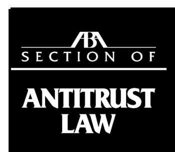

THE PRICE POINT

NEWSLETTER OF THE
ABA SECTION OF ANTITRUST LAW PRICING CONDUCT COMMITTEE

VOLUME 8, ISSUE 3 FALL 2009

We are pleased to bring you this issue of Pricing Conduct Committee's newsletter. It includes an examination of China's new anti-monopoly regime by Jonathan Palmer; Mark Lawson and Devin Dolive discuss geographic market definition in secondary-line price discrimination cases under the Robinson-Act, and Alberto Alemanno and Marco Ramondino provide an analysis of the European Court of Justice's recent decision on a recoupment requirement for predatory pricing claims in the EU.

If you have comments or questions about THE PRICE POINT, or if you are interested in submitting an article, please contact the Editor, Deborah Croyle, at dcroyle@orrick.com, or Committee Vice-Chair Scott Westrich at swestrich@orrick.com.

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NEW & NOTEWORTHY

Md. Code Ann., Comm. Law § 11-204(b) (eff. Oct. 1, 2009). The Maryland Antitrust Act is now amended to specify that "a minimum price below which a retailer, wholesaler, or distributor may not sell a commodity or service is an unreasonable restraint of trade or commerce," in effect repealing *Leegin Creative Leather Products Inc. v. PSKS Inc.*, 551 U.S. 877 (2007) for purposes of Maryland antitrust law.

Camarda v. Snapple Distribs., No. 07-4538-CV, 2009 WL 3018035 (2d Cir. Sept. 22, 2009). In an unpublished opinion, the Second Circuit affirmed summary judgment against the plaintiffs for lack of any actual injury under the Robinson-Patman Act. Camarda and other local distributors alleged that Snapple violated the Robinson-Patman Act by giving preferential pricing to transshippers that sold product in the plaintiffs' territories at lower prices, resulting in the plaintiffs' lost business. The Second Circuit, however, found that the plaintiffs failed to make the required showing that other factors could not have been the cause of their injury.

Masimo Corp. v. Tyco HealthCare Group LP, Nos. 07-55960, 56017, 2009 WL 3451725 (9th Cir. Oct. 28, 2009). In an unpublished opinion, the Ninth Circuit upheld an award of $43.5 million (after trebling) against Tyco for sole source contracting and market share discounting in the market for medical devices known as pulse oximeters. The court affirmed that these practices violated sections 1 and 2 of the Sherman Act and section 3 of the Clayton Act. Although declining also to hold Tyco liable for bundled discounting on the record before it, the Ninth Circuit noted that bundling could be unlawful even when meeting the discount attribution test of *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883 (9th Cir. 2008), if the bundled discounts effectively prevented customers from dealing in the goods of competitors. (Editors Scott Westrich and Deborah Croyle represented Masimo on appeal.)

CALL FOR ARTICLES. THE PRICE POINT is seeking submissions for its Winter 2010 issue. Consistent with the Pricing Conduct Committee's new broader focus, articles on resale price maintenance, predatory pricing, bundled pricing, price squeezes, or other pricing-related topics are welcome, as of course are articles on price discrimination and Robinson-Patman Act issues. Articles should be approximately 3,000 words in length, excluding notes. Submissions will be due January 15, 2010. If you are interested in writing for THE PRICE POINT, please email a short description of your proposed topic to Scott Westrich at swestrich@orrick.com and Deborah Croyle at dcroyle@orrick.com.

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China's Chief Price-Regulator Flexes New Antitrust Muscle

By Jonathan M. Palmer*

On August 12, 2009, the National Development and Reform Commission ("NDRC")—one of the three Chinese agencies charged with enforcing the landmark Anti-Monopoly Law ("AML")—released a draft of its first substantive set of AML implementing rules, titled "Provisions Against Monopolistic Pricing" (the "NDRC Draft"). The period for public review and comment concluded on September 6.[1]

The NDRC Draft identifies specific price-related conduct that is prohibited under the AML, including price-fixing, bid-rigging, and market division agreements, as well as dominant firm conduct such as selling at unreasonably high prices, procuring at unreasonably low prices, predatory pricing, price discrimination, and covertly refusing to deal with competitors through the use of high sales or low procurement prices.

On the positive side, the NDRC Draft sheds light on numerous concepts left undefined in the AML. But it also raises red flags. For instance, it makes "product cost" a central concept in determining illegal pricing behavior, yet fails to define the term. The NDRC Draft also targets potentially innocent parallel conduct, and simply presumes "collective dominance" in highly concentrated markets without a showing of any structural or economic links among the competitors. At the same time, the NDRC Draft contains no leniency provisions for early reporting and cooperation in the context of collective behavior.

Before turning to these substantive issues, it is important to reflect on NDRC's unique role within China's emerging antitrust enforcement regime.

I. THE THREE ANTI-MONOPOLY ENFORCEMENT AGENCIES

The State Council—China's highest executive body—did not create a new agency to enforce the AML. Neither did it delegate regulatory authority over the AML to a single existing agency. Rather, the "Anti-monopoly Authority" referenced in Article 10 of the AML is actually a role shared by NDRC with two other existing ministry-level agencies—the State Administration for Industry and Commerce ("SAIC") and the Ministry of Commerce ("MOFCOM"). Each agency is responsible for enforcing separate pieces of the legislation and for promulgating implementing rules (such as the NDRC Draft). Each agency also has its own unique skill set and area of traditional expertise.

A. SAIC: Protector of Consumer Welfare

SAIC, China's analog to the U.S. Federal Trade Commission, has traditionally regulated consumer welfare, deceptive advertising, commercial bribery, and other unfair business practices. It currently enforces China's 1993 Anti-Unfair Competition Law—which regulates, among other things, predatory pricing, tie-in sales, bid rigging, and price-fixing.[2] Under the AML, SAIC is responsible for enforcing the non-price-related provisions governing abuse of dominance and "monopoly agreements" (the AML's term of art for illegal concerted conduct). Compared to its sister agencies, SAIC has traditionally been more of a champion of Chinese consumers, and has been perceived as more hostile to dominant foreign multinationals. Like NDRC, SAIC has released draft implementing rules. Specifically, on April 27, 2009, SAIC released its draft "Provisions on Prohibiting Abuse of Dominant Market Positions," and "Provisions on Prohibiting Monopolistic Agreements."[3]

B. MOFCOM: The Third International Center for Merger Clearance

MOFCOM, with its traditional oversight of foreign investment and foreign acquisitions of domestic companies, was a natural selection to enforce the merger clearance provisions of the AML. Of the three Anti-Monopoly Authorities, it has been quickest off the mark. Within months of the AML's August 1, 2008 effective date, MOFCOM promulgated several sets of implementing rules, made dozens of merger decisions, and literally put China on the map as a third center of merger enforcement with decisions in the InBev/Anheuser Busch merger, the Mitsubishi Rayon/Lucite merger, and the failed Coca-Cola/Huiyan acquisition.

C. NDRC: Domestic Planning Agency or International Cartel Buster?

The third Anti-Monopoly Authority, NDRC, is responsible for regulating all price-related violations under the AML's "monopoly agreements" and abuse of dominance provisions. As China's powerful macro-economic planning agency, NDRC has historically regulated domestic pricing. Specifically, NDRC administers China's 1997 Pricing Law,[4] which regulates government "guided prices" and government "set prices" in certain industrial sectors, and further regulates domestic price-related wrongdoing such as price manipulation, below-cost pricing, and fraudulent acts aimed at price inflation.

1. NDRC's Extra-Territorial Reach and Enforcement Powers

As the NDRC Draft makes clear, NDRC now regulates "monopolistic pricing conduct that occurs *outside* the People's Republic of China that has the effect of eliminating or restricting competition in the domestic market of the People's Republic of China."[5] This extra-territorial reach creates a new role for an agency that has historically focused on domestic economic and industrial planning and policy, and has little expertise in free-market economic analysis. Given the size of China's markets and China's increasing integration with the global economy, NDRC's new global role may have far-reaching consequences. This is particularly true in light of its authority over both investigations[6] and adjudications of suspected price-related violations,[7] and its extensive powers. NDRC has the authority to conduct dawn raids, seal up and retain evidence, interrogate relevant parties,[8] and set civil fines of up to 10% of a firm's annual revenues, plus disgorgement of all illegal gains.[9]

2. NDRC of the Future

The NDRC Draft sheds no light on whether NDRC intends to follow the path of its sister agency, MOFCOM, and join European and U.S. enforcement agencies as a third key center of antitrust enforcement. The NDRC Draft does, however, provide a clear window into the agency's self-image as a price regulator with broad authority and muscle. As if to underscore the point, one day after NDRC released its draft for comment, it released statistics indicating that it had investigated 21,000 instances of price-related conduct during the first half of 2009, had confiscated illegal gains of RMB 380 million, and had imposed fines of up to RMB 30 million.[10] It has also been reported that NDRC is considering investigations of numerous additional targets, including foreign multinationals.[11] Although many of these investigations and enforcement actions are no doubt related to enforcement of the 1997 Pricing Law, the saber rattling shows that NDRC has no intention of sitting on the sidelines while MOFCOM and SAIC jockey for enforcement primacy.

II. KEY FEATURES OF THE NDRC DRAFT

A. <u>Illegal "Monopoly Agreements"</u>

Chapter II of the AML governs "monopoly agreements," which are defined to include "agreements, decisions or other concerted actions which eliminate or restrict competition."[12] As mentioned above, these provisions are administered jointly by SAIC (with respect to non-price-related violations) and NDRC (with respect to price-related violations), and each agency has circulated its own draft implementing rules.

1. Prohibited Horizontal Agreements

The AML prohibits as *per se* illegal all horizontal agreements between competitors to (1) fix or change prices, (2) limit output, (3) divide markets, (4) join in boycotts, or (5) restrict the purchase of new technology or facilities for the development of new technologies or new products.[13] There is also a catch-all prohibition for "other monopoly agreements as determined by the Anti-Monopoly Authority under the State Council."[14] Article 6 of the NDRC Draft implements AML Article 13 by further enumerating specific types of illegal pricing agreements. Specifically:

> (A) Agreements that fix or adjust various product prices;
> (B) Agreements that fix or adjust the range of price fluctuations;
> (C) Agreements that fix or adjust fees and discounts that may affect prices;
> (D) Agreements that set a uniform price as the basis for negotiating with third parties;
> (E) Agreements to use standard formulas to calculate price;
> (F) Agreements not to change prices without consent from other business operators;
> (G) Agreements that fix or adjust product prices through restrictions on production output or sales, or by dividing sales or procurement markets;
> (H) Other monopolistic pricing agreements prohibited by the price authority under the State Council [i.e., NDRC].

Under Article 8 of the NDRC Draft, "Monopolistic Pricing Agreements reached in tendering and bidding, as well as auction activities" are also prohibited.

2. Conscious Parallelism May Be Prohibited

The NDRC Draft expands significantly on the AML definition of "monopoly agreement" by inferring illegal concerted action from uniform, tacit, or parallel behavior. Specifically, Article 5 states:

> The following factors shall be taken into consideration when identifying and determining concerted action:
> (A) Whether there is uniformity in various business operators' price-related behavior. If business operators set or adjust the prices of the same types of products with the same or similar standards or price ranges, at the same time or within a similar time frame, then such business

> operators are engaging in uniform price-related behavior.
>
> (B) Whether there has been a communication among business operators.
>
> In determining the existence of concerted action, the structure of and changes in the market shall be considered.

Although the language is vague, it signals a troubling departure from international norms and suggests that even innocent contacts or communications in the context of parallel conduct may give rise to liability.[15]

3. Vertical Agreements

Under both the AML and the NDRC Draft, only vertical agreements that fix resale prices and/or minimum prices are *per se* illegal.[16] The NDRC Draft, however, also contains a catch-all provision defining as illegal any vertical agreements that are determined to be "monopoly agreements" by NDRC.

4. Block Exemptions

Following the European model, certain agreements are immune from prosecution if they fall within one or more *block exemptions*.[17] These include, among others, agreements for the purpose of improving technology, developing new products, upgrading product quality, reducing costs, improving efficiency, unifying standards, conserving energy, protecting the environment, or protecting the legitimate interests of international trade.[18]

III. DOMINANT FIRM CONDUCT

Chapter III of the AML governs the "abuse of market dominance." To the extent such actions eliminate or restrict competition and are otherwise unjustified, enterprises with a "dominant market position" are prohibited from (i) selling or buying at unfair prices, (ii) pricing below cost, (iii) discriminatory pricing, (iv) refusing to deal with competitors, (v) requiring exclusive dealing arrangements and requiring tie-in sales.[19] As with the provisions on "Monopoly Agreements," the AML's abuse of dominance provisions are administered jointly by SAIC (with respect to non-price-related violations) and NDRC (with respect to price-related violations). Articles 11-15 of the NDRC Draft define terms and create an analytical framework for implementing the price-related prohibitions in Article 17 of the AML.

A. The "Rule of Reason" With Chinese Characteristics

The AML prohibits each category of "abuse of dominance" conduct only to the extent that it involves "unreasonable" prices, or is otherwise "without justification." The NDRC Draft attempts to clarify these concepts. Specifically, it defines overly high and low, or unfairly high and low, prices and enumerates examples of adequate "justifications"—e.g., pricing below cost in order to promote sales to pay debts, or price discrimination where trading partners are able to obtain substitute products. This fits China's legal system, which is rooted in the positivist civil law tradition rather than the common-law tradition of case-by-case analysis. Although the approach is much more rigid than the flexible *rule-of-reason* approach of U.S. courts, it nevertheless provides helpful guidance to business operators.

B. Definition of Dominance

Under the AML, an enterprise has a "dominant market position" if it is able to control price or output in the relevant market, or block or affect market access.[20] Consistent with international practices, dominance under the AML is determined based on an economic analysis of factors such as market share, control over sales or purchasing markets, financial strength, and barriers to entry.[21]

Articles 16- 20 of the NDRC Draft attempt to clarify these concepts in practice. Article 17, for instance, defines key terms used in the AML:

> As referenced in these Provisions, "a dominant market position," applies in circumstances where business operators are able to control product prices, output and other transactional conditions in the relevant market, or to prevent or affect entry in the relevant market by other business operators.
>
> The phrase, "other transactional conditions" refers to factors other than product price and quantity that can have a substantial effect on market transactions, including product grades, payment conditions, payment methods and after-sale services.
>
> The ability "to prevent or affect entry in the relevant market by other business operators" means the ability to exclude or delay other business operators' entry in the relevant market within a reasonable time period; or to raise the entry cost so significantly that it renders it impossible for such business operators to compete effectively with incumbent business operators even if they are able to enter the relevant market.

1. Analytical Framework for Determining Dominance

Article 18 lays out the factors for consideration in determining whether a business operator has a "dominant market position." These include:

> (A) The market share of the given business operators in the relevant market, and the state of competition in the relevant market.
>
> "Market share" refers to proportion of sale revenues or sales volume in the relevant market. Considerations regarding the "state of competition" in the relevant market may include the level of development of the market, the number of existing competitors, whether there are potential competitors and entry barriers, the market share of other business operators, the level of differentiation among comparable products and the transparency of the market.
>
> (B) The ability of the given business operators to control the relevant sales markets or the procurement markets for raw and processed materials.
>
> The ability to "control the relevant sales markets or the procurement markets for raw and processed materials" includes the ability to control sales and raw and processed materials, procurement channels, the ability to affect or determine the price, quantity, contract duration or other transactional conditions or the ability to procure raw and processed materials with priority. "Raw and processed materials" include raw materials, processed materials, parts and components and the relevant equipment necessary for business operation.
>
> (C) Financial and technological capacity of the given business operators.
>
> The "financial and technological capacity" of business operators includes factors such as the scale of the business operators' assets, its financial capabilities, profitability, financing capability, research and development capacity, facilities and equipment, level of technological innovation and application, and the intellectual property rights held. When analyzing the "financial and technological capacity" of business operators, their affiliates' financial and technological capacity, and such affiliates' effect on relevant market entry and production capacity expansion, shall also be taken into consideration.
>
> (D) The dependency of other business operators on the given business operators.
>
> The factors that affect such dependency include transactional volume with the given business operators, the duration of the trading relationship, and the ease with which trading counterparts may switch to other business operators.
>
> (E) The difficulty for other business operators to enter the relevant market.
>
> The factors affecting relevant market entry include the relevant system for market access, possession of essential facilities such as pipes and networks, sales channels, capital, technology and other necessary requirements for attaining economies of scale, and cost advantages.
>
> (F) Other factors relevant to determining whether a business operator has a dominant market position.

2. Market Definition

For purposes of defining the relevant market, Article 16 of the NDRC Draft incorporates the market definition guidelines issued by the State Council in July 2000. [22] These employ both demand and supply substitution methods to determine market definition, as well as the "hypothetical monopolist test" to the extent it may be appropriate in certain circumstances.

3. Presumption of Dominance with a 50% Market Share

Under Article 19 of the AML, "a dominant market position is presumed, but may be rebutted, where the market share of one enterprise accounts for 1/2 of the relevant market." Article 20 of the Draft Rules identifies the evidence that may be used to rebut the presumption of dominance based on a 50% market share:

> Business operators who are presumed to have a dominant market position shall be determined as not having a dominant market position if they can provide evidence that shows the following:
>
> (A) That it is relatively easy for other business operators to enter the relevant market;
>
> (B) That there is sufficient competition in the relevant market;
>
> (C) That, according to factors listed in Article 18, the business operators do not have the ability to control product prices, output and other transactional conditions in the relevant market, or to prevent or affect entry in the relevant market by other business operators.

C. Collective Dominance

Under the AML, a "dominant market position" is also presumed where the joint market share of two undertakings accounts for 2/3 of the relevant market, or where the joint market share of three undertakings

accounts for 3/4 of the market.[23] The AML provides, however, that enterprises that meet these thresholds "shall not be considered to have a dominant market position provided there is opposite evidence."[24]

Although the concept of joint or collective dominance has still not been fully implemented in Europe and has no direct counterpart in the U.S., the NDRC Draft does not appear to follow international norms of targeting only *unilateral* conduct, absent structural or economic links among the relevant actors. To the contrary, the NDRC Draft imposes a burden on market participants to come forward with specifically identified "opposite evidence" to show a lack of collective dominance. Specifically, business operators who are presumed to share collective dominance under the 2/3 and 3/4 rules of the AML "may only rebut that presumption through proof that there is competition in fact among them, and that any individual competitor does not have a more prominent market position than the other business operators in the relevant market."[25] The concept of "more prominent market position" is undefined and confusing, although it appears simply to suggest that there cannot be "collective dominance" in a market with a single monopolist.

D. Prohibited Dominant Firm Conduct

Article 11 of the NDRC Draft identifies four specific prohibitions under the abuse of dominance provisions of the AML (and further includes a catch-all provision for "other monopolistic pricing prohibited by" NDRC). Each of the four enumerated prohibitions is discussed below.

1. Selling at Unreasonably High Prices / Procuring at Unreasonably Low Prices

Article 12 of the NDRC Draft lays out the factors that may be considered in determining whether prices are "unfairly high" and "unfairly low." These include:

> (A) Whether the sales price is significantly higher than the cost of the product, or whether the procurement price is significantly lower than the cost of the product;
>
> (B) Whether a business operator raises the product sales price above a reasonable level or lowers the product procurement price below a reasonable level while costs are stable;
>
> (C) Whether a price increase for product sales is significantly higher than the increase in the product cost, or whether a price decrease for product procurement is significantly lower than the decrease in cost for the trading counterpart;
>
> (D) Whether a price is significantly higher or lower than the price set by other business operators selling or procuring the same type of products.

With its focus on product "cost"—rather than economic efficiency—this provision exposes NDRC's roots as the interventionist price regulator in China's old command economy. In its new role as a regulator of competition in an emerging market economy, using vague concepts such as "product cost," may inhibit rather than encourage competition. The NDRC Draft, for instance, makes no effort to distinguish average cost from marginal cost, or short run from long run costs, and it does not provide any analytical framework for determining the components of a cost calculation.

Moreover, the use of comparisons to competitor prices as the analytical tool for determining anti-competitive pricing may lead to absurd results. In efficient economies, enterprises charge less when they are more efficient. Under Article 12, however, their efficiency and zeal to compete on price could theoretically be held against them.

2. Predatory Pricing

Article 13 of the NDRC Draft clarifies the analytical framework for determining whether pricing below cost constitutes illegal predatory pricing. It provides:

> Business operators with a dominant market position shall not sell products at a price that is below product cost without justification.
>
> The phrase "price that is below product cost," referenced in the preceding paragraph, applies where business operators constantly sell products at a loss in order to exclude competitors or potential competitors.
>
> "Justifications," as referenced in the first paragraph, include:
>
> (A) Price decreases permitted by law for fresh produce, seasonal products, products about to reach expiration date and overstocked products.
>
> (B) Price decreases to promote sales in response to the need to pay debts, change lines of production or suspend a business;
>
> (C) Price decreases as a result of short term or small scale promotions aimed at attracting customers;
>
> (D) Price decreases aimed at counteracting other business operators' strategy of selling at a price that is below product cost;
>
> (E) Price decreases that result from reduced costs with economies of scale such that consumers can enjoy the benefit derived from such reduced price;

(F) Other justifications recognized by the price authority under the State Council [i.e., NDRC].

Although the enumerated justifications provide needed clarity, Section 12 again gives no framework for determining the central—though elastic and multi-faceted—concept of "product cost." Neither does Section 12 premise liability on a showing that the alleged predatory conduct could have had a reasonable chance of success in recouping the money lost on the below-cost pricing. As drafted, therefore, NDRC theoretically creates liability for some pro-competitive pricing behavior.

3. Pricing as Disguised Refusal to Deal

Article 14 of the NDRC Draft states that "[b]usiness operators with a dominant market position shall not refuse to engage in transactions with trading counterparts by setting overly high or overly low prices without justification." It further clarifies that "overly high or overly low prices" are prices that, "if applied, would prevent a trading counterpart from generating ordinary profits through ordinary production and sales activities." The NDRC Draft does not enumerate or define any "justifications" for price-based refusals to deal.

As drafted, Article 14 calls into question everyday business decisions regarding who to choose as trading partners. It may actually have a chilling effect on competition by discouraging business operators from switching to more efficient suppliers. It also evaluates wrongdoing against the benchmark of a trading partner's ability to operate at a profit—a comparison that may say much more about a trading partner's efficiency than it does about the reasonableness of an offered "price." As a matter of statutory construction, this provision also appears to go beyond the authority of the AML because it technically prohibits disguised refusals to deal—even without an underlying showing of competitive harm. It also goes well beyond the "outer boundary" of *Aspen Skiing Co. v. Aspen Highland Skiing Corp.* ,[26] which is in turn at the "outer boundary" of U.S. refusal-to-deal law.[27]

4. Price Discrimination

Article 15 of the NDRC Draft states that a "business operator with a dominant market position shall not, without justification, discriminate with respect to price against trading counterparts who otherwise have equal standing." As in other sections, NDRC specifically enumerates acceptable "justifications." In the case of price discrimination, they include:

(A) Price discrimination that does not have a substantial negative effect on trading counterparts' competition in the market;

(B) Price discrimination where trading counterparts are able to obtain the same types of products or substitute products from other business operators;

(C) Other justifications recognized by the price authority under the State Council.

Article 15 also defines "equal standing" as applying to situations where business operators conduct transactions with trading counterparts with respect to "the same types and same grades of products, and where the same or similar conditions exist with respect to the transactional methods, procedures, quantities, payment, settlement and after-sales services." For further clarification, Article 15 states that "[g]iving the same price to trading counterparts of different standing is considered discriminatory treatment."

IV. CONCLUSION

Lawyers who advise foreign multinationals with business interests in China should pay careful attention to the final published "Provisions Against Monopolistic Pricing." Those final regulations—which NDRC expects to issue by year-end—may well address some of the concerns raised in this article (and those raised during the public comment period). In any event, the new regulations, if enforced with energy and purpose, will have a profound effect on business practices in China.

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[1] *See* Caijing.com.cn, Draft Rules on Monopoly Price, http://english.caijing.com.cn/2009-08-13/110223866.html (last visited Oct. 29, 2009) (English language report).

[2] Law of the People's Republic of China Against Unfair Competition, Order of the President of the People's Republic of China, No. 10 (1993) (P.R.C.), *unofficial translation available at* http://www.fdi.gov.cn/pub/FDI_EN/Laws/GeneralLawsandRegulations/BasicLaws/P020060620320757961260.pdf (last visited Oct. 29, 2009).

[3] The full Chinese language text of SAIC's draft provisions may be found at http://www.saic.gov.cn/zwgk/zyfb/qt/fld/200904/t20090427_37769.html (last visited Oct. 29, 2009).

[4] Price Law of the People's Republic of China, Order of the President of the P[e]ople's Republic of China, No. 92 (1997) (P.R.C), *unofficial translation available at* http://www.fdi.gov.cn/pub/FDI_EN/Laws/GeneralLawsandRegulations/BasicLaws/P020060620320511406803.pdf (last visited Oct. 29, 2009).

[5] NDRC Draft, Article 2 (emphasis added). Throughout this article, quotations of both the NDRC Draft and the AML are based on Orrick, Herrington & Sutcliffe LLP's unofficial translation from the Chinese. Translations are provided as a

courtesy only, and are not to be construed as legal opinion or advice.

[6] AML, Article 38.

[7] *Id.*, Article 44.

[8] *Id.*, Article 39.

[9] *Id.*, Articles 46-47.

[10] *See* Chinese language report at http://www.12312.gov.cn/zhyw/bwdt/528737.shtml (last visited Oct. 29, 2009).

[11] *See* Chinese language report at http://www.chinareviewnews.com/doc/1007/3/1/4/100731482.html?coluid=7&kindid=0&docid=100731482 (last visited Oct. 29, 2009).

[12] AML, Art. 13 (2007) (P.R.C.) (unofficial translation), *available at* http://english.mofcom.gov.cn/aarticle/policyrelease/announcement/200712/20071205277972.html (last visited Oct. 29, 2009).

[13] *Id.*

[14] *Id.*

[15] SAIC's draft Provisions on Prohibiting Monopolistic Agreements (April 27, 2009 Draft) contain similar provisions for implementing AML Article 13 in the non-price-related context.

[16] AML, Article 14; NDRC Draft, Article 7.

[17] AML, Article 15; NDRC Draft, Article 10.

[18] AML, Article 15; NDRC Draft, Article 10.

[19] AML, Article 17.

[20] *Id.*, Article 17.

[21] *Id.*, Article 18.

[22] *See* Anti-Monopoly Committee of State Council, Guidelines on Defined Relevant Markets (July 7, 2009), Chinese language version, http://english.mofcom.gov.cn/aarticle/subject/cv/updates/200907/20090706389441.html (last visited Oct. 29, 2009).

[23] AML, Article 19.

[24] *Id.*

[25] NDRC Draft, Article 20.

[26] 472 U.S. 585 (1985).

[27] *See* Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 409 (2004).

GEOGRAPHIC MARKET DEFINITION IN SECONDARY-LINE PRICE DISCRIMINATION CASES

By Mark M. Lawson and Devin C. Dolive*

What must a plaintiff show in terms of market definition in order to prevail in a secondary-line price discrimination case? Courts have long held that the antitrust plaintiff bears the burden of proving the geographic market in Section 2 monopolization case[1] and in merger cases under the Clayton Act.[2] In recent years, some courts have also required that the plaintiff define the relevant geographic market in both primary-line[3] and secondary-line[4] Robinson-Patman Act cases. In addition, many courts have held that expert testimony is required to define a geographic market, including in price discrimination cases.[5]

In the primary-line price discrimination case, the rationale behind requiring definition of a relevant geographic market is to allow an assessment of the seller's market share.[6] After all, there is no reason for courts to be concerned about supposedly predatory pricing where the seller has no hope of ever gaining monopoly power. Instead, such predatory pricing is merely a boon to consumers.[7] In contrast, market share is usually not at issue in a secondary-line price discrimination case, although a plaintiff in a secondary-line price discrimination case still must show that he (as the disfavored purchaser) competed with the favored purchaser. And courts have employed the term "geographic market" in this secondary-line context.[8] This said, it can be argued that a less rigorous definition of the "geographic market" is required in the secondary-line price discrimination context than is required in primary-line price discrimination and monopoly cases.

Indeed, the requirement that a plaintiff define the relevant geographic market in a secondary-line case, at least with expert testimony, is a relatively new development. For instance, in *Ingram v. Phillips Petroleum Co.*,[9] the court noted that "competition between the purchasers is essential to actionable price discrimination,"[10] but then held that motor fuel retail outlets in Clovis, New Mexico and Farewell, Texas were in "practical competition" with each other without reviewing any type of expert testimony.[11]

Moreover, where a secondary-line price discrimination plaintiff brings claims under a state statute, it may not even be necessary to show such "practical competition." Many states have statutes applicable to specific industries that do not include any requirement that the plaintiff show an injury to competition. For instance, a number of states have enacted motor vehicle statutes that prohibit offers to sell and sales of vehicles at a lower actual price to one dealer than an actual price offered to another dealer, often without any mention of a competitive injury requirement.[12] Other states have enacted statutes applicable to sales of various types of equipment, again without any competitive injury requirement.[13] A Wisconsin state court has noted that Wisconsin statutes establish *per se* violations, "without requiring any proof of an adverse effect upon competitors or competition generally."[14] On the other hand, other courts have held that violations of state antitrust statutes modeled after federal statutes require proof of a relevant market.[15]

Where a secondary-line price discrimination plaintiff must prove a "relevant geographic market" that is, an "area of effective competition … in which the seller operates, and to which the purchaser can practicably turn for supplies,"[16] courts have allowed a variety of evidence to be used to support the geographic market definition. As noted above, some require expert testimony.[17] In terms of specific data, measurement of the relevant geographic market can depend upon a number of factors including "[p]rice data and such corroborative factors as transportation costs, delivery limitations, customer convenience and preference, and the location and facilities of other producers and distributors."[18] "Price data, corroborated by th[ese] factors …, are perhaps the most probative evidence of the relevance of the given market."[19]

As to how price data is used, the Sixth Circuit has concluded that a cross-price elasticity study is *not* required to show competition.[20] According to at least one economist, "a great deal of data would be needed such as information on natural boundaries, traffic flow, traffic patterns, population distribution, market conditions, existing development, etc." to perform a "cross-price elasticity" analysis,[21] and "the next best method which is generally accepted in the economics community (and was originally suggested by a Nobel Laureate in economics, George J. Stigler) is to determine whether a positive correlation exists between the retail prices of two products or two services in question."[22]

This "price correlation" test has been described as follows:

> One method often used to determine whether it is likely that two products are in the same market is to examine the behavior of the product prices over a period of time. When two products are in the same market (because of either demand or supply substitution), their prices will tend to move together. Thus one useful and powerful way to test whether two products are in the same market is to correlate their prices. This test is best thought of as necessary, but not sufficient. If prices are not highly correlated, it is unlikely that they are part of a single market; but if they are highly correlated, they may well be part of the same market.[23]

Of course, per the "necessary but not sufficient" language quoted above, a price correlation alone does not necessarily prove a market, and price correlations "must be purged of common factors such as seasonality in demand or price movements of a common input, that have nothing to do with competitive pressures." [24] Nonetheless, one court has stated, "the most compelling evidence that an area is competitively unified is statistical evidence of pricing interdependence…."[25]

There are other tests as well, although to date few of them seem to have actually been employed to define a geographic market, at least not in published opinions involving secondary-line price discrimination claims. [26] For instance, the Elzinga-Hogarty test (also sometimes referred to as a "LIFO-LOFI" or "shipments" test) has been frequently employed in the merger context but not so much in other antitrust contexts. [27] The Elzinga-Hogarty test "delineates" the geographic boundaries of markets on the basis of two percentages—LIFO ("little in from outside") and LOFI ("little out from inside"). [28] Each percentage is "calculated by division, with the numerator being the quantity of the relevant product being produced and consumed within the candidate market."[29] The "denominator for the LIFO percentage is the quantity of the relevant product that is consumed within the candidate market, from whatever source, and the denominator for the LOFI percentage is the quantity of the relevant product that is produced in the candidate market, whatever the point of consumption."[30]

Per the Elzinga-Hogarty test, "a candidate market is deemed to be a market only if the LIFO and LOFI percentages exceed particular thresholds; that is, only if the area has relatively little imports and relatively little exports." [31] "Elzinga and Hogarty originally suggested cutoffs of at least seventy-five percent for both percentages"[32] but they later changed their minds and "preferred a ninety percent cutoff for the average of the two percentages."[33]

Dr. Elzinga "has admitted that the LOFI-LIFO 'test' is a conservative one which estimates only minimum size. The actual market may be … larger than the shipment data would estimate.'" [34] As such, the Elzinga-Hogarty test "may *understate* the *geographic* market because the locations that buyers patronize at current prices—on which the Elzinga-Hogarty test is based—do not account for the possibility that buyers would substitute more distant locations in the event of a price rise."[35] Unfortunately, this is not the only weakness of the Elzinga-Hogarty test: "The test also can *overstate* the market where geographic price discrimination is employed."[36] If a seller is engaged in geographic price discrimination and "a product or service *cannot be resold*, a producer could control the competitive effect of its exercise of market power by pricing its services or products differently to one segment of the market as opposed to another,"[37] and "a producer could raise prices only to customers located closer to the producer and with fewer alternatives than more distant customers with more potential alternatives."[38] In addition, the Elzinga-Hogarty test may also "*overstate* the geographic market when the *product market* includes goods that are not perfect substitutes."[39]

Needless to say, the Elzinga-Hogarty test has been criticized for certain shortcomings. In the context of a hospital merger, a party employing Dr. Elzinga as an expert noted in a pre-trial brief: "Dr. Elzinga will explain how, due to health insurance, the prices a hospital charges for its services have little, if any, impact on the choices of hospitals by a patient," and "it is fundamentally erroneous to use the Elzinga-Hogarty test in defining geographic markets in hospital merger cases."[40] Nevertheless, in its heyday, the Elzinga-Hogarty test was routinely used by the FTC to analyze hospital mergers.[41]

The shortcomings discussed above do not necessarily "doom" the Elzinga-Hogarty test. One court has noted: "In theory, additional information about the way shipment flows would change in response to variations in prices and about product differentiation could be incorporated into the shipments analysis to avoid these problems." [42] Moreover, shipments data "certainly can be of value in delineating markets, particularly as a first cut."[43]

It is worth noting that the purpose behind proving a relevant geographic market in a secondary-line price discrimination case differs from the purpose behind proving a market in other antitrust contexts. For example, in a merger case, the concern is that the market definition might err by defining a market as *smaller* than it actually is, because the court then might be prompted to find a potential monopoly where none exists. In contrast, in the secondary-line price discrimination case, the concern is that the market definition might err by defining a market as *larger* than it actually is, because the court then might be prompted to find illegal price discrimination even though the favored and disfavored purchaser weren't really competing.

Even the Elzinga-Hogarty test's risk of *overstating* the size of the geographic market should be of little concern in most secondary-line cases. Many state price discrimination laws apply to particular goods such as motor vehicles or equipment of the same make and model,[44] so there should be little issue concerning the existence of "substitutes" in defining the relevant product market. Likewise, the RPA applies to "commodities of like grade and quality,"[45] and does *not* look at goods in secondary-line cases that are economic substitutes of each other. The RPA and many state price discriminations statutes also apply to commodities and goods that can be *resold* to others, so there may be little opportunity for a supplier to engage in geographic price discrimination.

As such, with these distinctions in mind, there are number of industries (i.e. motor fuel marketing and other retail stores) where the Elzinga-Hogarty test could

be used to determine competition between stores. Although this has yet to be explored in detail in reported case law, at least one Missouri trial court and one academic journal article have noted the potential for analyses based on retail credit card data.[46] The Elzinga-Hogarty test would seem useful in determining where the customers of the favored and disfavored purchasers reside,[47] and in other contexts, courts have looked at Elzinga-Hogarty data based on customer zip code information.[48] Indeed, such a test could be used to verify the results of a "Price Correlation" test, discussed above. By using credit data, it may even be possible to determine how far customers actually travel to make purchases, thus potentially addressing any issues concerning customer convenience and preferences and how the customer's transportation costs affect the size of the market.[49] Moreover, credit card data has the advantage of potentially showing whether customers' geographic buying patterns remain consistent over time.

In an age of increasing globalization and interconnectedness, courts may be tempted to give more thought to the type of proof required to prove geographic markets in the secondary-line price discrimination context. For example, a retailer in Maine may be able to show that he was competing with a retailer in Arizona for sales to at least one customer, but does this really mean the retailer in Maine should be able to sue his wholesaler if the wholesaler sells at a lower price to the retailer in Arizona? Under these circumstances, the antitrust plaintiff in Maine would be well advised to have pricing (and shipments) data in hand to show (if he can) that he was in "practical competition" with the favored purchaser in Arizona.

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[1] *See*, *e.g.*, Spectrum Sports, Inc. v. McQuillan*,* 506 U.S. 447, 459 (1993).

[2] *See* United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 381, 394 (1956). Congress apparently also viewed a properly defined relevant market as a necessary element of a Section 7 claim. *See* S. Rep. 81-1775, at 5 (1950) ("In determining the area of effective competition for a given product, it will be necessary to decide what comprises an appreciable segment of the market."). Of course, monopoly power may be proven by direct proof of the control of prices or exclusion of competition versus the use of market shares based on a properly defined market as a surrogate for market power. *See* E.I. du Pont, 351 U.S. at 393; Toys "R" Us, Inc. v. F.T.C., 221 F.3d 928, 937 (7th Cir. 2000).

[3] *See*, *e.g.*, Bailey v. Allgas, Inc.*,* 148 F. Supp. 2d 1222, 1231 (N.D. Ala. 2000), *aff'd*, 284 F.3d 1237, 1246 (11th Cir. 2002); Cogan v. Harford Memorial Hospital, 843 F. Supp. 1013, 1020 (D. Md. 1994) ("To allow a jury to make a finding as to the geographic market, Cogan must provide the court with expert testimony on this highly technical economic question.").

[4] *See*, *e.g.*, Best Brands Beverage, Inc. v. Falstaff Brewing Corp., 842 F.2d 578, 585 (2d Cir. 1987) ("The competitive nexus requirement is satisfied where there is a showing of 'competitive contact' between the recipients of the price differential. It must therefore be shown that, as of the time the price differential was imposed, the favored and disfavored purchasers competed at the same functional level, i.e., all wholesalers or all retailers, and within the same geographic market.") (citation omitted); Water Craft Management, L.L.C. v. Mercury Marine, 361 F. Supp. 2d 518, 537-38 (M.D. La. 2004), *aff'd*, 457 F.3d 484 (5th Cir. 2006); *see also* United Food Mart, Inc. v. Motiva Enterprises, LLC*,* 457 F. Supp. 2d 1329, 1341 (S.D. Fla. 2005) (secondary-line price discrimination claim under the Florida Motor Fuel Marketing Practices Act).

[5] *See*, *e.g.*, *Bailey*, 148 F. Supp. 2d at 1231 (primary-line price discrimination under the RPA); *Water Craft*, 361 F. Supp. 2d at 542 (secondary-line price discrimination under the RPA); *United Food Mart, Inc.,* 457 F. Supp. 2d at 1341 (secondary-line claim under the Florida Motor Fuel Marketing Practices Act); Shahbazi v. Equilon Enterprises, No. HO28871, 2006 WL 3020938, at *5 (Cal. App. Oct. 24, 2006) (secondary-line claim under California Unfair Practices Act); *see also* Virginia Vermiculite, Ltd. v. W.R. Grace & Co.*,* 98 F. Supp. 2d 729, 732, 736 (W.D. Va. 2000) (commenting on a Section 2 Sherman Act claim: "Market analyses for antitrust markets generally require some expertise in the field of industrial organization."); *but see* Victus, Ltd. v. The Collezione Europa U.S.A., Inc., 26 F. Supp. 2d 772, 786-87 (M.D.N.C. 1998) (commenting on Section 2 Sherman Act counterclaim: "Testimony from an economist is not necessary; however, some evidence of the effects of price increases on the proposed market, and an analysis of consumer reactions to such a scenario, would make Europa's argument more plausible.").

[6] Bailey v. Allgas, Inc. 284 F.3d 1237, 1246 (11th Cir. 2002) ("Once the relevant market has been determined, it is possible to calculate a seller's percentage share of that market"); Rebel Oil Co. v. Atlantic Richfield Co., 51 F.3d 1421, 1434 (9th Cir. 1995) ("Without a definition of the relevant market, it is impossible to determine market share").

[7] *See* Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224 (1993).

[8] *See, e.g., Best Brands*, 842 F.2d at 585 ("The competitive nexus requirement is satisfied where there is a showing of 'competitive contact' between the recipients of the price differential. It must therefore be shown that, as of the time the price differential was imposed, the favored and disfavored purchasers competed at the same functional level, i.e., all wholesalers or all retailers, and within the same geographic market.") (citation omitted).

[9] 259 F. Supp. 176 (D.N.M. 1966).

[10] *Id.* at 182.

[11] *Id.*; *see also* Bargain Car Wash, Inc., v. Standard Oil Co. (Indiana), 466 F.2d 1163, 1168 (7th Cir. 1972) ("It is readily apparent … that the zones did not represent actual areas of competition in the sale of gasoline. Indeed, the findings recognize at least twelve zones surrounding Bargain's zone that were competitive, and American's witnesses readily admitted as much.").

[12] *See, e.g.*, DEL. CODE tit. 6, § 4913(b)(10); GA. CODE § 10-1-662(a)(12); ME. REV. STAT. tit. 10, § 1174(3)(E); MASS. GEN. LAWS ch. 93B, § 4(c)(5); NEV. REV. STAT. § 482.36386(1); N.H. REV. STAT. § 357-C:3(III)(e); R.I. GEN. LAWS § 31-5.1-4(c)(4)(i); S.C. CODE § 56-15-40(3)(e); VA. CODE § 46.2-1568.1(1), & § 46.2-1568.1(2); WASH. REV. CODE § 46.96.185(1)(a).

[13] *See*, *e.g.*, FLA. STAT. §§ 686.413(3)(e), & 686.611(3)(e); N.Y. GEN. BUS. LAW § 696-b(7); S.C. CODE § 39-6-50(c)(4); TEX. BUS. & COM. CODE § 55.154(b)(1).

[14] Obstetrical & Gynecological Ass'n of Neenah, S.C. v. Landig, 384 N.W.2d 719, 721 (Wis. App. 1986); *see also* Bruce P. White & Christopher J. Littlefield, *Arizona's New Equipment Dealer Protection Laws*, 30-FEB ARIZONA ATT'Y 20, 22 (Feb. 1994) ("Further, unlike the price discrimination provisions of the Robinson-Patman Act which require a showing of competitive injury to establish a violation, the AEDPL appears to create a per se prohibition on price discrimination among similarly situated dealers.").

[15] *See, e.g.*, Berlyn, Inc. v. Gazette Newspapers, 223 F. Supp. 2d 718, 726 (D. Md. 2002), *aff'd,* 73 Fed. Appx. 576 (4th Cir. 2003); *see also* Shahbazi v. Equilon Enterprises, No. H028871, 2006 WL 3020938, at *4 n.9 (Cal. App. Oct. 24, 2006) ("When California's laws are patterned on federal statutes, federal cases construing those federal statutes may be looked to for persuasive guidance."); Redmond Ready-Mix, Inc. v. Coats, 582 P.2d 1340, 1346 (Or. 1978) ("ORS 646.040 is comparable with s 2(a) of the Robinson-Patman Act, 15 U.S.C. s 13(a) (1976). Under such circumstances federal cases interpreting the federal statutes are persuasive to us in interpreting the Oregon statute.") (citations omitted).

[16] Bailey v. Allgas, Inc. 284 F.3d 1237, 1247 (11th Cir. 2002) (quoting Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 320, 327 (1961); *see also* J & S Oil, Inc. v. Irving Oil Corp., 63 F. Supp. 2d 62, 68 (D. Me. 1999) ("Simply put, the geographic market for retail gasoline depends on how far individuals are willing and able to travel to purchase the product.").

[17] *See* note 5, *supra*.

[18] *Bailey*, 284 F.3d at 1247 (quoting T. Harris Young & Assocs., Inc. v. Marquette Elecs., Inc., 931 F.2d 816, 823 (11th Cir. 1991)).

[19] L.A. Draper & Son v. Wheelabrator-Frye, Inc., 735 F.2d 414, 423 (11th Cir. 1984).

[20] Lewis v. Phillip Morris Inc., 355 F.3d 515, 531 (6th Cir. 2004).

[21] United Food Mart, Inc. v. Motiva Enterprises, LLC, 404 F. Supp. 2d 1344, 1348 (S.D. Fla. 2005); *see also* In the Matter of Olin Corp*.,* 113 F.T.C. 400, 1990 WL 10012633, at ¶173 (F.T.C. June 13, 1990) ("To be sure, 'cross-elasticity of supply and demand' is an attractive concept in defining an 'economic market.' … . However, the 'real world' has seldom, if ever, been as accommodating as one might wish in terms of providing precise or reliable price-quantity data of sufficient scope or depth to enable us to define with any degree of precision an economic market with respect to any product or a group of products.").

[22] *United Food Mart*, 404 F. Supp. 2d at 1348.

[23] Andrew M. Rosenfield, *The Use of Economic Analysis in Antitrust Litigation and Counseling*, 1986 COLUM. BUS. L. REV. 49, 63 (1986) (*citing* George J. Stigler & Robert A. Sherwin, *The Extent of the Market*, 28 J.L. & ECON. 555 (Oct. 1985)); *see also* Dennis W. Carlton & Jeffrey M. Perloff, MODERN INDUSTRIAL ORGANIZATION 647 (4th ed. 2004) ("If Products A and B are in the same economic market, then their prices should tend to move closely together. Therefore, a reasonable *first* step in defining economic markets is to examine the price correlations … .") (emphasis in original); Rebel Oil Co. v. Atlantic Richfield Co., 808 F. Supp. 1464, 1467-68 (D. Nev. 1992), *aff'd,* 51 F.3d 1421 (9th Cir. 1995) ("The expert noted that under the 'Stigler' method of proving supply elasticity, high price correlation indicates that consumers view the products as substitutes for each other.").

[24] Niels Haldrup, et al., *Sequential v. Simultaneous Market Delineation*: *The Relevant Antitrust Market for Salmon,* 4 J. COMPETITION L. & ECON., 893, 896 (Sept. 2008).

[25] Jim Walter Corp. v. F.T.C., 625 F.2d 676, 682 (5th Cir. 1980).

[26] *See*, *e.g*., Janusz A. Ordover & Daniel M. Wall, *Understanding Econometric Methods of Market Definition,* ANTITRUST 20 (Summer 1989) ("Others would include the LOFI (little out from the inside) and LIFO (little in from the outside) tests for geographic markets developed by Elzinga and Hogarty, the regression approach proposed by Horowitz, the price correlation test of Stigler and Sherwin, and the well-known five percent price increase test of the 1982 Department of Justice Merger Guidelines.") (citations omitted); *see also* Jeffrey Church & Roger Ware, INDUSTRIAL ORGANIZATION: A STRATEGIC APPROACH 619 (2000) ("The structural approach to market definition uses indirect evidence to infer elasticity of demand. Information of potential relevance is price correlations, shipment flows, and qualitative criteria.").

[27] *See* Gregory J. Werden, *The History of Antitrust Market Delineation*, 76 MARQ. L. REV. 123, 210 (1992) ("The Elzinga-Hogarty test has been applied to numerous antitrust cases, but has not been generally relied on by the courts. The test is now particularly popular for hospital mergers, and has been relied on in that context to some extent by both the FTC and the courts.").

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] *Id.*

[32] *Id.*

[33] *Id.*

[34] In the Matter of Weyerhaeuser Co., 106 F.T.C. 172, 1985 WL 668940, at *51 (F.T.C. Sept. 26, 1985) (quoting Kenneth G. Elzinga, *Defining Geographic Market Boundaries*, 26 ANTITRUST BULL. 739, 743 (1981)).

[35] Jonathan B. Baker, *Market Definition*: *An Analytical Overview*, 74 ANTITRUST L.J. 129, 154 (2007) (emphasis added).

[36] United States v. Rockford Memorial Hospital, 717 F. Supp. 1251, 1267 n.12 (N.D. Ill. 1989) (emphasis added), *aff'd,* 898 F.2d 1278 (7th Cir. 1990).

[37] *Id.* (emphasis added).

[38] *Id.*

[39] *Id.* (emphasis added).

[40] Public Version of Complaint Counsel's Revised Pre-Trial Brief, In the Matter of Evanston Nw. Healthcare Corp., 2005 WL 435838, at p. 20 (F.T.C. Jan. 27, 2005); *see also* Staff Adv. Op./Comment Letter, 2003 WL 1736809, at *4 n.16 (F.T.C. April 1, 2003) ("The use of the Elzinga-Hogarty test defining geographic markets for hospital mergers has been widely and correctly criticized… . The basic problem with the Elzinga-Hogarty test is that it does not provide evidence directly relevant to the central issue, i.e., to what extent employers and consumers require access to a local hospital in their healthcare plans."); DOJ News Release, DOJ 04-506, 2004 WL 1638852, at *3 (D.O.J. July 23, 2004) ("To date, the agencies' experience and research indicate that the Elzinga-Hogarty test is not valid or reliable in defining geographic markets in hospital merger cases.").

[41] *See* note 27, *supra*; *see also* Nilavar v. Mercy Health Sys. – W. Ohio, 494 F. Supp. 2d 604, 613 n.12 (S.D. Ohio 2005) ("LIFO (Little In From Outside) and LOFI (Little Out From Inside) are the fundamental analytical tools used by economists employing the Elizinga-Hogarty test. That test is used to evaluate proposed markets in antitrust cases and can prove a plaintiff's market definitions by demonstrating that relatively little product enters the market from outside the proposed geographic area and that relatively little product leaves the market from inside the proposed geographic area."), *aff'd*, 244 Fed. Appx. 690 (6th Cir. 2007).

[42] United States v. Rockford Memorial Hospital, 717 F. Supp. 1251, 1267 n.12 (N.D. Ill. 1989), *aff'd,* 898 F.2d 1278 (7th Cir. 1990).

[43] Gregory J. Werden, *The History of Antitrust Market Delineation,* 76 MARQ. L. REV. 123, 210 (1992); *but see* Jeffrey Church & Roger Ware, INDUSTRIAL ORGANIZATION: A STRATEGIC APPROACH 616 (2000) ("While the results may be suggestive, LIFO and LOFI are usually inconclusive with regard to market definition on their own … .").

[44] *See* notes 12 and 13, *supra.*

[45] 15 U.S.C. § 13(a).

[46] Memorandum and Order, Sidney L. Turpin, et al. v. BP Products North America Inc., *et al.*, In the Circuit Court for the City of St. Louis, No. 22002-08365-01 (June 27, 2007), at pp. 32-33 ("There is no doubt that this information [credit card data concerning customers who have purchased motor fuel via credit card at stations in the St. Louis area] is highly relevant to issues in the case. It is relevant because, among other reasons, it might allow Plaintiffs' experts to use the address information to better determine the size and scope of relevant geographic market areas in which competition occurs in the greater St. Louis metropolitan area, and the distances customers will drive to obtain gasoline. This information, in turn, could allow Plaintiffs to show who their competitors were … ."); *see also* Brady Foust & Howard Botts, *Creating a 'Convex Hull' with a GIS: A Better Estimate of Market Area Size and Shape*, 15 PAPERS & PROCEEDINGS OF APPLIED GEOGRAPHY CONFERENCES 85, 87 (1992) ("Customer origin data can be used to define accurately the size and shape of a market area if some *geographic identifier* of each customer's home or work place can be obtained … . Direct data sources use geographic information supplied by the consumer. These data are increasingly captured by 'point-of-sale' systems, but they can also be obtained through store survey forms, credit card data and addresses on personal checks.") (emphasis in original).

[47] *See*, *e.g.*, England v. Chrysler Corp., 493 F.2d 269, 271-72 (9th Cir. 1974) ("[T]he advantaged and disadvantaged parties must be shown to be competing customers … in order for there to be discrimination."); Yamaha Store of Bend, Oregon, Inc. v. Yamaha Motor Corp., 798 P.2d 656, 659 (Or. 1990) ("[I]f the favored and disfavored buyers … do not in fact compete for the same customers, there cannot be a reasonable probability of harm to competition.").

[48] *See*, *e.g.*, F.T.C. v. Freeman Hospital, 69 F.3d 260, 264-65 (8th Cir. 1995) ("In undertaking this analysis, Dr. Leffler again used patient zip code information and determined that approximately ninety percent of hospital admissions of people residing in the proposed service area were admissions to hospitals within the service area.").

[49] *See*, *e.g.*, Bathke v. Casey's General Stores, Inc., 64 F.3d 340, 346 (8th Cir. 1995) ("Casey's has pointed to the unrefuted evidence that 42% of the people living in the relevant towns work elsewhere. Given these facts, it is entirely possible, if not likely, that those consumers have alternatives to purchase gas beyond their town of residence."); J & S Oil, Inc. v. Irving Oil Corp., 63 F. Supp. 2d 62, 68 (D. Me. 1999) ("Simply put, the geographic market for retail gasoline depends on how far individuals are willing and able to travel to purchase the product."); *see also Gas Guesses: Consumers Remain Price Sensitive, Overestimate Retailer Profit*, CSP DAILY NEWS (Feb. 3, 2009), *available at* GAS GUESSES/CSP DAILY NEWS/ MAGAZINE/CSP INFORMATION GROUP, INC. ("Even with gasoline prices at the beginning of 2009 approximately $1.40 per gallon below last year's levels, consumers remain incredibly price sensitive, with 70% saying that price is the most important factor in deciding where to purchase gasoline, and more than half of all consumers (51%) reporting that they will drive 10 minutes out of their way to save as little as five cents per gallon.").

THE EUROPEAN COURT OF JUSTICE'S FRANCE TÉLÉCOM/WANADOO JUDGMENT: CHRONICLE OF A FAILED CHICAGOAN REVOLUTION

(*France Télécom SA v. Commission*, Case No. C-202/07 P (E.C.J. April 2, 2009))

By Alberto Alemanno and Marco Ramondino*

The inveterate problem of any predatory pricing doctrine is distinguishing between harmful predatory pricing and desirable competitive price-cutting. Indeed, because competitive price cutting is among the most desirable effects of competition, "the last thing one would want would be to enable firms to use antitrust law to discipline rival price cuts." [1] The challenge for any antitrust regime is therefore to develop a test capable of adequately deterring harmful predatory pricing without discouraging competitive price cutting.

Over the last decade, the debate in the European Union (the "EU") on predatory pricing revolved mainly around whether to include, in the test for predation, proof of the possibility of recoupment of losses incurred by a dominant firm while selling at a loss. Prior to the *France Télécom* case, the European Court of Justice (the "ECJ") had limited opportunities[2] to examine the test for predation applied by the European Commission and left this fundamental issue open. In *Akzo*, the ECJ did not address the issue of recoupment but set the now classic test for predation, under which prices below average variable costs (i.e. costs that vary depending on the quantities produced) are abusive *per se* while prices below average total costs (i.e. fixed costs plus variable costs), but above average variable costs, must be regarded as abusive if they are part of a plan for eliminating a competitor.[3] In *Tetra Pak II* the ECJ held that "in the circumstances of the case" it was not necessary to prove the possibility of recoupment. One of the distinctive features of the *Tetra Pak II* case was that the dominant company held a particularly strong market position which, while falling short of monopoly, has often been regarded as being a "super dominance." This has led commentators and the appellant in the *France Télécom* case to argue that when a company is "only" dominant and not super dominant, proof of recoupment should indeed be part of the predatory pricing test.[4]

With its 2009 *France Télécom* judgment,[5] the ECJ proved this interpretation of *Tetra Pak II* to be incorrect. In paragraph 110, the ECJ seems to identify the distinctive feature of *Tetra Pak II* in the fact that "the eliminatory intent of the [dominant] undertaking … could be presumed in view of that undertaking's application of prices lower than average variable costs." Although this authoritative interpretation of the *Tetra Pak II* judgment does not seem consistent with *Tetra Pak II*'s wording, which suggests that the characteristics of the dominant position and not of the abuse obviated the need to prove recoupment of losses, the ECJ has nevertheless clarified its position on recoupment. While controversial, this is a welcome development, and one which is now reflected in the recent Commission's Guidance on Article 82 enforcement priorities (published in February 2009).[6]

I. FACTS AND BACKGROUND

In July 1999, the Commission of the European Communities ("the Commission") launched a sector inquiry into the provision of local loop access services and the use of residential local loop in the EU. As a result of this inquiry, the Commission opened an investigation into the activities of France Télécom. In its decision of July 16, 2003,[7] (the "contested decision") it found that Wanadoo Interactive SA ("WIN"), a subsidiary of France Télécom, had engaged in predatory pricing of its high speed internet access services, eXtense and Wanadoo ADSL, in breach of Article 82 EC.[8] The Commission found evidence that the below-cost pricing applied by WIN formed part of a deliberate strategy of predation aimed at pre-empting the strategic market for high-speed internet access during a key phase of its development at the expense of competitors.

In Article 1 of the contested decision, the Commission found that, from March 2001 to October 2002, WIN had infringed Article 82 EC by charging predatory prices for its eXtense and Wanadoo ADSL services, that is, charging prices that did not enable it to cover its average variable costs (AVC – costs that vary depending on the quantities produced or, as in the present case, on the number of clients served) until August 2001, or to cover its average total costs (ATC – average fixed costs plus average variable costs) from August 2001 onwards, as part of a plan to pre-empt the market for high-speed internet access. In Article 2 of its decision, the Commission ordered WIN to bring the infringement to an end and in Article 4, imposed a fine on WIN of EUR 10.35 million.

A. The Judgment of the Court of First Instance

On October 2, 2003, WIN filed an application to annul the contested decision with the CFI; following the merger between Wanadoo and France Télécom in September 2004, France Télécom became the applicant. In support of the application, France Télécom maintained in essence that the Commission had infringed Article

82 EC in failing to establish, to the requisite legal standard, that WIN had abused its dominant position by charging predatory prices for the services in question. In particular, France Télécom challenged the Commission's application of both (i) the test to assess the recovery of costs, and (ii) the test of predation.

In assessing the recovery of costs, the Commission had relied on the adjusted costs method of calculation, under which it compared France Télécom's monthly revenues with the sum of its recurrent monthly costs and the portion of its non-recurrent costs over a 48 month period (the average life time of a subscription) which was attributable to one month. In particular, the Commission calculated the average of the resulting ratio for four consecutive periods: from January 1 to July 31, 2001, from August 1 to October 15, 2001, from October 15, 2001, to February 15, 2002, and from February 15 to October 15, 2002.

In applying its test of predation, the Commission had found that the pricing practice concerned was eliminatory, inasmuch as the prices charged by WIN were below average variable costs, and that it was abusive, inasmuch as the prices charged were above AVC but below ATC. To prove the latter, the Commission provided evidence that WIN's pricing practice formed part of a plan to pre-empt the market.

1. The Complaints in Relation to the Recovery of Costs Test

The CFI first recalled, in paragraphs 129 and 130 of the judgment under appeal, the broad discretion which the Commission has in matters involving complex economic assessment and the tests identified by the ECJ's case-law for determining whether a price can be found to be predatory. Referring inter alia to *Akzo* and *Tetra Pak II*, the Court of First Instance noted that, "first, prices below average variable costs give grounds for assuming that a pricing practice is eliminatory and that, if the prices are below average total costs but above average variable costs, those prices must be regarded as abusive if they are determined as part of a plan for eliminating a competitor."[9]

Having so stated, the CFI endorsed the adjusted cost method of calculation as applied by the Commission. That method is described in paragraph 132 of the judgment under appeal: in accordance with the principle of depreciation of assets, the Commission had spread the costs of acquiring customers over 48 months. On that basis, it had made a separate assessment of adjusted variable costs and adjusted full costs.

The CFI then rejected WIN's argument that the adjusted cost method did not take into account the variations in costs over the course of the 48-month period concerned,[10] an approach unfavourable to WIN. The Court observed, in paragraph 143 of the judgment under appeal, that the Commission had indeed taken into account for each period of infringement and for all subscribers the successive reductions in tariffs applied by WIN. The CFI also found that even if WIN were to prove that the method which it advocated (that is to say, the method of discounted cash flows) was appropriate in some respects, that would be insufficient to demonstrate that the method used by the Commission was unlawful.[11]

In addition, WIN maintained that the Commission had erred in the application of its own method of calculation, particularly in the calculation of fixed and variable costs. According to WIN, if the adjusted cost method had been applied correctly the rates of recovery of full costs would have increased from a margin of 90 to 91% to a margin of 98 to 99%. In that respect, the CFI held that, independently of the admissibility of that plea, the fact that the Commission, in exercising its discretion, accepted that a rate of recovery of variable costs of 99.7% did not amount to an infringement could not require the Commission to take the same approach with respect to a rate of recovery of full costs of 98 or 99%, as the case may be. The plea therefore was rejected as ineffective.[12]

2. The Complaints in Relation to the Test of Predation

The CFI also dismissed WIN's complaints relating to the test of predation applied by the Commission. It first rejected WIN's arguments that an undertaking has a right to align its prices, in good faith, with those previously charged by one of its competitors where those prices are lower than that undertaking's costs. Having noted that neither the Commission's practice nor the case-law of the Community courts recognised such a right, the CFI pointed out that undertakings in a dominant position have special obligations imposed on them and can be deprived of the right to adopt a course of conduct or take measures which are not in themselves abusive and which would even be unobjectionable if adopted or taken by non-dominant undertakings.[13] As a result, the CFI concluded that

> WIN cannot … rely on an absolute right to align its prices on those of its competitors in order to justify its conduct. Even if alignment of prices by a dominant undertaking with those of its competitors is not in itself abusive or objectionable, it might become so where it is aimed not only at protecting its interests but also at strengthening and abusing its dominant position.[14]

Second, the CFI rejected WIN's allegation that it did not have a plan of predation and reduction in competition. According to WIN, the Commission

committed a serious infringement of Article 82 EC in finding that a plan to eliminate competition existed. Such a plan could not be considered rational given the market conditions concerned, particularly since the barriers to entry to that market were low.[15] Referring to Community case-law, the CFI recalled that in the case of predatory pricing, where prices are below average total costs, the existence of a plan to eliminate competition has to be proved and intention to eliminate competition established on the basis of sound and consistent evidence.[16] It then held that the statements referred to by the Commission, which were contained in internal company documents, were indicative of a plan of predation and were reinforced by other evidence. The CFI concluded that the Commission had provided solid and consistent evidence as to the existence of a plan of predation for the entire infringement period.[17]

Third, WIN submitted that the Commission erred in law in finding that it was not necessary to demonstrate the possibility of recouping the losses which it suffered as a result of the application of the pricing policy.[18] The Court of First Instance held that, in accordance with *Akzo* and *Tetra Pak II*,[19] the Commission was right to take the view that proof of recoupment of losses was not a precondition to making a finding of predatory pricing. In line with the ECJ's case-law, the Commission was able to conclude that prices below average variable costs are abusive. In that case, the eliminatory nature of such pricing was presumed. In relation to full costs, the Commission also had to provide evidence that WIN's predatory pricing formed part of a plan to "pre-empt" the market. According to the CFI, in neither of those situations was it necessary to prove, in addition, that WIN had a realistic chance of recouping its losses.[20]

II. THE JUDGMENT OF THE COURT OF JUSTICE

France Télécom put forward seven grounds in support of its appeal of the CFI's decision: (i) failure to state reasons; (ii) infringement of Article 82 EC by denying WIN the right to align its prices in good faith on those of its competitors; (iii) error in the assessment of the lawfulness of the method used by the Commission to calculate the rate of recovery of costs; error in law and breach of its duty to state reasons, inasmuch as: (iv) it held that the revenues and costs subsequent to the period that the alleged breach lasted should not be taken into account in the calculation of the rate of recovery of costs and (v) it found that a price leading to a reduction in the undertaking's market share is capable of being found to be predatory; (vi) alleged distortion of the evidence and error in law in its assessment of whether a plan of predation existed; (vii) breach of Article 82 EC, inasmuch as it refused to take account of the impossibility of recouping the losses. In our review of the *France Télécom* judgment we will mainly focus on the grounds relating to the predation test.

A. The Advocate General's Opinion: Chronicle of a Failed Chicagoan Revolution

On 25 September, 2008, Advocate General Mazak[21] delivered his opinion, a non-binding analysis and recommendations, on the *France Télécom* case.[22] On the points of substance, the Advocate General ("AG") concluded that France Télécom's appeal should be upheld and that the CFI had erred in law. In particular, he proposed to uphold the following two pleas:

1. The First Ground of Appeal, Alleging Failure To State Reasons:

a. The CFI Failed To State Reasons When Commenting on a Dominant Firm's Right To Align Prices

As regards a dominant undertaking's right to align its prices with those of its competitors, Advocate General Mazak agreed with the CFI's general proposition that dominant undertakings have no absolute right to align their prices where to do so would result in abusive conduct. However, the Advocate General found that the CFI had failed to apply this general proposition to the particular facts of the France Télécom case.[23] As a result, he considered the lack of reasoning on the part of the CFI and the deficiency in its line of argument to be "all the more serious as it would appear that this is the first case in which the defence of alignment has been directly addressed by the Community courts in a situation such as that in the present case."[24]

b. The CFI Failed To State Reasons Why (Possibility of) Recoupment Need Not Be Shown

In taking up this claim, the AG criticised the CFI for failing to explain why it considered that proof of the possibility of recoupment of losses was not necessary in the light of the specific facts of the case. He noted that, while the CFI cited a judgment which unambiguously stated that it was not appropriate to require proof that a dominant undertaking had a realistic chance of recouping its losses, the ECJ had taken care to add "*in the circumstances of that particular case*." As a result, the AG argued, the CFI should not have simply turned that statement, which was clearly based on the specific facts of *Tetra Pak II*, into a general rule.

2. Likely Recoupment as a Precondition To Finding Predatory Pricing

As regards to this controversial ground, the Advocate General concluded that the CFI's (and Commission's) interpretation of the ECJ's case law was incorrect: the ECJ would have already adopted a requirement of recoupment under Article 82 EC.[25] In his view, proof of the possibility of recoupment is required not only since *Tetra Pak II*, where the Court, by using the qualifying words "in the circumstances of the present case," "clearly intended to avoid making a general statement that would render it unnecessary to prove" this requirement in future predatory pricing cases, but also since the older *Akzo* and *Hoffman-La Roche* judgments.[26] He concluded that, as a result, the CFI should have assessed whether, on the basis of the facts of the case, it was necessary to consider the prospect of recoupment.

In addition the AG, although dismissing the second ground of appeal (alleging infringement of Article 82 EC—alignment of prices with those of competitors) as inadmissible, opined that, in his view, a dominant firm should, on occasion, be allowed to align its prices with those of competitors.

It might be tempting to agree with the AG on this point, as several commentators do[27] when discussing circumstances such as when the dominant firm is selling old stock. But what if the dominant company engaging in such behaviour pursues the clear objective of damaging a new entrant in a market where it has been the incumbent for many years? This hard question remains unfortunately unanswered by the AG opinion.

B. Conclusion on AG Opinion and Comment

In sum, the AG made a call for a major change in the assessment of predatory pricing, by placing a greater focus on the impact on consumer welfare and less on the protection of market participants. Regardless of the merits of his position, the problem is that the case law supposedly justifying this shift does not seem to support it. As is well-known, both *Akzo* and *Tetra Pak II* are cases where the dominant concern was the preservation of competition rather than the safeguard of the interests of consumers. It is worth quoting the CFI in France Télécom at length:

> In relation to the recoupment of losses, the Court of Justice (in *Tetra Pak II*) added, in paragraph 44 of that judgment: '[I]t would not be appropriate, *in the circumstances of the present case*, to require in addition proof that Tetra Pak had a realistic chance of recouping its losses. *It must be possible to penalise predatory pricing whenever there is a risk that competitors will be eliminated.* The Court of First Instance found, at paragraphs 151 and 191 of its judgment, that *there was such a risk in this case*. The aim pursued, which is to maintain undistorted competition, rules out waiting until such a strategy leads to the actual elimination of competitors.[28]

This shows that the reason proof of likely recoupment was unnecessary in *Tetra Pak II* was that the Commission had proved there was a risk that a competitor would be eliminated. As a result, under the existing predatory test, as soon as the conditions set out in *Akzo* are satisfied, a risk of elimination is shown and there is no need for recoupment. Regardless of whether this is a good or bad approach to predatory price-cutting, this is what the actual case-law of the Court stands for.

Finally, the attempt made by the AG to derive the existence of a general rule proof of likely recoupment from the qualifying words "in the circumstances of the present case" employed by the ECJ in Tetra Pak II, does not seem to be well-grounded. As illustrated above, the rationale for penalising predatory price-cutting under the actual test is to avoid the risk that a competitor is eliminated. Therefore, the focus is on the risk to competitors rather than whether the dominant company recoups its losses or not.

Notwithstanding our empathy for Advocate General Mazak's efforts to align himself with the views of Advocate General Jacobs, who stated in Bronner that "the primary purpose of Art 82 EC is … to safeguard the interests of consumers … rather that to protect the position of particular competitors,"29 he did not manage to find—besides his own opinion—any solid foundation upon which to base his new approach to predatory price-cutting under Article 82 EC.

In the light of the above reasons, it appears difficult, even controversial, to claim a basis for the AG's call for a new test of predation in the Court's case law. It would have been more credible to expressly advise the Court to change its approach to predatory price-cutting rather than trying to achieve this outcome by reinterpreting its case law.

C. The ECJ Judgment

1. The First Plea

Under the first plea, France Télécom claimed that that the CFI failed to state reasons with respect to the rejection of the arguments it set forth in first instance regarding the need to prove the possibility of recoupment of losses and the right for a dominant firm to align its prices on those of its competitors. The ECJ divided the plea in two parts.

First, the ECJ examined the applicant's argument regarding the test of predation. France Télécom argued that the ECJ in its Tetra Pak II judgment concluded that the Commission was not required to prove the possibility of recouping losses in the

circumstances of the case. Therefore, it continued, when the CFI applied the approach set in Tetra Pak II, it should have stated how the circumstances of the case resembled the ones in Tetra Pak II and thus justified the same treatment. The Commission responded that the ECJ's case law did not require it to demonstrate that the recoupment of losses was not possible and that the CFI stated sufficient reasons to reject the appellant's plea.

When examining the first part of the first plea, the ECJ first noted that the obligation to give reasons does not mean that the CFI is obliged to respond in detail to every single argument advanced, especially if the argument is not clear and precise.[30] The ECJ then pointed out that in *Akzo* and *Tetra Pak II* it had already found, first, that prices below average variable costs must always be considered abusive and, second, that prices below average total costs but above average variable costs may be considered abusive if an exclusionary intention is shown. The ECJ then analyzed the first instance judgment, concluded that the CFI had applied the same reasoning as in *Tetra Pak II*, and agreed that the Commission had good grounds for finding that the pricing practice concerned was eliminatory. The CFI found that the prices charged by WIN were, as in *Tetra Pak II*, below average variable costs and that, concerning total costs, the Commission had also provided evidence that the pricing practice adopted by WIN formed part of a plan to "pre-empt" the market. The ECJ concluded that the circumstances of the case were analogous to those in *Tetra Pak* because for a part of the relevant period, WIN's prices were below average variable costs and for the other part, below total costs with a predatory intent. Therefore, the CFI had sufficiently stated reasons to uphold the conclusions of the Commission on this point.

In the second part of the first plea, France Télécom argued that the CFI failed to state adequate reasons for rejecting its argument that an undertaking in a dominant position has the right to align its prices with those of its competitors. The Commission contended that France Télécom had invoked an absolute right for every undertaking to align its prices with those of its competitors, even if it is in a dominant position and its prices are below its cost. The Commission asserted that the CFI properly ruled that such right does not exist.

The ECJ found that the CFI had indeed sufficiently stated reasons to explain why it is not possible to rely on the *Akzo* decision to justify the existence of an absolute right for a dominant firm to meet prices of its competitors regardless of abuse of its dominant position. The ECJ therefore rejected the first plea in its entirety.

2. The Second Plea

According to France Télécom, the CFI infringed article 82 EC by denying WIN the right, recognized by the case-law, to align its price in good faith on those of its competitors. Furthermore, it contested the CFI's failure to assess whether the measure taken by WIN to align its prices with those of its competitors were reasonable and proportionate. The Commission contested the existence of an absolute right for a dominant firm to align its prices with those of its competitors, even when this would imply applying prices below its variable costs. The Commission also contended that France Télécom had raised the issue of whether the CFI should have verified that the measures adopted by WIN were proportionate and reasonable for the first time on appeal, without arguing that the CFI erred in law or provided a contradictory motivation.

The ECJ concluded that France Télécom's first argument, relating to the right for a dominant firm to align, in good faith, its prices with those of its competitors, was inadmissible as France Télécom failed to explain in what way the CFI violated article 82 EC. The ECJ found also the second argument inadmissible, as the need to verify the reasonability and proportionality of the measures taken by WIN to align its prices with those of its competitors was raised for the first time on appeal. The ECJ therefore rejected the second plea.

3. The Seventh Plea

The seventh plea was divided in two parts by the ECJ. In the first, France Télécom argued that the CFI violated article 82 EC, by failing to recognize that the ECJ's case law requires demonstration of the possibility of recouping losses in order to prove predation. The Commission responded that the ECJ's case-law does not require such a demonstration. In addition, the Commission argued that below-cost prices violate article 82 EC if they are applied by a dominant firm, which by definition is capable of pricing over the competitive level and recouping losses incurred by predation. Therefore under EU law, unlike U.S. law, recoupment need not be demonstrated. Finally the Commission argued that in a market with exponential growth, such as the one for high speed internet access services, recoupment would have been likely.

The ECJ first observed that the objective of article 82 EC is to avoid distorting the structure of a market in which competition is already weakened because of the presence of the dominant firm. Such distortions may include not only actions that directly harm consumers but also those that, by eliminating competitors through means other than competition on the merits, weaken the competitive structure of the market. Then the ECJ pointed to the case law and noted (1) that prices below average variable costs must be considered abusive *per se*, as it can be presumed that the dominant firm, in applying such prices, pursues no other economic objective save that of eliminating its competitors; and (2) prices below average total costs but above average variable costs are to be considered abusive only in the context of a plan having the purpose of eliminating a

competitor. The ECJ thus concluded that the proof of the possibility of recoupment of losses is not required by the case-law. The ECJ noted, however, that this does not preclude the Commission finding that recoupment is a relevant factor in assessing whether a practice is abusive.

The ECJ then recalled that in the past it had already dispensed with the possibility of recoupment when the eliminatory intent of the dominant firm could be presumed from the fact that it charged prices lower than average variable costs. The Court also pointed out that the impossibility of recouping losses does not prevent a dominant firm from strengthening its dominant position, especially when successful in eliminating one or more of its competitors. The ECJ concluded that the CFI was right in finding that proof of the possibility of recouping losses is not a necessary precondition for a finding of predatory pricing.

In the second part of the seventh plea, France Télécom claimed that it had submitted evidence that recoupment of losses was impossible and that the CFI did not examine this argument. The Commission argued that this argument was not raised in first instance and that it was therefore inadmissible. The Commission argued further that, in any event, the argument was implicitly rejected by the CFI. Finally, the Commission pointed out that the contested decision had expressly concluded that recoupment was possible.

The ECJ found the second part of the seventh ground to be manifestly unfounded, as France Télécom had not raised in first instance any plea contesting the Commission's disregard of evidence submitted by WIN to prove that recoupment of losses was impossible.

III. COMMENT

In *France Télécom*, the ECJ seized the opportunity in the first predatory pricing case before it since *Tetra Pak II* to have a say in the debate over the need to prove the possibility of recoupment of losses and clarify certain ambiguities in its case-law concerning the test for predation.

Over the years, various commentators have promoted a change of direction in the approach to predatory pricing in the EU and have suggested the adoption of a more economic analysis, largely inspired by the U.S. practice, which includes proof of recoupment. The limited number of cases brought by the Commission against dominant companies for predatory pricing, however, failed to prove reform urgent, or even necessary. Yet the Court seems to have had those critics in mind when it set as a starting point of its analysis the classic definition of dominance provided for in *Hoffman Laroche*,[31] where a dominant position is described as "a position of economic strength enjoyed by an undertaking which enables it … to behave to an appreciable extent independently of its competitors, its customers and ultimately of the consumers." The Court thus set the ground for the rest of its reasoning by affirming, albeit implicitly, that the conditions for sanctioning a predatory pricing practice are profoundly different on the two sides of the Atlantic.

The message inherent in the ECJ's reasoning is that only a dominant firm, that is, an undertaking that by definition can act independently from its competitors and customers and that is already in a position to set its prices above the competitive level, can be found to infringe article 82 by selling at a loss.

In particular—the Court seems to suggest—in the Community system, proof of recoupment would be redundant if added to the one of dominance. The two would overlap to a significant extent, as both aim to show whether the conditions of competition in a given market allow the perpetrator of the infringement to apply prices above the competitive level, with the important difference that in the case of dominance the market power is pre-existing and not a consequence of the infringement. This seems to be confirmed by the fact that the ECJ recalled, almost obsessively, that competition is weakened in the market in which the dominant firm is active.[32]

The ECJ concluded its reasoning, in paragraph 117 of the judgment, by observing that even when recoupment is not possible, the elimination of competitors in itself damages customers by reducing their choices. We would add—expanding on the ECJ's reasoning—that it reduces pressure on the dominant firm to innovate, improve the quality of its products and, why not, reduce prices. In any event, as suggested by the Court at paragraph 117, recoupment may be a "relevant factor" in assessing, notably from an *ex post* standpoint, whether or not the practice concerned is abusive.

Thus, with the *France Télécom* judgment, the ECJ decided to go beyond the stale debate over which interest EU competition law intends to protect. Without recalling that long debate and its origins, it suffices to say here that such interest has variously been identified as the protection of competition, competitors or customers. The Court seems to want to convey the message that the protection of customers overlaps with the protection of competition between a plurality of undertakings. In other words, the ECJ, while confirming the latest trend of the European Courts, which favors the protection of customers over that of competitors, has nevertheless indicated that the interests of customers can only be protected by ensuring that a plurality of operators are active in the market.

On a separate note, it is worth pointing out that the ECJ confirmed that a dominant undertaking cannot justify its commercial practice by invoking a "meeting competition defence" when its prices are below average variable costs or, if a predatory intent can be proven, above average variable costs but below its total costs. After the *France Télécom* judgment, it may be stated that "To recoup or not to recoup? That *was* the question."

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[1] E. ELHAUGE AND D. GERADIN, GLOBAL COMPETITION LAW AND ECONOMICS 314 (2007).

[2] We refer in particular to Cases C-62/86, Akzo v. Commission, 1991 E.C.R. I-3359, and C-333/94 P, Tetra Pak v. Commission, 1996 E.C.R. I-5951 (*Tetra Pak II*).

[3] Case C-62/86, Akzo v. Commission, 1991 E.C.R. I-3359 ¶¶ 71-72.

[4] C-333/94 P, Tetra Pak v. Commission, 1996 E.C.R. I-5951 (*Tetra Pak II*), ¶ 44.

[5] Case C-202/07 P, *France Télécom SA v. Commission*, 2009 E.C.R. ____.

[6] Available at http://ec.europa.eu/competition/antitrust/art82/index.html.

[7] Commission decision COMP/38.233 – Wanadoo Interactive.

[8] According to the decision, in the case of Wanadoo ADSL, at the material time, the customer had to pay a monthly subscription to France Télécom for the service and the ADSL modem rental, together with a subscription to WIN as its internet service provider ("ISP"). In the case of the eXtense service, the modem was bought by the user who paid only a monthly subscription to WIN corresponding to the service supplied by France Télécom and the flat-rate unlimited internet access.

[9] Judgment of the Court of First Instance of the European Communities of 30 January 2007 in Case T-340/03 *France Télécom v. Commission*, 2007 E.C.R. II-107, ¶ 130.

[10] *Id.*, ¶ 138.

[11] *Id.*, ¶ 153.

[12] *Id.*, ¶¶ 165-169.

[13] *Id.*, ¶ 186 .

[14] *Id.*, ¶ 187.

[15] *Id.*, ¶ 188.

[16] *Id.*, ¶¶ 195-198.

[17] *Id.*, ¶¶ 199-215.

[18] *Id.*, ¶¶ 219-223.

[19] At the origin of this case, the Commission found that Tetra Pak, which has 90% market share of the aseptic cartons market, had engaged in predatory pricing in the market for non-aseptic cartons. On appeal before the ECJ, Tetra Pak argued that evidence of the recoupment of losses after the competitor's exit was a "constitutive element in the notion of predatory pricing." C-333/94 P, Tetra Pak v. Commission, 1996 E.C.R. I-5951 (*Tetra Pak II*), ¶ 40. It did so because, since the sales below cost took place in the non-aseptic cartons market, in which it did not have a dominant position, Tetra Pak had no realistic chance of recouping its losses later.

[20] Judgment of the Court of First Instance of the European Communities of 30 January 2007 in Case T-340/03, *France Télécom v. Commission*, 2007 E.C.R. II-107, ¶¶ 224-229.

[21] An Advocate General is a member of the ECJ whose role is to present, upon request of the Court, an independent and impartial opinion on cases that present novel or unresolved issues. The opinions are fully reasoned, set out the relevant facts and legislation, discuss the issues raised and provide a non-binding recommendation to the judges.

[22] Opinion of Advocate General Mazák in Case C-202/07 P, *France Télécom SA v. Commission*, 2009 E.C.R. ____ (Sept. 25, 2008).

[23] *Id.*, ¶ 43.

[24] *Id.*, ¶ 51.

[25] *Id.*, ¶ 69 of the AG opinion. *But see* R. WISH, COMPETITION LAW 650 (4th ed. 2001).

[26]Case 85/76, *Hoffmann-La Roche v. Commission*, 1979 E.C.R. 461.

[27] *See*, *e.g.*, BELLAMY & CHILD, EUROPEAN COMMUNITY LAW OF COMPETITION § 10.071, at 956-57 (6th ed. 2008) ("To the extent that [the *Akzo* rule] implies a rule that pricing below average variable costs … must be predatory, it seems too rigid. Prices below [average variable costs] may be set pro-competitively …"); M. MOTTA, COMPETITION POLICY 453 (2004); J. FAULL AND A. NIKPAY, THE EC LAW OF COMPETITION § 4.287, at 379 (2007); A. EZRACHI, EC COMPETITION LAW 136 (2008); WHISH, R., COMPETITION LAW 649 (4th ed. 2001); A. JONES AND B. SUFRIN, EC COMPETITION LAW 339 (2001); L. Garzaniti and F. Liberatore, *Recent Developments in the European Commission's Practice in the Communications Sector: Part 2*, 2004 E.C.L.R. 25(4), at 234-240.

[28] Judgment of the Court of First Instance of the European Communities of 30 January 2007 in Case T-340/03, *France Télécom v. Commission*, 2007 E.C.R. II-107, ¶ 226 (emphasis added).

[29] Case C-7/97, 1998 E.C.R. I-7791, ¶ 58.

[30] Cases C-120/06 P and C-121/06 P, ¶ 91; *see also* Case C-404/04 P, *Technische Glaswerke Ilmenau v. Commission*, 2007 E.C.R. I-1, ¶ 90; Case C-197/99 P, *Belgium v. Commission* 2003 E.C.R. I-8461, ¶ 81; Case C-274/99 P, C*onnolly v. Commission*, 2001 E.C.R. I-1611, ¶ 121; .

[31] Case 85/76, *Hoffmann-La Roche v. Commission*, 1979 E.C.R. 461, 38. *See also id.* at ¶ 103.

[32] *See* Case C-202/07 P, *France Télécom SA v. Commission*, 2009 E.C.R. ____, ¶¶ 104, 107 and 112.