. & Lawrence J. White eds., 3d ed. 1999) [hereinafter Antitrust Revolution, 3d ed.] ("[M]ore selective price reductions targeted against particular rivals will be relatively more costly to those rivals.").

213. Dalton & Esposito, Re-Examination, supra note 115, at 166 ("Standard typically did not cut prices throughout a market when combating a rival. Rather, Standard generally cut prices only to customers of its rivals, leaving unchanged the prices to the customers that it served."); Leslie, *Standard Oil*, supra note 7, at 592 ("Standard identified those buyers who were using a particular seller that Standard had targeted for elimination.").

logue that was then used to direct its sales force to capture or recapture the customers of rival refiners.[214]

Such targeted price cuts can both drive out the target rival and send a message to other rivals (and their financiers) that the predator is willing to suffer losses in order to drive competitors from the market.

Second, firms have employed fighting brands, which are lower-priced—sometimes predatorily priced—versions of a product. A firm may launch a fighting brand in its competitors' markets while continuing to charge a higher price for its own name-brand product. The most famous fighting brand was American Tobacco Company's Battle Ax, a chewing tobacco whose price plummeted below cost as American Tobacco inflicted losses on its competitors—and itself—in a bid to force its rivals to participate in a tobacco cartel.[215] In addition to reducing price, American Tobacco engaged in an expansive advertising campaign for Battle Ax, particularly in its rivals' home markets.[216] American Tobacco's losses during the 1895 to 1898 period exceeded $3,400,000,[217] but the firm succeeded. The so-called "plug war" ended when the major producers formed a trust that eventually controlled eighty-five percent of the market, until the trust was dissolved by the Supreme Court.[218] The fighting brand can be a new product or a reintroduced one, as when the vice president of marketing for North American Philips Consumer Product Division proposed that, should a rival enter the rotary shaver market in the United States, Philips should "kill this stone dead by introducing old models at very low prices."[219] Fighting brands have been employed by dominant firms in the markets for photographic paper, thread, and rear projection readouts.[220]

Third, a monopolist can create and sell through bogus companies in order to conceal its targeted price cuts from its customers who might otherwise be angered by the price discrimination. For example, Standard

214. Dalton & Esposito, Re-Examination, supra note 115, at 161.

215. See Burns, supra note 202, at 38 (noting "nominal wholesale price of *Battle Ax* fell to 13 cents per pound, a level apparently below the average cost of production, which included the 6-cent federal excise tax").

216. Id. at 38–39.

217. Id. at 39.

218. Ross D. Petty, Antitrust and Innovation: Are Product Modifications Ever Predatory?, 22 Suffolk U. L. Rev. 997, 1008–09 (1988).

219. U.S. Philips Corp. v. Windmere Corp., 861 F.2d 695, 698 (Fed. Cir. 1988) (internal quotation marks omitted).

220. Petty, supra note 218, at 1009–11. The precursor to fighting brands were so-called fighting ships, which referred to steamship conferences which launched "'fighting ships' to offer a lower price on a competitor's newly announced route in order to prevent the rival from obtaining cargo." Id. at 1007–08. The strategy of fighting ships bears a remarkable resemblance to the predatory pricing claims against dominant airlines, which target the routes of new upstart low-cost airlines, while continuing to charge supracompetitive fares on their other routes.

Oil set up several bogus companies that represented themselves as independent of Standard while charging a lower price—sometimes a predatorily low price—than Standard and its rivals.[221] Tobacco companies used bogus independents, too.[222] Under this scheme, the dominant firm continues to supply its loyal customers at the going rate, while the shell firm sells at a loss to its rivals' customers. Once the rivals are driven from the market, the bogus independent firm simply vanishes, leaving all customers dependent on the monopolist.[223]

In sum, a predatory firm need not cut prices across its product line to all of its customers. It can target its cuts, while purchasing a reputation for predation. It can develop a fighting brand. Alternatively, it can conceal its price predation behind a bogus shell company. Predatory firms have employed all of these tactics, which reduce the losses associated with predatory pricing and, thus, increase the likelihood of recoupment.

4. *Recoupment in Multifirm Markets.* — Courts assume that recoupment is impossible unless the predator can force all of its competitors from the market.[224] Some economists further assume that recoupment is impossible unless the predator succeeds in driving its rivals from the market relatively permanently. For example, Jean-Jacques Laffont and Jean Tirole argue that "'[p]redation corresponds to a sacrifice of short-term profits in order to boost long-term gains by forcing rivals out of the market. Predation can be profitable only if it leads competitors to exit the market enduringly.'"[225] Some courts have used these assumptions to construct bright line tests to create quasi-safe harbors in which recoupment is legally improbable, if not impossible to prove. For example, in *Rose Acre*, Judge Easterbrook implied that recoupment is unattainable if the predator's market share is below thirty percent in the market in which the predation took place.[226] But this approach ignores the possibility of recoupment in multifirm markets. Even if competitors remain in

221. Dalton & Esposito, Re-Examination, supra note 115, at 169.

222. See, e.g., Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2244–45 (discussing American Tobacco Company's use of bogus independents).

223. See, e.g., Leslie, *Standard Oil*, supra note 7, at 594 (describing dissolution of bogus companies in context of *Standard Oil*).

224. See Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 231–32 (1993) (rejecting possibility of competitive injury through oligopolistic price coordination because plaintiff failed to demonstrate likelihood of recoupment).

225. Barry Nalebuff, Exclusionary Bundling, 50 Antitrust Bull. 321, 322 (2005) (quoting Jean-Jacques Laffont & Jean Tirole, Competition in Telecommunications 163 (2000)).

226. A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1403 (7th Cir. 1989) ("Cases frequently say that as a matter of law single-firm shares of 30% or less cannot establish market power."). But see Goldstein, supra note 81, at 1773 ("Easterbrook's analysis of market share is questionable. He indicates that 30% is the minimum market share necessary to establish market power sufficient to recoup lost profits." (citing *Rose Acre*, 881 F.2d at 1403)).

the market, recoupment can occur through either cartel or oligopoly pricing. In either scenario, the threat of predatory pricing can discipline the market, resulting in higher prices and, consequently, recoupment.

a. *Recoupment Through Cartelization.* — The Chicago School and its adherents in the federal courts assume that when the predator attempts to increase price in order to recoup its investment in predatory pricing, any remaining competitors will bid the price down. For example, the *Matsushita* Court found it implausible that a cartel of Japanese manufacturers could recoup a joint investment in predatory pricing.[227]

This line of thinking fails to appreciate the relationship between predatory pricing and cartelization. Predatory pricing can force otherwise obstinate rivals to cooperate in a cartel by using a combined carrot-and-stick approach in which the predator threatens to continue below-cost pricing until the target accepts the invitation to charge supracompetitive prices, a result that makes all market participants better off than either predation or true competition.[228] Historically, dominant firms have employed aggressive pricing to punish "rogue" firms and to convince them to raise prices.[229] Indeed, price punishment by a single player is relatively common among stable cartels. For example, when the diamond-producing nation of Zaire sold more diamonds than it had been allotted by the cartel, DeBeers—the leader of the diamond cartel—punished Zaire by flooding the market with diamonds, driving the price down considerably. Zaire ultimately pleaded to return to the cartel fold.[230] DeBeers's actions reflect the predatory pricing dynamic: DeBeers took a loss in the short term in order to force Zaire to be a loyal cartel member in the long term. In some markets, the predator can target its disciplinary price cuts to a particular segment of the market in order to inflict maximum injury on the recalcitrant firm.[231] In any case, the history of cartel enforcement mechanisms shows that cartel members, especially cartel leaders, use price wars—including below-cost pricing—to disci-

227. Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 592–93 (1986) (finding it unlikely alleged Japanese cartel could maintain supracompetitive prices to recoup losses).

228. See 3A Areeda & Hovenkamp, supra note 75, ¶ 727, at 86–87 ("The dominant firm may use predation merely to intimidate rivals from cutting price or increasing output, and even promising the victims oligopoly returns once they acquiesce.").

229. See, e.g., John D. Clark, The Federal Trust Policy 12 (1931) (discussing predatory pricing by shipping conferences); Fritz Machlup, The Basing-Point System: An Economic Analysis of a Controversial Pricing Practice 130–31 (1949) (discussing steel industry).

230. See Christopher R. Leslie, Trust, Distrust, and Antitrust, 82 Tex. L. Rev. 515, 619–22 (2004) (discussing DeBeers's tactics against Zaire).

231. See Herbert Hovenkamp, The Antitrust Enterprise 168–69 (2005) [hereinafter Hovenkamp, Antitrust Enterprise] ("Drastic price cuts by the oligopoly leadership are one form of discipline, particularly if the cuts can be confined to a particular market niche where they will inflict the largest amount of harm on the price cutter.").

pline uncooperative cartel members.[232] Examples include cartels involving shipping, steel, tobacco, vitamins, and computer memory.[233] Additionally, a firm may employ predatory pricing to gain leadership over a cartel. For example, Archer Daniels Midland (ADM), a large agribusiness firm, charged a price significantly below its marginal cost in order to coerce its rivals into letting it lead the global cartel in the amino acid lysine.[234] Finally, predatory pricing can help stabilize an existing cartel by keeping out new entrants who would disrupt a collusive market.[235]

The historical examples prove that competitors do not have to leave the market in order for the predator to recoup. Recoupment can occur through cartel pricing in the aftermath of predation.[236] Unfortunately, courts do not appreciate the ubiquity or effectiveness of the predatory pricing as a mechanism for cartel creation and enforcement. This leads them to underestimate the likelihood of recoupment.

b. *Recoupment Through Oligopoly Pricing.* — Even if the firms in a concentrated market do not engage in explicit price fixing through a cartel, a price predator may be able to recoup through oligopoly pricing. Firms in an oligopoly—a market with few sellers—can charge supracompetitive prices when the firms jointly recognize that they are collectively better off if they do not undercut each other's prices. When price increases are achieved without actual agreement among the firms, oligopoly pricing does not fall within section 1's prohibition on anticompetitive agreements.[237]

The *Brooke Group* majority opined that the losses sustained in predatory pricing could not feasibly be recouped in an oligopoly market. After

232. See, e.g., Jeremiah Whipple Jenks, The Trust Problem 147–48 (rev. ed. 1909) (noting how Whiskey Trust in late nineteenth century used significant price cuts to force rivals to join whiskey cartel); see also Malcolm v. Marathon Oil Co., 642 F.2d 845, 850 (5th Cir. Unit B Apr. 1981) ("Malcolm testified that one of his competitors told him that prices would soon rise but 'they were going to go back down' unless Malcolm raised his prices.").

233. See Christopher R. Leslie, Rationality Analysis in Antitrust, 158 U. Pa. L. Rev. 261, 291–92 (2010) [hereinafter Leslie, Rationality Analysis] (describing how cartels use price wars to discipline rogue members).

234. John M. Connor, Global Cartels Redux: The Amino Acid Lysine Antitrust Litigation, as reprinted in Antitrust Revolution, 4th ed., supra note 81, at 252, 259–60 (noting ADM may have continued pricing below cost if Asian manufacturers had not acquiesced to joining ADM-dominated cartel); Leslie, Rationality Analysis, supra note 233, at 280–81 (noting ADM's predatory pricing was part of strategy "to threaten the Asian firms by suggesting that if they did not divide the world market to ADM's liking, then ADM would flood the market, drive the price down, and potentially drive other lysine producers from the market entirely").

235. See Craswell & Fratrik, supra note 108, at 20 (noting potential disruptive effect to collusion scheme of entry by warehouse store into market).

236. See Leslie, *Standard Oil*, supra note 7, at 583–84 (citing example of Standard Oil-led cartel).

237. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 227 (1993).

acknowledging the theoretical possibility of recoupment through oligopoly pricing,[238] the *Brooke Group* majority rejected this as "the least likely means of recouping predatory losses."[239] Although the evidence showed that the tobacco industry was controlled by a well-heeled oligopoly, the majority reasoned that any tacit coordination among tobacco firms would have been "unmanageable"[240] and B&W "had no reasonable prospect of recouping its predatory losses."[241] Concluding that recoupment through oligopoly pricing was implausible, the Court ruled that B&W was entitled to judgment as a matter of law.[242]

The *Brooke Group* majority's reasoning and holding are flawed both factually and theoretically. Tobacco companies had historically secured above-market profits through years of oligopoly pricing, as the *Brooke Group* majority itself admitted.[243] The facts of *Brooke Group* demonstrate how recoupment through oligopoly can succeed. While concluding that oligopoly pricing was an implausible means of recoupment, the Court acknowledged that following B&W's alleged price predation, "the list prices on all cigarettes, generic and branded alike, rose to a significant degree during the late 1980's. From 1986 to 1989, list prices on both generic and branded cigarettes increased twice a year by similar amounts."[244] Further, the expert evidence at trial showed that "these price increases outpaced increases in costs, taxes, and promotional expenditures. The list prices of generics, moreover, rose at a faster rate than the prices of branded cigarettes, thus narrowing the list price differential between branded and generic products."[245] Not only *could* B&W recoup through oligopoly pricing, it actually did.

Abundant economics literature demonstrates the profitability of recoupment through oligopoly pricing, even considering the specter of free riding.[246] Indeed, recoupment through oligopoly pricing may be more likely than recoupment through monopoly pricing. Professors

238. See id. at 225 (requiring plaintiff to demonstrate oligopolistic scheme "would cause a rise in prices above a competitive level that would be sufficient to compensate for the amounts expended on the predation").

239. Id. at 228.

240. Id. at 238.

241. Id. at 243.

242. Id.

243. Id. at 213 ("The cigarette industry . . . has long been one of America's most profitable, in part because for many years there was no significant price competition among the rival firms.").

244. Id. at 235 (citation omitted).

245. Id. (citation omitted).

246. See, e.g., Bolton, Brodley & Riordan, Response, supra note 122, at 2502–03 ("While a predatory pricing strategy by an oligopoly may be partially undermined by free riding, it can still be profitable. . . . [S]ome or all members of the oligopoly may have an incentive to adopt aggressive policies, such as below-cost pricing, that contribute to the foreclosure of new entrants." (footnote omitted)).

Areeda and Hovenkamp explain that if the goal of the predation is to cartelize rather than monopolize the market, then the target of the predation has more incentive to eventually cooperate with the predator than if the predator's goal is to drive the target from the market entirely.[247] If the target acquiesces by raising price instead of fighting back, "the predatory period can be shorter, with less drastic and more selective price cuts. Since the predatory investment is less, recoupment need not be so large either as under monopolistic predation."[248] Using price predation to impose oligopoly pricing and to discipline rogue firms is cost-effective because in many markets, the targeted rival would sooner engage in profit-maximizing oligopoly pricing than exit the market altogether.[249] Firms know how to read the signals of price predation as an invitation to engage in oligopoly pricing.[250] This is the language of business and, while some federal judges may not speak it, executives do fluently.

5. *Recoupment Through Distorting Test Markets.* — In some instances, targeted predatory pricing can deter entry in multiple markets. Even if recoupment does not occur in the isolated geographic market in which the below-cost pricing occurred, the predatory pricing is profitable because recoupment is achieved across geographic markets, including those in which price did not dip below cost. For example, predatory pricing can profitably delay a rival's entry into the market when the predatory pricing disrupts market testing. Before entering a new geographic market, many firms will first test the market to determine whether the expected profits from entering that particular geographic market exceed the expected costs. A dominant incumbent can use predatory pricing to deter or delay entry through the use of so-called test market predation, in which the "predator frustrates the prey's market probe by openly cutting price in the test market to keep the prey ignorant about normal market conditions."[251] The targeted price predation precludes the would-be entrant from discerning that entry would be profitable.[252]

Perhaps the most famous instance of test market predation is General Foods's response to Procter & Gamble's (P&G) attempted entry

247. 3A Areeda & Hovenkamp, supra note 75, ¶ 727, at 84 (noting predator can more quickly convince price cutter to raise price than drive it from market entirely).

248. Id.

249. See id. ("[P]redation intended to create or maintain an oligopoly offers its victims a profitable escape—indeed, one that may promise even more profits than the pre-predation market.").

250. See id., at 94 ("But the defendant's response to the plaintiff's introduction of generic cigarettes—introducing a closely similar or identical product and radically cutting the price—is a conventional form of oligopoly retaliation that is unlikely to be misread.").

251. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2248–49.

252. Id. at 2311 ("The predator cuts prices to reduce the entrant's sales in the test market, which prevents the entrant from discovering whether demand is sufficiently strong to justify its continued presence in the test market.").

into General Foods's turf.[253] General Foods sold Maxwell House brand coffee in the eastern United States and dominated that geographic market.[254] P&G's Folgers brand coffee was the market leader in the West, but was not available on the East Coast.[255] To determine whether to expand east, P&G decided to use some eastern cities as test markets for Folgers.[256] General Foods responded by slashing the price of Maxwell House coffee to below average variable cost for about a year in the test market cities (while maintaining its higher, profitable price in other markets).[257] At times, General Foods sold Maxwell House coffee for less than the cost of the unprocessed green coffee beans.[258] General Foods's strategy worked; P&G declined to enter the Eastern market and made no other attempts for another seven to eight years.[259] Although General Foods suffered losses for a year in a few markets, the strategy allowed it to reap supracompetitive profits in several more markets for many years. Most importantly for our purposes, General Foods probably recouped its investment in price predation.[260]

Test market predation shows how to leverage the money invested in predatory pricing in isolated markets in a manner that allows recoupment across many markets. Test market predation creates the impression that new entry will be unprofitable and thus dissuades entry on a grand scale.[261] By delaying entry, test market predation hurts consumers who are denied both choice and price competition in the short term.[262]

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253. Gen. Foods Corp., 103 F.T.C. 204, 208–09 (1984) (dismissing complaint alleging General Foods used "its dominant position . . . to frustrate the entry of other regular coffee producers into certain relevant markets, and to prevent . . . competition . . . in the relevant markets").

254. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2314 (citing John C. Hilke & Philip B. Nelson, Strategic Behavior and Attempted Monopolization: The Coffee (*General Foods*) Case, *in* The Antitrust Revolution: Economics, Competition, and Policy 208, 222 (John E. Kwoka, Jr. & Lawrence J. White eds., 1989)).

255. Bolton, Brodley & Riordan, Response, supra note 122, at 2521.

256. Id.

257. Id.

258. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2314.

259. Bolton, Brodley & Riordan, Response, supra note 122, at 2521.

260. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2317 ("General Foods was able to maintain higher prices in other eastern markets. The resulting deferral of P&G's entry in the East for several years should have enabled General Foods to recoup fully its predatory investments in the limited test markets . . . ." (footnote omitted)).

261. See Bolton, Brodley & Riordan, Response, supra note 122, at 2523 ("Under a test market strategy . . . the victim remains uncertain whether entry would be profitable and . . . may decline to enter." (footnotes omitted)).

262. See id. at 2522 ("[D]elayed competition hurts consumers just as much as permanent restraints during the period of delay . . . .").

C. *The Ramifications of the Recoupment Requirement*

The development of the recoupment requirement has been a boon for predatory pricing defendants. In adopting the requirement for section 2 monopolization claims, the *Brooke Group* Court repeated *Matsushita*'s mantra that "'predatory pricing schemes are rarely tried, and even more rarely successful'" because recoupment is so unlikely.[263] By requiring plaintiffs to prove recoupment while instructing lower courts that recoupment does not happen, the Court invited lower courts to systematically reject predatory pricing claims.[264] Lower courts obliged, routinely granting summary judgment to predatory pricing defendants because recoupment seemed unlikely.[265] The leading antitrust treatise notes, "By the stringency of its demand for proof of recoupment, the Court cleared the way for summary rejection of most predatory pricing claims."[266]

As a professor, Frank Easterbrook had long advocated that predatory pricing should not be illegal.[267] As a judge, by inserting the recoupment requirement into section 2 predatory pricing cases, he effectively made his wish come true. Easterbrook's reliance on the recoupment requirement to reject predatory pricing claims seems disingenuous at best since Easterbrook argued that recoupment was not possible.[268] To say that

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263. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 226 (1993) (quoting Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986)).

264. See Benz, supra note 188, at 741 (noting it is "virtually impossible to defeat a motion for summary judgment" by predatory pricing defendant).

265. See, e.g., Nat'l Parcel Servs., Inc. v. J.B. Hunt Logistics, Inc., 150 F.3d 970, 971 (8th Cir. 1998) (affirming summary judgment for trucking company defendant that engaged in predatory pricing because there was no "dangerous probability" of defendant recouping losses stemming from its pricing); Clark v. Flow Measurement, Inc., 948 F. Supp. 519, 528 (D.S.C. 1996) ("[T]he plaintiffs' antitrust claims also fail because the plaintiffs cannot sufficiently show that Flow Measurement has an economically viable scheme for recoupment."); C.B. Trucking, Inc. v. Waste Mgmt., Inc., 944 F. Supp. 66, 69 (D. Mass. 1996) (affirming summary judgment for defendant because even if defendant was engaged in predatory pricing, there was no "dangerous probability" of recoupment).

266. 3A Areeda & Hovenkamp, supra note 75, ¶ 726, at 72; see also Jordan, supra note 133, at 292 (claiming, with one exception, "every lawsuit could have been decided for defendant on summary judgment based upon plaintiff's failure to show that defendant could recoup its losses").

267. See, e.g., Easterbrook, supra note 106, at 29 (arguing market competition, not courts, should deal with issue of below-cost pricing); id. at 36–37 (arguing net effect of predatory pricing is to reduce, not increase, price).

268. See id. at 27 n.55 ("This shows the futility of a conspiracy to charge low prices; recoupment will be impossible."); see also Baker, supra note 125, at 589 ("Price predation is almost always irrational, according to the Chicago School, because recoupment is almost always implausible."); Kenneth G. Elzinga & David E. Mills, Predatory Pricing and Strategic Theory, 89 Geo. L.J. 2475, 2477 (2001) ("Paul Milgrom and John Roberts summarized this influence by observing that 'a large fraction of the economics profession would argue that . . . predation is an irrational strategy for attempting to gain or maintain a monopoly

predatory pricing is illegal only when accompanied by a high probability of recoupment—while arguing that recoupment is not possible—is essentially a one-two punch that legalizes predatory pricing. As Professors Areeda and Hovenkamp have explained, "any requirement that a plaintiff actually provide evidence indicating that the monopoly 'payoff' will be greater than the predation investment involves undue speculation and becomes a virtual rule of nonliability."[269]

The Supreme Court did not officially eliminate predatory pricing from the reach of the Sherman Act.[270] But, given the low success rate following the imposition of the recoupment requirement, the cause of action seems somewhat academic. If courts are going to require plaintiffs in predatory pricing cases to prove that a dangerous probability exists that the defendant will recoup its losses from below-cost pricing, then judges need to better understand the myriad ways in which recoupment can take place. In addition to improving their recoupment analysis, courts should consider whether to jettison the recoupment requirement altogether because, as Part III argues, predatory pricing schemes do, in fact, inflict injury regardless of whether recoupment occurs.

III. Predatory Pricing Injures Competition Even Without Recoupment

The sad irony of the repeated judicial misapplication of the recoupment requirement in predatory pricing cases is the fact that this element is unnecessary and inappropriate. Whether a monopolist recoups the money that it has spent to acquire monopoly power does not determine whether its anticompetitive conduct has harmed consumer welfare. Antitrust law cares about consumer welfare and should protect efficient competitors from illegal predatory conduct that injures competition. This Part explains how, even if there is no recoupment, antitrust injury may still result from the failed attempt at predatory pricing.

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position and that it is, therefore, unlikely to be adopted in practice.'" (quoting Paul Milgrom & John Roberts, Predation, Reputation, and Entry Deterrence, 27 J. Econ. Theory 280, 280 (1982))); John E. Kwoka, Jr. & Lawrence J. White, Introduction to Antitrust Revolution, 3d ed., supra note 212, at 1, 2 ("On other issues, the Chicago School has spoken equally strongly. Price cuts almost invariably reflect lower costs and are therefore procompetitive. For price cuts to be predatory, by contrast, requires various stringent conditions that are unlikely to be met, and hence predation is unlikely to occur.").

269. 3A Areeda & Hovenkamp, supra note 75, ¶ 724, at 38.

270. The Court continues to claim that predatory pricing can violate section 2 of the Sherman Act. See Pac. Bell Tel. Co. v. Linkline Commc'ns, Inc., 129 S. Ct. 1109, 1118 (2009) ("[W]e have ruled that firms may not charge 'predatory' prices—below-cost prices that drive rivals out of the market and allow the monopolist to raise its prices later and recoup its losses." (citing Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222–24 (1993))).

A. *Harm to Consumers*

Courts and commentators routinely praise the first phase of predatory pricing, in which the predator charges a price below cost. Judges characterize this as a gift to consumers that antitrust law should be loath to penalize or deter.[271] When characterizing predatory pricing as beneficial to consumers, judges and scholars routinely fail to acknowledge that there are two separately identifiable categories of consumers who are affected by predatory pricing. The first group of consumers is composed of those who purchase the products during the predation phase. These consumers enjoy the benefits of paying a lower price for the product. The second group of consumers includes those who purchase the product during the recoupment phase, after the predator has raised the price. The recoupment inquiry focuses on whether the predator will be able to raise the price high enough and long enough to recover all of the losses that resulted from the lower prices to the first group of consumers.

Consumers paying monopoly prices in the post-predation period are injured even if the monopoly price is insufficient to recoup the investment in predatory pricing. Some commentators have suggested that "in order to injure consumers, the prices set by the surviving firm . . . must rise to a supracompetitive level for a time period sufficient to allow the predator firm to recover its investment . . . including the time value of money."[272] That is incorrect because the plaintiffs' antitrust injury exists independent of recoupment. Professors Areeda and Hovenkamp have explained that "post-predation prices can be significantly supracompetitive, thereby injuring consumers, and yet be insufficient in size or duration to provide full recoupment for the defendant's investment in predation."[273] Consumers who pay supracompetitive prices in the post-predation period are injured regardless of recoupment because they are being forced to pay a monopoly price for the product. The fact that earlier consumers received a lower price is irrelevant to the fact that current customers are being victimized by a monopoly that acquired its power through predatory conduct and not through efficiency or a superior product. Even if there is insufficient recoupment, there is still a monopoly for a temporary period and that violates section 2 if the monopoly was achieved through anticompetitive conduct. It is of little solace to current consumers who must deal with a monopolist charging supracompetitive prices that consumers in the past got a really good deal. If the plaintiffs are consumers who made purchases at monopoly prices and are suffering antitrust injury, why should it be a defense that other consumers—who are not plaintiffs—paid lower prices? This does not diminish the antitrust injury of the current plaintiffs.

271. See supra notes 65–67 and accompanying text.

272. Jordan, supra note 133, at 289–90.

273. 3A Areeda & Hovenkamp, supra note 75, ¶ 726, at 77.

B. *Harm to Efficiency*

Predatory pricing also causes inefficiency, regardless of whether the predator recoups its investment. During the period of below-cost pricing, predatory pricing causes overconsumption as consumers base their purchasing decisions on the artificially deflated price. This overconsumption is inefficient for two related reasons. First, below-cost pricing creates artificial demand for the product. In a properly functioning market, prices signal consumers about the scarcity and social value of a particular product.[274] Below-cost pricing sends consumers the wrong signal and causes resources to shift away from higher-value uses.[275] Professor Williamson has explained that if consumers adapt their consumption and investment patterns on the mistaken belief that the (predatory) low price is enduring, consumers can suffer net losses if they incur fixed costs based on their assumption that the relative prices were stable.[276] The Supreme Court in *Brooke Group* acknowledged that "unsuccessful predatory pricing may encourage some inefficient substitution toward the product being sold at less than its cost."[277] As a result, predatory pricing shifts resources away from other, more efficient uses.

Second, pricing below cost creates allocative inefficiency in the form of deadweight loss.[278] In antitrust jurisprudence, deadweight loss generally refers to underconsumption caused by a monopolist or cartel reducing output and increasing price, which results in consumers being denied access to a product despite their willingness to pay the efficient equilibrium price.[279] Deadweight loss can also take the form of overcon-

274. See Paul L. Joskow & Alvin K. Klevorick, A Framework for Analyzing Predatory Pricing Policy, 89 Yale L.J. 213, 224 n.31 (1979) (discussing short-run allocative inefficiency in predatory pricing).

275. See id. ("If price is less than short-run marginal cost, and . . . demand is . . . elastic, the price will not give consumers the proper signal about the scarcity value of the good. Thus, consumers will purchase too much . . . [and] too many resources will be devoted to producing the . . . good in the short run.").

276. Williamson, supra note 192, at 290–91; see also Daniel A. Crane, The Paradox of Predatory Pricing, 91 Cornell L. Rev. 1, 35 (2005) ("[B]elow-cost, nonexclusionary prices may harm consumers by sending false price signals that result in poor consumption planning by consumers.").

277. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224 (1993). In other cases, not involving predatory pricing, the Supreme Court has suggested that antitrust law cares about this type of resource misallocation. See Arizona v. Maricopa Cnty. Med. Soc'y, 457 U.S. 332, 347–48 (1982) (condemning maximum price fixing, in part, because it distorts resource allocation by discouraging provision of services and experimentation).

278. See F.M. Scherer, Predatory Pricing and the Sherman Act: A Comment, 89 Harv. L. Rev. 869, 872–73 (1976) (discussing deadweight loss and concluding "short-run allocative inefficiencies associated with pricing below marginal cost can hardly be ignored").

279. See Christopher R. Leslie, Antitrust Damages and Deadweight Loss, 51 Antitrust Bull. 521, 524–26 (2006) (discussing concept of deadweight loss).

sumption when an inefficiently low price induces consumers to purchase products that cost more to produce than the buyers value them.[280]

Finally, even failed attempts at predatory pricing hurt competitors which are more efficient than the predator. In some of the airline predatory pricing cases, in which courts awarded victories to defendants, new competitors were driven from the market even though they had lower costs.[281] Predatory pricing schemes injure efficient competitors that must defend against inefficiently low prices and, perhaps, exit the market temporarily.[282] The exit of an efficient competitor, followed later by its reentry or the entry of another competitor in response to the defendant's post-predation monopoly pricing, imposes social costs.[283]

If antitrust law cares about efficiency, then it should condemn predatory pricing whether or not the predator successfully recoups its investment in below-cost pricing. The various forms of inefficiency caused by predatory pricing are not dependent on recoupment.[284]

IV. RECONSIDERING THE RECOUPMENT REQUIREMENT

At a minimum, judges should refine their recoupment analysis. This Part goes one step further and argues that it is time to abandon the recoupment requirement in section 2 predatory pricing cases. The recoupment element is unnecessarily burdensome[285] and is too hard to

280. See Crane, supra note 276, at 35 ("[N]onpredatory below-cost pricing is allocatively inefficient, even if it does not lead to, or threaten, later supracompetitive pricing, because it induces the consumption of goods by some consumers who value them at less than the cost of production, creating a deadweight loss."); Christopher R. Leslie, Achieving Efficiency Through Collusion: A Market Failure Defense to Horizontal Price-Fixing, 81 Calif. L. Rev. 243, 270 (1993) ("[D]eadweight loss also exists when trades occur that should not have."). William Landes has also acknowledged that "below-cost pricing causes a deadweight loss." William M. Landes, Optimal Sanctions for Antitrust Violations, 50 U. Chi. L. Rev. 652, 670 (1983). Landes, however, argues that this deadweight loss does not justify antitrust liability "[b]ecause the deadweight loss is a private loss to the predator." Id. at 671.

281. See, e.g., United States v. AMR Corp., 335 F.3d 1109, 1111–12 (10th Cir. 2003) (granting summary judgment to predatory pricing defendant while noting excluded competitors had lower costs).

282. See Herbert Hovenkamp, Antitrust's Protected Classes, 88 Mich. L. Rev. 1, 36 (1989) ("[F]ailed attempts can impose large social costs. . . . [T]he attempt itself can impose enormous losses on rivals who must spend resources defending themselves or make costly exits from the market in favor of other firms.").

283. Some scholars fail to recognize this. See, e.g., Landes, supra note 280, at 678 ("In the case of predatory pricing . . . the optimal penalty is zero when below-cost pricing is followed immediately by entry.").

284. This argument is further elaborated upon later in this Article. See infra Part IV.C (demonstrating whether or not anticompetitive behaviors prove profitable, they may nonetheless impede efficiency and harm consumers).

285. See Erik Hovenkamp & Herbert Hovenkamp, Exclusionary Bundled Discounts and the Antitrust Modernization Commission, 53 Antitrust Bull. 517, 539 (2008) ("One

accurately predict in many cases.[286] Recoupment analysis requires a level of predictive ability beyond that required in traditional monopoly power analysis because courts must predict profitability and not merely power. The element invites and often requires rank speculation.[287] While some scholars have advocated improving the recoupment element by making it more clear, more structured, or more expansive,[288] tinkering does not solve the fundamental problem. The recoupment element is based on a false empirical premise and ignores relevant economic theory. It should be discarded outright.[289]

This Part explains how eliminating the recoupment requirement in predatory pricing litigation would better serve the purposes of antitrust law. First, although the recoupment requirement is claimed to be necessary to prevent false positives, predatory pricing law has other elements that are better suited for this task. Second, the recoupment requirement creates false negatives, which are also inefficient. Third, the recoupment requirement immunizes anticompetitive conduct, which should be condemned. Fourth, eliminating the recoupment requirement conserves judicial resources.

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problem with the recoupment problem as *Brooke Group* articulated it is the great information demands it makes in close cases.").

286. See Phillip E. Areeda, Predatory Pricing, 49 Antitrust L.J. 897, 898 (1980) ("[T]he court will not often know enough to measure the height of relevant entry barriers, or to assess whether a given height would assure a successful predator of recouping his losses.").

287. See Hovenkamp & Hovenkamp, supra note 285, at 539 ("Predicting the length and opportunity cost of a predation strategy, what the likely recoupment (supracompetitive) price would be, when entry might occur and how quickly it would move prices back to the competitive level is typically an exercise in pure speculation except in very obvious situations."); id. at 540 ("[I]n extreme cases on both ends the relevant information might be readily obtained and a prediction fairly clear. But in the vast middle any testimony that profitable recoupment in the *Brooke Group* sense would or would not result is bound to involve significant amounts of conjecture.").

288. See Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2263, 2270 (arguing for use of modern economic and strategic theories in proving predation and recoupment); see also Bolton, Brodley & Riordan, Response, supra note 122, at 2512 ("For example, Elzinga and Mills recommended . . . that proof of recoupment be based on . . . the likely present discounted value of profits, an approach that presents formidable difficulties of proof. A correct calculation under this approach would require projections of future profits and a knowledge of the predator's capital costs." (footnotes omitted)); C. Scott Hemphill, Note, The Role of Recoupment in Predatory Pricing Analyses, 53 Stan. L. Rev. 1581, 1608–12 (2001) (arguing for modifications to structural elements in, and excluding conduct from, recoupment analysis).

289. Others have come to a similar conclusion. See Hovenkamp & Hovenkamp, supra note 285, at 539 ("A better approach for litigation purposes is to abandon the strict recoupment requirement, but ensure that the market at issue is one that is structurally capable of being monopolized.").

A. *Reducing False Positives Through More Appropriate Filters*

The primary debate in predatory pricing is how to distinguish between legitimate price competition and predatory pricing designed to eliminate long-term competition. The recoupment requirement is unnecessary to demarcate this line.[290] Some commentators fear that without the recoupment requirement, ordinary price reductions could be found illegal under the Sherman Act.[291] However, there are other requirements for liability that protect against false positives. These other elements are more appropriate filters, and the recoupment requirement can interfere with their operation.

1. *Monopoly Power.* — Section 2 of the Sherman Act condemns both monopolization and attempted monopolization.[292] Each is a separate cause of action with its own elements. Illegal monopolization has two elements under the *Grinnell* test: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."[293] In order to prove the first element, the plaintiff must define the relevant market in which the defendant operates and then show that the defendant possesses monopoly power in that market.[294] This is generally done by showing that the defendant controls a dominant market share and that barriers to entry prevent new rivals from entering the market and bidding the price down.[295] Illegal attempted monopolization has three elements under the *Spectrum Sports* test: "[(1)] the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power."[296] The third element of the *Spectrum Sports* test is similar to the first prong of the *Grinnell* test in that it requires the plaintiff to define the relevant market and to show that, as a result of the defendant's anticompetitive conduct, there is a dangerous probability that the defendant will

290. See generally Craswell & Fratrik, supra note 108, at 8–14 (describing methods of distinguishing legitimate price competition from predatory pricing).

291. See supra notes 52–63 and accompanying text (discussing risk of false positives as rationale for recoupment requirement in predatory pricing claims).

292. 15 U.S.C. § 2 (2012).

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

294. See, e.g., United States v. Microsoft Corp., 253 F.3d 34, 51–56 (D.C. Cir. 2001) (per curiam) (defining relevant market as Intel-compatible PC operating systems and finding Microsoft had monopoly power within defined market in analysis of first *Grinnell* prong).

295. Id. at 51.

296. Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 456 (1993) (citing 3 Phillip Areeda & Donald F. Turner, Antitrust Law ¶ 820, at 312 (1978)).

monopolize this market.[297] This nominally third element is often analyzed first.[298] In addition to these elements for liability, private plaintiffs bringing section 2 cases must also prove that they suffered antitrust injury caused by the antitrust violation.[299]

The first element of the *Grinnell* test and the third element of the *Spectrum Sports* test act as threshold elements because unilateral anticompetitive conduct, such as below-cost pricing, does not violate section 2 unless the defendant has monopoly power or a dangerous probability of achieving monopoly power through its anticompetitive conduct. Predatory pricing is a way to satisfy the second element of the *Grinnell* test and the first element of the *Spectrum Sports* test. It is a form of monopoly—or anticompetitive—conduct. But given the market power requirement, which is a threshold element, the prohibition against predatory pricing only applies to monopolists and would-be monopolists.

The monopoly power element reduces the risk that predatory pricing claims will deter beneficial competition. Because section 2 applies only to monopolists (and would-be monopolists), the vast majority of American businesses are completely unaffected by section 2 predatory pricing law. Firms without significant market share can use all variety of loss leaders and promotional discounts without incurring section 2 liability.[300] If the predator reduces price below cost and injures its rivals, but fails to acquire the power to raise prices above supracompetitive levels, then its conduct may be anticompetitive, but section 2 liability does not attach.[301]

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297. See id. ("In order to determine whether there is a dangerous probability of monopolization, courts have found it necessary to consider the relevant market and the defendant's ability to lessen or destroy competition in that market.").

298. See, e.g., Int'l Tel. & Tel. Corp., 104 F.T.C. 280, 407 (1984) ("[T]he [FTC] has taken the position that in attempted monopolization cases, the dangerous probability of success element should be evaluated 'before proceeding to the other two elements.'" (quoting Gen. Foods Corp., 103 F.T.C. 204, 346 (1984))).

299. See supra Part I.B.2.b (noting distinction between injury to competitors and injury to competition in antitrust actions).

300. For example, below-cost promotional pricing by a new entrant is legal under section 2. See Williamson, supra note 192, at 324 ("Such promotions may be the only effective way to overcome customer habit in industries where the product is differentiated by manufacturers."); see also Jordan, supra note 133, at 270 ("[B]usiness managers . . . can use low prices, 'loss leaders,' or promotional discounts to increase their firm's market share without running afoul of the predatory pricing laws, so long as their business poses no threat of monopolizing the market in which it competes.").

301. See, e.g., Pool Water Prods. v. Olin Corp., 258 F.3d 1024, 1035 (9th Cir. 2001) ("Defendants managed only to drive prices down; they were never able to raise prices to supracompetitive levels."); 3B Areeda & Hovenkamp, supra note 75, ¶ 807, at 449 ("[W]hen challenged exclusionary conduct had ended three years earlier without increasing the defendant's market share or forcing the exit of any competitor, a court is likely to see no dangerous probability of success." (citing Ashkanazy v. I. Rokeach & Sons, Inc., 757 F. Supp. 1527 (N.D. Ill. 1991))).

The correct focus for section 2 analysis is market domination, not recoupment. Yet courts in predatory pricing cases sometimes confuse the two concepts by suggesting that they necessarily go together.[302] For example, the Eighth Circuit has articulated the recoupment requirement such that a defendant "'must be able to create a real possibility of both driving out a rival by loss-creating price cutting and then holding on to that advantage to recoup losses; in other words, the price-cutter must be able at least to threaten domination of the market.'"[303] This conflates two different concepts because a predatory firm could illegally monopolize the market without recouping its losses. Recoupment requires something more; it requires the ability to earn sufficient monopoly profits to make the whole venture a worthwhile expenditure of funds.

The confusion between market power and recoupment is particularly acute in attempted monopolization jurisprudence. Attempted monopolization claims require the plaintiff to prove that there is a dangerous probability of a defendant acquiring monopoly power through its anticompetitive conduct.[304] Pricing below cost does not implicate section 2 unless the conduct "threatens actual monopolization."[305] In cases not involving predatory pricing, courts have articulated this element of the attempted monopolization test as requiring the plaintiff to show a "dangerous probability of success"—success referring to successful acquisition of monopoly power.[306] Through a sleight of hand, the Supreme Court in

302. See, e.g., W. Parcel Express v. UPS, 65 F. Supp. 2d 1052, 1063 (N.D. Cal. 1998) ("[W]ithout market power, the predator's recoupment will be thwarted by competitors who will offer their services at prices below the predator's supra-competitive prices."); see also Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal & Prof'l Publ'ns, Inc., 63 F.3d 1540, 1554 (10th Cir. 1995) (linking recoupment and market power); Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1200–01 (3d Cir. 1995) (same).

303. Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc., 824 F.2d 582, 599 (8th Cir. 1987) (quoting Henry v. Chloride, Inc., 809 F.2d 1334, 1345 (8th Cir. 1987)).

304. See *Multistate Legal Studies*, 63 F.3d at 1554–56 (analyzing dangerous probability of success in attempt case).

305. Ind. Grocery, Inc. v. Super Valu Stores, Inc., 864 F.2d 1409, 1413–14 (7th Cir. 1989); see also Springfield Terminal Ry. Co. v. Canadian Pac. Ltd., 133 F.3d 103, 109 (1st Cir. 1997) ("[M]ere existence of predatory price cutting, and the extent of such conduct sufficient to justify a finding of dangerous probability of monopolization, are two quite different issues."); Wheeling-Pittsburgh Steel Corp. v. Mitsui & Co., 35 F. Supp. 2d 597, 601–02 (S.D. Ohio 1999) ("[T]he Sherman Act had been interpreted to prohibit cut-throat pricing only when such pricing posed 'a dangerous probability of actual monopolization.'" (quoting Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 455 (1993))).

306. See, e.g., Gulf States Reorg. Grp., Inc. v. Nucor Corp., No. 11-14983, 2013 U.S. App. LEXIS 14187, at *8 (11th Cir. July 15, 2013) ("A dangerous probability of success arises when the defendant comes close to achieving monopoly power in the relevant market."); E.I. du Pont de Nemours & Co. v. Kolon Indus., Inc., 637 F.3d 435, 441 (4th Cir. 2011) ("An attempted monopolization offense consists of: (1) the use of anticompetitive conduct; (2) with specific intent to monopolize; and (3) a dangerous probability of success."); Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 903 n.13

Brooke Group essentially redefined "success" as "recoupment."[307] Thus, the plaintiff must now show not only that the predator is dangerously close to acquiring monopoly power, but also that the defendant enjoys a dangerous probability of recouping its investment in predatory pricing. Since *Brooke Group*, lower courts have interpreted the legal test in predatory pricing claims to require a dangerous probability of recoupment.[308]

Yet an important distinction exists between a dangerous probability of achieving monopoly power and a dangerous probability of recoupment. Antitrust law does not care whether or not monopolists are profitable; it cares whether or not dominant firms are acquiring their monopoly power through anticompetitive conduct unrelated to efficiency or competition on the merits.[309] Predicting the probability of recoupment does not advance the goals of antitrust; in contrast, predicting the probability of monopolization is important because that will determine whether courts need to step in and prevent the creation of monopoly before it is too late.

The solution to this problem is simple: Treat predatory pricing claims like other section 2 claims. Focusing on monopoly power—instead of recoupment—in both monopolization and attempted monopolization cases is the correct approach for several reasons. First, such an approach more correctly addresses the *Brooke Group* factors.[310] Most of these factors—e.g., whether "the market is highly diffuse and competitive, . . . where new entry is easy, or the defendant lacks adequate excess capacity to absorb the market shares of his rivals and cannot quickly create or purchase new capacity"[311]—speak to monopoly power, not simply recoupment.[312] This muddles the antitrust analysis because the discussion about

(9th Cir. 2008) (noting there is no "liability for attempted monopolization unless the . . . elements of a specific intent to monopolize and dangerous probability of success are satisfied").

307. See Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224–25 (1993) (discussing dangerous probability of recouping, as opposed to dangerous probability of monopolizing relevant market).

308. See, e.g., Vollrath Co. v. Sammi Corp., 9 F.3d 1455, 1460 (9th Cir. 1993) (noting *Spectrum Sports* requires "'dangerous probability of achieving monopoly power'" but applying *Brooke Group* language of "'dangerous probability[] of recouping its investment in below-cost prices'" (alteration in *Vollrath*) (quoting *Brooke Group*, 509 U.S. at 224; *Spectrum Sports*, 506 U.S. at 447)).

309. See infra notes 374–384 and accompanying text (noting courts do not inquire into cost-effectiveness of acquisition of monopoly power outside predatory pricing context).

310. See *Brooke Group*, 509 U.S. at 225 (noting recoupment factors, including "extent and duration of the alleged predation, the relative financial strength of the predator and its intended victim, and their respective incentives and will").

311. Id. at 226.

312. See Bolton, Brodley & Riordan, Response, supra note 122, at 2507 ("[E]vidence of anticompetitive effects can establish market power."). The dangerous probability of monopolization element already examines the same factors that *Brooke Group* articulates as

barriers to entry is part of the first element of *Grinnell*: Does the defendant possess monopoly power?[313] Even in the absence of a recoupment requirement, courts must determine whether the absence of entry barriers precludes section 2 liability.[314] If barriers to entry are too low—and/or other factors of recoupment are not present—this probably means that the defendant does not have monopoly power or a dangerous probability of acquiring it. Thus, there is no liability, regardless of whether the defendant engaged in below-cost pricing.[315] But this analysis should take place in the evaluation of the monopoly power element, not through a convoluted recoupment requirement, which courts often get wrong.[316]

Second, focusing on monopoly power—instead of recoupment—reduces the risk of judicial mistakes. Courts have much experience determining whether a defendant has monopoly power (or a dangerous probability of acquiring it), but are not equally adept at predicting recoupment. The monopoly power element should suffice. The absence of monopoly power means that there is no illegal predatory pricing—not because there is no probability of recoupment but rather because there is no monopoly power, which is the first element of a monopolization claim under *Grinnell*.[317] Courts should focus on the monopoly power inquiry, something that they do relatively well compared to their recoupment analysis. Determining the presence—or future likelihood—of monopoly power is something that antitrust courts do routinely since this determination is relevant to all monopolization and attempted monopolization claims, not just predatory pricing claims. This element is an effective screen against false positives in predatory pricing claims.[318]

In sum, the monopoly power element is an appropriate filter for predatory pricing liability. Antitrust law cares about market power, not

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relevant to recoupment, including "a defendant's market share, whether the defendant is a multimarket firm, the number and strength of other competitors, market trends, and entry barriers." Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal & Prof'l Publ'ns, Inc., 63 F.3d 1540, 1554 (10th Cir. 1995).

313. If the cause of action is attempted monopolization, then the "barriers to entry" discussion should take place when applying the element of dangerous probability of the defendant achieving monopoly power.

314. See 3A Areeda & Hovenkamp, supra note 75, ¶ 724, at 42 ("[A]s *Brooke* and other Supreme Court decisions recognize, when entry barriers are not high, predation cannot be found on *any* price.").

315. See Lawrence J. White, Antitrust Activities During the Clinton Administration, *in* High-Stakes Antitrust, supra note 149, at 11, 27 (discussing *American Airlines* case, in which American was awarded summary judgment despite having lowered prices).

316. See supra Part II (discussing frequent judicial errors in recoupment analysis).

317. The same reasoning applies to the third element of an attempted monopolization claim under *Spectrum Sports*.

318. See Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2283 (describing market power screen as "most frequent grounds on which courts have dismissed predatory pricing suits without trial").

profitability. The probability of successfully monopolizing—not recouping—is the more appropriate standard. The former is easier to analyze and predict, is more relevant to antitrust's goal of preventing illegal monopolization, and fits within the antitrust framework for attempted monopolization claims. In contrast, the amount of money spent to acquire monopoly power is irrelevant. What matters is whether—through charging a predatory price—the defendant has either acquired monopoly power or created a dangerous probability of acquiring monopoly power. Proper application of the monopoly power screen should eliminate the need for the recoupment inquiry.[319]

2. *Price Below Cost.* — A predatory pricing plaintiff must prove that the defendant is charging a price below an appropriate measure of cost. That is the essence of predatory pricing.[320] The price-below-cost element protects against condemning healthy competition.[321] Those who express concern about false positives in predatory pricing incorrectly define a false positive as condemning predatory pricing when there was no probability of recoupment.[322] That is not a false positive. If a firm acquires monopoly power through predatory pricing regardless of the probability of recoupment, then antitrust liability is a true positive.[323]

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319. See Hovenkamp & Hovenkamp, supra note 285, at 539 ("None of this matters very much if we abandon the strict recoupment requirement altogether and adhere to some more basic structural principles—namely, that monopolization requires a market with high entry barriers and economies of scale that persist over high output ranges relative to demand at cost prices.").

320. There is, however, a robust scholarly debate concerning whether above-cost price cuts can constitute predatory pricing. Compare Aaron S. Edlin, Stopping Above-Cost Predatory Pricing, 111 Yale L.J. 941, 942 (2002) ("[T]here is no compelling reason to restrict predation cases to below-cost pricing, as above-cost pricing can also hurt consumers by limiting competition." (footnote omitted)), with Einer Elhauge, Why Above-Cost Price Cuts to Drive Out Entrants Are Not Predatory—and the Implications for Defining Costs and Market Power, 112 Yale L.J. 681, 827 (2003) ("[A]ntitrust law should not recognize any claim of above-cost predatory pricing.").

321. See, e.g., United States v. AMR Corp., 335 F.3d 1109, 1113–14 (10th Cir. 2003) (citing below-cost pricing as alleged anticompetitive conduct distinguishing pricing scheme from healthy competition); Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1198 (3d Cir. 1995) (discussing how above-cost but below-market prices do not harm competition); Arthur S. Langenderfer, Inc. v. S.E. Johnson Co., 917 F.2d 1413, 1440 (6th Cir. 1990) (expressing concern about condemning price cuts which merely stimulate healthy competition); Chillicothe Sand & Gravel Co. v. Martin Marietta Corp., 615 F.2d 427, 432 (7th Cir. 1980) (citing below-cost pricing as "relevant and an extremely useful factor in determining the presence of predatory conduct"); Laitram Mach., Inc. v. Carnitech A/S, 884 F. Supp. 1074, 1080–81 (E.D. La. 1995) (discussing how above-cost pricing only excludes less efficient competitors).

322. See supra Part I.B.1 (noting federal judges have interpreted recoupment requirement as proxy for below-cost pricing).

323. In contrast, it would be a false positive if courts were condemning a defendant for predatory pricing when the defendant was not a monopolist, not charging a price below cost, or not injuring competition.

The price-below-cost element is often a more efficient filter to reduce the risk of false positives than recoupment.[324] The fact that a dominant firm has priced below cost is strong evidence that the firm's decisionmakers have determined that recoupment is likely.[325] As Professors Areeda and Hovenkamp explain, "[i]nnocent firms do not ordinarily set prices below average variable cost, which entails both short-run and long-run losses. With only a few narrow exceptions, such prices are irrational unless they are intended to destroy or discipline rivals in anticipation of later monopoly prices."[326] A factual determination that the defendant used predatory pricing to acquire monopoly power is strong evidence that the party in the best position to evaluate the probabilities expected recoupment.

The recoupment requirement, however, sometimes nullifies the element of below-cost pricing. Courts use the recoupment element to prevent consideration of the core antitrust issues of whether the defendant charged a price below its costs and, if so, whether this harmed competition.[327] Using recoupment as a filter, once a judge decides that recoupment is unlikely, "the defendant is entitled to judgment as a matter of law regardless of whether it priced below its costs."[328] By treating recoupment as a threshold element that trumps other elements of a predatory pricing claim, courts have diminished the significance of the price-below-cost element, which is the definitional element of predatory pricing. For example, Judge Easterbrook in *Rose Acre* used recoupment as a filter to avoid the price-below-cost inquiry *even though* the defendant charged a price below cost in order to drive the plaintiff from the market.[329] Courts have sought to limit the plaintiff's discovery to issues of recoupment, suggesting that discovery on price-cost issues should not be allowed until

324. See 3A Areeda & Hovenkamp, supra note 75, ¶ 724, at 38 ("Recoupment and price/cost relationships are 'alternative' screening devices, and the latter may often provide a quicker resolution of the case."); Denger & Herfort, supra note 52, at 558 ("[C]lear cost-related standards may be more susceptible to speedy resolution than such issues as market definition and market shares, entry and capacity factors . . . . [P]rompt resolution of the cost-related issues through articulation of clearly defined . . . standards may serve the purposes articulated in *Brooke Group* even more effectively . . . .").

325. See 3A Areeda & Hovenkamp, supra note 75, ¶ 724, at 38 ("When a price is clearly below average variable cost (or marginal cost) with no adequate alternative explanation, the firm's managers have calculated that such a payoff was worth the risk. No court is in a better position to make this calculation than the firms' managers themselves.").

326. Id. ¶ 727, at 96 (footnote omitted).

327. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224–25 (1993) (focusing on recoupment rather than existence and effects of defendant's below-cost pricing).

328. Austin, supra note 85, at 898.

329. A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1398 (7th Cir. 1989) (noting expert evidence of below-cost pricing).

the plaintiff can establish probability of recoupment.[330] In some instances, courts have reasoned that "if the market structure renders recoupment of profits lost during the price cut phase difficult or risky, it may be unlikely that the seller's price cut is predatory."[331] This is backwards logic, because if the price is below cost, then it is entirely inappropriate to use the probability of recoupment as a proxy for whether the price was, in fact, predatory. If anything, the inference should go the other direction: In the presence of proof of below-cost pricing, courts should presume the probability of recoupment because a rational firm would not incur the loss unless it reasonably expected to recoup.

The pricing-below-cost element is not without problems, chief of which remains a lack of uniformity as to the appropriate measure of cost for predatory pricing claims. Courts and commentators have devoted much ink to what precisely constitutes "below-cost pricing."[332] Unfortunately, the Supreme Court has ducked the issue all three times that it has been presented to the Court.[333] Most circuits use average variable cost as their measure.[334] A Supreme Court declaration of a single measure of cost for predatory pricing purposes would bring needed clarity to predatory pricing law.[335] Until then, whatever the measure of cost, the plaintiff must prove below-cost pricing with evidence, not "theoretical speculation that a defendant is pricing below that measure."[336] The price-below-cost element is not a perfect filter,[337] but it does not need to be because the other elements discussed in this section also help screen out false positives.

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330. See 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 54 (noting court in Rebel Oil Co. v. Atl. Richfield Co., 133 F.R.D. 41 (D. Nev. 1990), limited initial discovery to market structure, excluding below-cost pricing from discovery).

331. Irvin Indus., Inc. v. Goodyear Aerospace Corp., 974 F.2d 241, 244 (2d Cir. 1992); see also *Rose Acre*, 881 F.2d at 1401 ("The investment must be recouped. If a monopoly price later is impossible, then the sequence is unprofitable and we may infer that the low price now is not predatory.").

332. See, e.g., William J. Baumol, Predation and the Logic of the Average Variable Cost Test, 39 J.L. & Econ. 49, 59 (1996) (discussing variability in defining average variable cost).

333. See Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224–26 (1993); Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 117–18 n.12 (1986); Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 584–85 n.8 (1986).

334. 1 Am. Bar Ass'n Section of Antitrust Law, Antitrust Law Developments 278 (7th ed. 2012) (attributing courts' preference for variable costs, rather than marginal costs, to relative ease of calculation).

335. If courts could agree on the appropriate measure of cost, including what properly constitutes a cost, then it would be easier to determine the cost element directly, rather than rely on the recoupment element.

336. Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1198 (3d Cir. 1995).

337. See Baker, supra note 125, at 587–88 ("If cost is measured incorrectly, a firm pricing at or above cost might nevertheless appear to price below cost. This possibility cannot be dismissed, given the difficult conceptual and measurement issues surrounding the definition of cost." (footnote omitted)).

3. *Predatory Intent.* — Where applicable, an intent requirement insures that the plaintiff must prove that the defendant is charging a price below cost in order to eliminate its competitors altogether and to act like a monopolist in the aftermath. The Supreme Court has not explicitly endorsed this element for predatory pricing claims. In *Cargill*, however, the Court defined predatory pricing as pricing below cost "for the *purpose* of eliminating competitors in the short run and reducing competition in the long run."[338] Although the Supreme Court did not list intent as a requirement in either *Matsushita* or *Brooke Group*, some courts have imposed this burden on plaintiffs alleging predatory pricing.[339] For example, the Fifth Circuit has opined that "[p]redatory pricing differs from healthy competitive pricing in its motive: a predator by his pricing practices seeks 'to impose losses on other firms, not garner [sic] gains for itself.'"[340]

Some judges denigrate the intent element. In his influential *Rose Acre* opinion, Judge Easterbrook held that "the defendant's state of mind [is] irrelevant."[341] He rejected predatory intent as an element in predatory pricing cases because it is merely the "drive to succeed [that] lies at the core of a rivalrous economy."[342] Economist John McGee argued that intent was irrelevant because only effects matter.[343] But this suggests that

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338. *Cargill*, 479 U.S. at 117 (emphasis added).

339. See, e.g., McGahee v. N. Propane Gas Co., 858 F.2d 1487, 1503 (11th Cir. 1988) ("To withstand judgment as a matter of law, plaintiff must have other evidence, either objective or subjective, of predatory intent."); Richter Concrete Corp. v. Hilltop Concrete Corp., 691 F.2d 818, 823 (6th Cir. 1982) (noting courts have adopted cost-based tests to determine presence of anticompetitive intent); Helmac Prods. Corp. v. Roth (Plastics) Corp., 814 F. Supp. 560, 566 (E.D. Mich. 1992) (attributing "intent to restrain or monopolize trade or commerce in the United States" requirement to antidumping statute). Not every circuit currently requires the plaintiff to prove a specific intent to destroy competition. See, e.g., A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1402 (7th Cir. 1989) ("[W]e now hold that intent is not a basis of liability (or a ground for inferring the existence of such a basis) in a predatory pricing case under the Sherman Act.").

340. Malcolm v. Marathon Oil Co., 642 F.2d 845, 853–54 (5th Cir. Unit B Apr. 1981) (quoting Lawrence Anthony Sullivan, Handbook of the Law of Antitrust 111 (1977)) (misquotation).

341. *Rose Acre*, 881 F.2d at 1401. Evidence of predatory intent included the president of the defendant calling the president of one of the plaintiffs and announcing, "We are going to run you out of the egg business. Your days are numbered." Id. at 1398 (internal quotation marks omitted). For further analysis of this aspect of the case, see Goldstein, supra note 81, at 1768 ("Intent was a particularly thorny issue in this case because plaintiffs presented strong and direct evidence that Rose Acre Farms intended to drive its competitors out of business."); id. at 1768–69 n.78 ("Rose Acre's treasurer also admitted that its costs of production had nothing to do with the selling price of its eggs, explaining that pricing below cost 'is the way to win in the long run.'" (quoting *Rose Acre*, 881 F.2d at 1398–99)).

342. *Rose Acre*, 881 F.2d at 1402.

343. McGee, Revisited, supra note 20, at 292.

courts should not consider recoupment, which tells us little about the effects on consumers of post-predation monopoly pricing. Instead, the recoupment element asks whether post-predation losses outweigh consumer gains during the predatory period.

The recoupment element can interfere with the intent element. Like Judge Easterbrook, the Court in *Brooke Group* essentially reasoned that evidence of predatory intent is irrelevant if the judge perceives recoupment as unlikely. The majority opined:

> [T]he record contains sufficient evidence from which a reasonable jury could conclude that Brown & Williamson envisioned or intended this anticompetitive course of events. There is also sufficient evidence in the record from which a reasonable jury could conclude that for a period of approximately 18 months, Brown & Williamson's prices on its generic cigarettes were below its costs, and that this below-cost pricing imposed losses on Liggett . . . . [However,] Liggett has failed to demonstrate . . . that in pursuing this scheme, Brown & Williamson had a reasonable prospect of recovering its losses from below-cost pricing through slowing the growth of generics. . . .
>
> No inference of recoupment is sustainable on this record, because no evidence suggests that Brown & Williamson—whatever its intent in introducing black and whites [generics] may have been—was likely to obtain the power to raise the prices for generic cigarettes above a competitive level.[344]

This view of predatory intent is shortsighted because intent evidence may show that the business calculated that there was a likelihood of recoupment. Firms are in a better position to make predictions about recoupment than federal judges who know little about the workings of the particular industry.[345] For example, the documentary evidence in *Brooke Group* showed B&W's predatory intent, including its recoupment calculations.[346]

Still, some courts belittle the notion of "predatory intent" as an element, protesting "the futility in attempting to discern predatory conduct

344. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 231–32 (1993) (citations omitted); see also Rebel Oil Co. v. Atl. Richfield Co., 146 F.3d 1088, 1097 (9th Cir. 1998) ("If intent cannot substitute for the required element of recoupment, it likewise cannot establish an antitrust violation in the absence of evidence of below-cost pricing.").

345. See supra notes 325–326 and accompanying text (noting discrepancy between business knowledge of companies' leadership and judges and therefore arguing for less stringent recoupment test).

346. Liggett Grp., Inc. v. Brown & Williamson Tobacco Corp., 748 F. Supp. 344, 354 (M.D.N.C. 1990), aff'd, 964 F.2d 335 (4th Cir. 1992), aff'd sub nom. *Brooke Group*, 509 U.S. 209; see also Kenneth L. Glazer, Predatory Pricing and Beyond: Life After *Brooke Group*, 62 Antitrust L.J. 605, 611–13 (1994) ("[T]he evidence made clear that . . . B&W . . . outlined how a firm with only 12 percent of the market could engage in successful predation.").

solely through evidence of a defendant's 'predatory intent.'"[347] This reasoning is a red herring created by treating a single element as if it were the test for liability unto itself. This view would be persuasive if predatory intent were the "sole" element necessary to prove predatory conduct. But, of course, predatory intent alone does not give rise to liability.[348] A claim for predatory pricing has many elements, as discussed in this section. Predatory intent works well in tandem with these other elements to distinguish good price cutting from anticompetitive price cutting and to reduce the risk of false positives.[349]

4. *Causal Antitrust Injury.* — Finally, a private plaintiff must prove causal antitrust injury. She must show that she has suffered an injury as a result of the defendant's antitrust violation.[350] This causation element can stop false positives.[351] If the alleged below-cost pricing does not cause an anticompetitive effect that inflicts antitrust injury on a proper plaintiff, then antitrust liability will not attach.

Competitors and consumers suffer their antitrust injury sequentially. The excluded competitors suffer antitrust injury during the predation period. When the targeted rival suffers lost sales or is driven from the market because of price predation, the lost profits are a form of antitrust injury, so long as the predatory firm is injuring competition in the market overall.

Consumers suffer their antitrust injury in the post-predation period, after the defendant has acquired monopoly power through predatory pricing and is charging a monopoly price. The higher price in the post-predation period reflects the new monopolist's attempt to recoup some

347. Morgan v. Ponder, 892 F.2d 1355, 1359 (8th Cir. 1989) (emphasis added); see also Int'l Travel Arrangers v. NWA, Inc., 991 F.2d 1389, 1395 (8th Cir. 1993) (quoting *Morgan*, 892 F.2d at 1359).

348. See, e.g., Hayes v. T.G. Solomon, 597 F.2d 958, 977–78 (5th Cir. 1979) ("A statement of intent to compete, however, even if perceived as a threat, is not unlawful. Such a manifestation of intent to triumph in the competitive market, in the absence of unfair, anti-competitive or predatory conduct, is not enough to establish an antitrust violation."). It is important to apply the intent element correctly. See William S. Comanor & H.E. Frech III, Predatory Pricing and the Meaning of Intent, 38 Antitrust Bull. 293, 302 n.30 (1993) ("As a casual look at the business trade press will show, businessmen often use sports or military language. Thus, aggressive memos are expected. Finding such documents, without more, is not necessarily evidence of predatory intent.").

349. See Goldstein, supra note 81, at 1790 ("For example, using subjective evidence of intent to supplement objective evidence such as below-cost pricing reduces the risks of misinterpreting either the intent or the cost figures.").

350. See, e.g., Marsann Co. v. Brammall, Inc., 788 F.2d 611, 613 (9th Cir. 1986) ("Under a claim of attempted monopolization by predatory pricing, a plaintiff must prove . . . causal antitrust injury.").

351. See Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2269 ("Under *Brooke* and *Matsushita*, proof of an injury to competition, actual or probable, is an essential element of a predatory pricing case."); Hay, supra note 116, at 362 ("Pricing is predatory if and only if it has an anticompetitive effect.").

of its prior investment in predatory pricing.[352] The public suffers antitrust injury whether or not the defendant is charging a sufficiently high price to recoup its investment in predatory pricing.[353]

The recoupment inquiry has distorted the element of causal antitrust injury. The *Brooke Group* Court held:

> If circumstances indicate that below-cost pricing could likely produce its intended effect on the target, there is still the further question whether it would likely injure competition in the relevant market. The plaintiff must demonstrate that there is a likelihood that the predatory scheme alleged would cause a rise in prices above a competitive level that would be sufficient to compensate for the amounts expended on the predation, including the time value of the money invested in it.[354]

The Court failed to recognize that raising "prices above a competitive level" is sufficient to show antitrust injury; the additional requirement that the monopoly profits would likely "be sufficient to compensate for the amounts expended on the predation" simply protects illegal monopolists.[355] It does not matter whether this act of charging the monopoly price will actually result in the new monopolist recovering its entire investment in predatory pricing; the current consumer paying the higher-than-competitive price will suffer an antitrust injury that was the direct and intended result of the defendant's predatory conduct.

The causal antitrust injury requirement helps to distinguish between legitimate and illegitimate price cutting by ensuring that the plaintiff was actually injured by the predatory pricing. The recoupment requirement distorts the analysis by shifting focus from the victim's injury to the predator's profits. Further, it obscures the fact that the antitrust injury can occur in markets besides the precise market in which the price predation took place.[356]

5. *Legitimate Business Justifications.* — Finally, in addition to the above elements, which serve as filters against false positives, predatory pricing

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352. Professor Areeda recognized this injury in his argument before the *Brooke Group* Court. See Oral Argument at 19:54, Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993) (No. 92-466), available at http://www.oyez.org/cases/1990-1999/1992/1992_92_466#argument (on file with the *Columbia Law Review*) ("The fact that the generic segment grew in size is, I suggest, more a response to the explosion in prices that came, rather than anything else. It is that explosion in prices that demonstrates the injury to consumers.").

353. Also, the public suffers antitrust injury from reduced choice even if the defendant does not recoup its losses.

354. *Brooke Group*, 509 U.S. at 225.

355. I say "illegal" monopolists in the sense that their monopolies were not earned through greater efficiency or other competition on the merits.

356. See supra Part II.B.1–2 (explaining recoupment in other markets); see also Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2267–68 ("By logical extension, the injury to competition and consumers may occur in either the predatory market or in a strategically related market where the effects of the predation are felt.").

defendants can avoid liability by arguing that they had a legitimate business justification for their pricing strategy. If an antitrust plaintiff is able to present a prima facie section 2 case, the defendant "may proffer a 'procompetitive justification' for its conduct," which is "a nonpretextual claim that its conduct is indeed a form of competition on the merits because it involves, for example, greater efficiency or enhanced consumer appeal."[357] This business justification defense exists for predatory pricing claims.[358] Examples of possible legitimate business justifications for charging a price below cost include: "(1) compensating buyers for taking the risk of buying a new product; (2) expanding demand to a level which will allow the entrant to achieve scale economies; and (3) keeping prices at competitive levels, expecting costs to decline because of the 'learning curve' phenomenon."[359] Predatory pricing defendants can also argue that they were just "meeting competition."[360]

The business justification defense helps distinguish illegal predatory pricing from competition on the merits. Professors Bolton, Brodley, and Riordan explain:

> [The] business justification or efficiencies defense serves as a means of eliminating cases where below-cost pricing by a firm with market power is likely to be welfare-enhancing, rather than predatory. In these cases, the sacrifice of present profits through low pricing is justified for reasons other than exclusion or disciplining of rivals.[361]

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357. United States v. Microsoft Corp., 253 F.3d 34, 59 (D.C. Cir. 2001) (per curiam).

358. See, e.g., Stearns Airport Equip. Co. v. FMC Corp., 170 F.3d 518, 522 (5th Cir. 1999) ("The key factor courts have analyzed in order to determine whether challenged conduct is or is not competition on the merits is the proffered business justification for the act.").

359. Carstensen, supra note 53, at 960; see also Great Atl. & Pac. Tea Co. v. Ervin, 23 F. Supp. 70, 80 (D. Minn. 1938) (per curiam) ("A sudden necessity of paying claims of importunate creditors might furnish a reason for sales at less than cost plus overhead."); Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2278 (identifying "promotional pricing, learning-by-doing, and network externalities" as "three types of market-expanding efficiency defenses").

360. See Richter Concrete Corp. v. Hilltop Concrete Corp., 691 F.2d 818, 826 (6th Cir. 1982) ("It is not anticompetitive for a company to reduce prices to meet lower prices already being charged by competitors."); ILC Peripherals Leasing Corp. v. IBM, 458 F. Supp. 423, 433 (N.D. Cal. 1978) ("A company should not be guilty of predatory pricing, regardless of its costs, when it reduces prices to meet lower prices already being charged by its competitors."); United States v. Am. Optical Co., 39 F.R.D. 580, 584 (N.D. Cal. 1966) (noting predatory pricing "defendants are entitled to show that their pricing policies were established, not from predatory motives, but for legitimate business purposes, including the purpose of meeting competition"). But see United States v. AMR Corp., 335 F.3d 1109, 1120 n.15 (10th Cir. 2003) ("The Supreme Court has never mentioned the possibility of such a defense under the Sherman Act. We therefore decline to rule that the 'meeting competition' defense applies in the § 2 context.").

361. Bolton, Brodley & Riordan, Predatory Pricing, supra note 8, at 2274 (footnote omitted).

If below-cost pricing is truly defensive or efficient under the circumstances of the case, the business justification defense precludes antitrust liability.[362]

In short, the business justification defense serves to prevent false positives, and could continue to do so in the absence of a recoupment requirement.

6. *Summary.* — Eliminating the recoupment requirement should not meaningfully increase the risk of false positives. In general, whenever any element is added to a cause of action, the probability of false positives decreases because every element increases the likelihood that the defendant will win, rightly or wrongly. However, the prima facie elements and the defenses in predatory pricing cases are sufficient filters against false positives. Furthermore, eliminating the recoupment requirement does not represent the wholesale elimination of one element. Rather, it is the mere restoration of an existing element—monopoly power—so that it more accurately reflects the purposes of antitrust law. Antitrust law does not care whether or not a monopolist increases its net profitability. It cares whether a monopolist acquires its power legitimately.

B. *Reducing False Negatives*

Courts in all areas of law must balance the risk of false positives against the risk of false negatives. While the recoupment requirement reduces the risk of false positives, it increases the risk of false negatives. False negatives are also to be avoided. Failure to condemn illegal activity can encourage it. In the context of antitrust law, false negatives undermine deterrence of anticompetitive conduct, which creates inefficiency and hurts consumers. In predatory pricing cases, false negatives mean that efficient firms driven from the market and consumers forced to pay monopoly prices have no recourse.

Supporters of the recoupment requirement incorrectly believe that false negatives are not a problem in predatory pricing litigation. The recoupment requirement is based on the premise that predatory pricing does not happen.[363] Some courts presume that predatory pricing does

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362. See id. at 2276 ("The courts have generally upheld most types of defensive below-cost pricing as compelled by competition.").

363. See Kwoka & White, Economic and Legal Context, supra note 120, at 180–83 (outlining argument "true predation is considerably less common than alleged" and "may be quite rational"); Trujillo, supra note 9, at 820 ("The Court's recoupment standard is premised upon the theory that 'predatory pricing schemes are rarely tried, and even more rarely successful,' and, as a result, the prerequisites to recovery are purposefully difficult to establish." (footnote omitted) (quoting Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986))); see also Craswell & Fratrik, supra note 108, at 2 ("[A]uthors who view predatory pricing as being extremely rare take a very different view from those who believe it to be a more common problem.").

not occur.[364] But predatory pricing does happen.[365] Ironically, the case in which the Supreme Court announced the recoupment requirement represents one of the most visible false negatives. *Brooke Group* held that the alleged predatory pricing must not have occurred because recoupment was implausible.[366] Yet, the evidence at trial shows that after engaging in below-cost pricing for eighteen months to force Liggett to raise its prices,[367] Brown & Williamson succeeded in raising the prices of both generic and branded cigarettes, profiting handsomely.[368]

The recoupment requirement creates false negatives, in part, because courts are not adept at predicting recoupment. Reliance on recoupment leads courts to incorrectly conclude that predation has not taken place. In the hands of judges unversed in the mechanics of competition and predation, recoupment presents an impossible-to-satisfy element in some courtrooms.[369] As Professors Areeda and Hovenkamp have explained:

> One downside of requiring proof of recoupment is that firms operating in markets where recoupment is thought impossible have a safe harbor. Once a market is observed to have low entry barriers or sufficient competition to make disciplined oligopoly unlikely, then any price in that market becomes lawful so far as federal antitrust is concerned. Firms in such markets are free to injure their rivals with unreasonably low prices.[370]

In short, by making the probability of recoupment too hard to prove, courts are encouraging anticompetitive conduct.[371]

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364. See, e.g., Advo, Inc. v. Phila. Newspapers, Inc., 51 F.3d 1191, 1196 (3d Cir. 1995) ("*Matsushita*... created a legal presumption, based on economic logic, that predatory pricing is unlikely to threaten competition." (emphases omitted)); Stitt Spark Plug Co. v. Champion Spark Plug Co., 840 F.2d 1253, 1255 (5th Cir. 1988) ("The [*Matsushita*] Court... [held] that the economic disincentives to predatory pricing often will justify a presumption that an allegation of such behavior is implausible.").

365. See, e.g., Springfield Terminal Ry. Co. v. Canadian Pac. Ltd., 133 F.3d 103, 105–06 (1st Cir. 1997) (describing railroad's below-cost bid as "predatory pricing incident"); Bolton, Brodley & Riordan, Response, supra note 122, at 2505 (citing examples); Rapp, supra note 117, at 596 (same).

366. Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 243 (1993) ("Brown & Williamson had no reasonable prospect of recouping its predatory losses and could not inflict the injury to competition the antitrust laws prohibit.").

367. Id. at 231 ("There is also sufficient evidence in the record from which a reasonable jury could conclude that for a period of approximately 18 months, Brown & Williamson's prices on its generic cigarettes were below its costs . . . .").

368. See supra notes 162–166 and accompanying text.

369. See Fox, supra note 73, at 607 ("[R]efusing to allow these findings, even though the jury had reached them at trial, further evidences the [*Brooke Group*] Court's adoption of a burden of proof that makes a finding of recoupment all but impossible.").

370. 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 50.

371. See Hovenkamp, Antitrust Enterprise, supra note 231, at 161 ("Second, while an overly aggressive predatory pricing law deters some legitimate conduct, complete nonenforcement encourages anticompetitive conduct."). The problem of false negatives

C. *Recoupment Is Irrelevant to Anticompetitive Effects*

The anticompetitive effects of predatory pricing—inefficiency and exclusion—exist independently of the monopolist's profitability. A predator may become a monopolist but not recoup its investment in predatory pricing. For example, the monopolist may have inaccurately predicted how long it would take to drive its competitors from the market and the monopoly price may be insufficient to recoup all of the greater-than-anticipated losses.[372] Or, the monopolist may have wrongly forecast the monopoly price. For instance, a predator could price below cost and sustain losses in anticipation that the monopoly price will be $100. If it later turns out that the monopoly price is $90, the predator may find that it is a monopolist but cannot recoup its entire investment in predation.[373]

For other section 2 causes of action, courts do not generally ask whether the monopolist paid an irrationally high price to acquire its monopoly. The antitrust defendant cannot argue that it is not liable because it paid too much to drive its competitors out of the market. Three examples should suffice. First, in *Lorain Journal*, the Supreme Court condemned a local newspaper's attempted monopolization of the advertising market by threatening its advertisers that it would cease doing business with them if they also bought advertising on the new local radio station.[374] The Court never suggested that if the Lorain Journal lost money on its gamble, then the company would not face antitrust liability. In *American Can*, the defendant acquired its monopoly power by purchasing the factories of its competitors.[375] It paid several times the market value for these factories and then destroyed many of them without even inspecting them first.[376] The district court held that American Can's conduct violated section 2 without asking whether or not the monopoly profits that American Can received outweighed the millions of dollars it spent acquiring that monopoly power through its aggressive acquisition

could be addressed either by making recoupment easier to prove or by eliminating the recoupment requirement altogether. Because, as Part IV.C, infra, argues, recoupment is irrelevant to anticompetitive effects, the latter is arguably the better course of action.

372. See Bolton, Brodley & Riordan, Response, supra note 122, at 2512–13 n.98 ("A predatory campaign may last longer than the predator anticipated, resulting in net losses . . . .").

373. Alternatively, the predator may simply be irrational, without ever having a reasonable probability of recoupment despite attaining monopoly status. See 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 48 ("[B]y making a showing of recoupment essential to predation claims, antitrust . . . limits condemnation . . . to those circumstances where the defendant was acting rationally. . . . [R]ivals can be injured by the irrationally motivated predatory pricing campaign just as much as the rational one. Why should they be denied recovery for the former?").

374. Lorain Journal Co. v. United States, 342 U.S. 143, 152–55 (1951).

375. United States v. Am. Can Co., 230 F. 859, 868–70 (D. Md. 1916).

376. Id. at 870–71.

campaign.[377] Similarly, in *Aspen Skiing*, the monopolist drove its sole rival from the market by refusing to accept profitable vouchers issued by its rivals, but the Court did not require that Skiing Co. recoup the cost of its anticompetitive act of refusing the vouchers.[378] In short, courts do not consider the profitability of defendant's monopoly conduct in other contexts.[379]

Courts are wise not to inquire as to whether the section 2 defendant made deft decisions: The inquiry is irrelevant. Courts should not ask whether or not the monopolist achieved its monopoly power in a cost-effective or net-profitable manner. It is cold comfort to the consumer forced to purchase from a monopolist that the monopolist is not recouping its investment in illegal exclusion.

Failure to profit should not be a defense to section 2 liability. This is particularly true with attempted monopolization claims because, by definition, the predator has not succeeded.[380] Antitrust law does not generally recognize an unprofitability defense. For example, the Supreme Court noted in *United States v. Falstaff Brewing Corp.* that "the test in § 7 [of the Clayton Act] cases is not whether anticompetitive conduct is profit maximizing."[381] As Professors Areeda and Hovenkamp note in their treatise, "[t]he law embodies no *general* principle that the legal system should not punish business conduct simply because the conduct is

377. Id. at 901–04.

378. Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 605–11 (1985).

379. See, e.g., 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 49 ("[I]n cases alleging monopolization by improper patent infringement litigation, the law does not require a showing that the value of any anticipated monopoly exceeds the cost of maintaining the wrongful suit." (footnote omitted)). The primary exception is predatory bidding. Relying on its predatory pricing jurisprudence, the Supreme Court has imposed a similar recoupment requirement in cases of predatory bidding. See Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 549 U.S. 312, 318–21 (2007) (applying *Brooke Group* analysis to predatory bidding). This makes the exploration of the recoupment requirement more important, as what was once an anomaly in predatory pricing law risks distorting other areas of antitrust law.

380. See Taylor Publ'g Co. v. Jostens, Inc., 216 F.3d 465, 474 (5th Cir. 2000) ("[A]ttempted monopolization claim necessarily involves conduct which has not yet succeeded . . . ."); Multiflex, Inc. v. Samuel Moore & Co., 709 F.2d 980, 990 (5th Cir. 1983) ("Attempted monopolization under section 2 is usually defined as an unsuccessful attempt to achieve monopolization."), abrogated in part by Deauville Corp. v. Federated Dep't Stores, Inc., 756 F.2d 1183 (5th Cir. 1985).

381. 410 U.S. 526, 572 (1973) (Marshall, J., concurring in the judgment) (discussing section 7 of the Clayton Act, which governs mergers); see also Greene v. Gen. Foods Corp., 517 F.2d 635, 646 (5th Cir. 1975) ("In any event, the degree of profitability or its lack resulting from an alleged antitrust violation should play no part in the determination whether the plaintiff's suit should be barred on equitable grounds."); cf. Robert L. Hubbard, Grunts, Winks, & Nods: What Meets the Agreement Element of a Section 1 Claim?, 5 Sedona Conf. J. 99, 101–02 (2004) ("Section 1 does not require the defendant to profit. Murder, jay-walking, and pollution need not be profitable (or even economically rational) to be illegal, and neither should unreasonable restraints on trade.").

unprofitable to the defendant."[382] This principle applies across business law more broadly.[383]

Through the recoupment requirement, antitrust law has lost its focus in predatory pricing law. Interpreted properly, antitrust law does not care whether or not anticompetitive conduct is profitable; it cares whether or not anticompetitive conduct reduces consumer welfare. Anticompetitive conduct can simultaneously reduce consumer welfare without increasing a predator's profits, as when the monopolist overspends to acquire its monopoly power. Even if the monopolist does not recoup, consumers forced to pay the monopoly price during the so-called recoupment phase suffer the same antitrust injury.[384] A lack of recoupment does not negate the anticompetitive effects of predatory pricing. Predatory pricing that succeeds in achieving monopoly power but fails to recoup is, in fact, harmful. It still inflicts antitrust injury on the excluded competitors and on consumers forced to pay a monopoly price in the post-predation phase.

D. *Eliminating the Recoupment Requirement Conserves Judicial Resources*

While Judge Easterbrook justified the recoupment requirement as efficient, the inquiry does not save judicial resources. Indeed, it complicates the antitrust analysis.[385] First, it requires parties and judges to obtain and evaluate data that is inherently complex.[386] The recoupment requirement asks courts to estimate the monopoly profits likely associated with future monopolization and then to discount those profits to the net present value of that stream of money in order to compare it to the stream of losses incurred during the period of predation. This in turn requires the court to determine the discount rate that should be applied, including whether the discount rate should be fixed or variable. This requires an additional degree of complication that is not present in any other an-

382. 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 48.

383. Other areas of law do not tie liability to profitability. If a pharmaceutical company spends $500 million to promote a drug that it knows is unsafe, that firm can be held liable in a subsequent fraud lawsuit even if it spent more on promotion than it made in sales.

384. See Edlin & Farrell, supra note 81, at 518 (noting "unprofitable predatory scheme could be harmful"). Furthermore, antitrust cares about the acquisition and maintenance of monopoly power even if the monopolist does not charge a monopoly price. See United States v. Aluminum Co. of Am., 148 F.2d 416, 427 (2d Cir. 1945) ("[I]t is no excuse for 'monopolizing' a market that the monopoly has not been used to extract from the consumer more than a 'fair' profit.").

385. See Goldstein, supra note 81, at 1781 ("[R]ecoupment analysis is actually quite complex."); id. at 1782 ("Easterbrook's assertion that determining the probability of recoupment is 'easy' is inaccurate.").

386. See Bolton, Brodley & Riordan, Response, supra note 122, at 2512 ("Proof of recoupment can be exceedingly difficult and costly if it requires detailed quantitative evidence that the predator has actually recouped its losses or is likely to do so.").

titrust cause of action. Some courts require that the plaintiff prove that the defendant can recoup its up-front losses plus interest.[387] This complicates the analysis even further since much of the information necessary to perform the recoupment calculation is difficult to get.[388]

Second, the recoupment element necessitates more experts and concomitant speculation.[389] Professors Areeda and Hovenkamp note how "an overly strict [recoupment] requirement can involve experts in unwarranted speculation in even moderately close cases and even require predictions about future technologies or customer preferences."[390] Because courts are not particularly adept at making these predictions,[391] the inquiry into recoupment—even with this battle of expert witnesses—is fraught with peril.

Removing the recoupment requirement could make predatory pricing litigation more efficient by removing debate and deliberation over this unnecessary inquiry.

CONCLUSION

Courts adopted the recoupment requirement because they confused why a predator would price below cost with why predatory pricing is anticompetitive. These are, however, separate issues. Antitrust law condemns monopolization through predatory pricing because it allows a monopolist to acquire market power for reasons unrelated to efficiency. Predatory pricing is exclusionary regardless of whether the monopolist recoups. If courts insist on requiring proof of recoupment, then at a minimum judges need to better appreciate the many ways in which a monopolist can recoup its investment in below-cost pricing. Further, courts should reconsider whether recoupment should be an element at all.

Every element in any antitrust legal test should serve a purpose. The primary goal for each element in a section 2 monopolization cause of action should be to separate anticompetitive conduct from procompeti-

387. See Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal & Prof'l Publ'ns, Inc., 63 F.3d 1540, 1556 (10th Cir. 1995) (noting jury question exists as to whether defendant could "maintain that monopoly long enough to recoup any predatory pricing losses plus interest").

388. See 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 52 (noting recoupment calculation requires knowledge of size of post-predation market share and "market's price elasticity of demand," as well as "accurate predictions about the time new entry will take, the ability of surviving rivals to expand their output, or of customers to identify substitutes").

389. See Wagle, supra note 74, at 102 ("Prosecutors and courts alike will be operating with less than full information concerning, for example, a firm's costs, its financial reserves, and barriers to re-entry or subsequent new entry.").

390. 3A Areeda & Hovenkamp, supra note 75, ¶ 725, at 50.

391. See supra Part II (noting courts tend to make mistakes when applying recoupment requirement).

tive (or competitively benign) conduct. Elements that increase the plaintiff's burden without helping to distinguish between exclusionary and efficient behavior simply make it harder to establish liability and, thus, may protect anticompetitive conduct.

Unfortunately, as the common law of antitrust has evolved, courts have sometimes created elements that are unnecessary and counterproductive. The recoupment requirement in predatory pricing litigation is a case in point. The recoupment requirement does not distinguish between anticompetitive and benign (or beneficial) conduct. Antitrust law punishes conduct because it is anticompetitive, not because it is profitable. Recoupment makes predatory pricing profitable, but it does not make predation anticompetitive. Predatory pricing can be anticompetitive and reduce consumer welfare even in the absence of recoupment. This makes recoupment an inappropriate element for an antitrust violation.

The proper inquiry is the probability that the defendant will acquire or maintain monopoly power through predatory pricing, not whether the defendant will recoup the money it spent to obtain that monopoly power.

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