Case at a Glance

Ross-Simmons operated a hardwood sawmill in Washington State from the 1960s until it went out of business in 2001. The defunct company filed a Section 2 case against Weyerhaeuser accusing the company of overpaying for the alder sawlogs and stockpiling these inputs in order to drive out competition from the regional market for sawlogs. In this case, the Supreme Court will review its precedent on predatory pricing claims in the context of a buyer-side monopoly (or monopsony).

What Is the Legal Standard for Determining When Bidding Is Predatory?

by Shubha Ghosh

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Issue

Can an antitrust plaintiff alleging predatory buying establish liability by persuading a jury that the defendant purchased more inputs "than it needed" or paid a higher price for those inputs "than necessary," so as to prevent the plaintiffs from obtaining the inputs they needed at a fair price, or must the plaintiff meet the higher standard of the two-part test established by the Supreme Court for predatory selling in *Brooke Group, Ltd. v. Brown & Williamson Tobacco Corp.,* 509 U.S. 209 (1993)?

Facts

As the district court opinion describes, this dispute arose from "the forests west of the Cascade Mountains in Oregon and Washington," which "contain enough hardwood lumber to support the only concentration of hardwood sawmills in the western United States." These mills constitute the "alder industry," named after the region's principal hardwood species, which, as the district court opinion states, "accounts for 95% of the annual Pacific Northwest hardwood lumber production." The supply of alder sawlogs is at the heart of this case. From 1998 to 2001, the price of alder sawlogs rose while the price of finished lumber, made from the alder sawlogs, went down. This unusual movements in prices forced Ross-Simmons, an established sawmill in the region, to incur large losses and to shut down. Ross-Simmons attributed the price fluctuations and the mill's eventual demise to the conduct of Weyerhaeuser, one of the largest manufactures of hardwood lumber in the world, which entered the alder sawlog market in 1980 when it acquired a regional sawmill. Throughout the 1980s and '90s, Weyerhaeuser acquired six other sawmills and, by 2001, had a 65 percent share of the Pacific Northwest alder sawlog market.

Most striking about the case are the contrasting pictures painted by the petitioner and respondent of the facts leading up to this dispute. Weyerhaeuser depicts the alder sawlog market as one of vigorous competition in which an integrated

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company took advantage of economies of scale to "extract higher value [from] the existing log flow and raw materials." Ross-Simmons portrays the market as one predated by Weyerhaeuser who started a campaign to monopolize the market in 1980 when it purchased two sawmills in Washington. What Weyerhaeuser portrays as healthy price competition, Ross-Simmons portrays as an aggressive and predatory bidding, purchasing, and stockpiling of raw materials in order to foreclose competition from smaller mills in the region.

Weyerhaeuser points out that while nine mills shut down in the Pacific Northwest during the period of alleged predation, four new mills opened and others expanded operations. Ross-Simmons, with a jury verdict on its side, points to Weyerhaeuser's practice of acquiring mills and expanding its market share during the 1990s. In part, these contrasting portraits are at the heart of the difficult issue of determining when aggressive competition is really a ploy to monopolize a market through anti-competitive practices.

Case Analysis

Ross-Simmons claimed that Weyerhaeuser violated Section 2 of the Sherman Act, 15 U.S.C. § 2, by overpaying for alder sawlogs and stockpiling what it purchased with the aim of driving out competing sawmills and monopolizing the alder sawlog market in the Pacific Northwest. Once competition had been removed, according to Ross-Simmons, Weyerhaeuser planned to recoup its losses from overpaying for the sawlogs by using its market power to reduce future prices paid for the logs. In support of its theory, Ross-Simmons introduced evidence at trial showing that sawlog prices increased during the period of alleged predation, that the price of finished lumber had decreased, and that Weyerhaeuser had suffered a decline in profits as a result of its overpayments for the logs.

Weyerhaeuser moved for summary judgment and for a judgment notwithstanding the verdict, arguing each time that Ross-Simmons failed to meet the standard established by the Supreme Court in its 1993 *Brooke Group* decision. At issue in *Brooke Group* had been a claim of predatory pricing brought against a seller of a product who allegedly underpriced his tobacco products to consumers in order to drive out competitors on the theory that the seller could recoup the lost profits by raising price after monopolizing the market. The Supreme Court held that a plaintiff must show two elements in order to make a case for predatory selling: (1) the plaintiff must show that the prices are below some measure of the rival's costs and (2) the plaintiff must show that the defendant had a dangerous probability of recouping its investment in below-cost pricing. By analogy, Weyerhaeuser argued that Ross-Simmons's claim of predatory buying could survive only of it showed that (1) Weyerhaeuser sold its product at a loss because of the overpayments for the raw materials and (2) Weyerhaeuser could recoup these losses after predation. Since Ross-Simmons failed to satisfy either element required by the *Brooke Group* decision, judgment should have been in Weyerhaeuser's favor.

The district court denied Weyerhaeuser's motion for summary judgment and its motion for judgment notwithstanding the verdict. In ruling on the summary judgment motion, the district court stated that it saw "no practical difference between predatory pricing that results in a company purposely selling a product at a loss of one cent per unit, versus selling the same product at a profit of only one cent per unit when the company would have earned a larger profit but for its anticompetitive conduct." In other words, the district court concluded that, contra *Brooke Group,* Ross-Simmons did not have to show a loss to establish predatory conduct since the decision to pursue reduced profits also supported an inference of anti-competitive conduct.

Consistent with the district court's rejection of *Brooke Group,* the United States Court of Appeals for the Ninth Circuit affirmed, rejecting Weyerhaeuser's arguments in favor of the two-part *Brooke Group* test. The Ninth Circuit was more categorical in its reasoning. While the appeals court did acknowledge the two-prong test, the court concluded that the test did not apply to the buyer-side predatory bidding context. The heightened standard of *Brooke Group* was developed for a case of predatory selling in order to balance the pro-competitive benefits of lower prices that are created by seller predation with the anti-competitive harms of potentially monopolizing the market. In the case of buyer-side predatory bidding, there are no benefits to consumers from a firm bidding up the price of an input, and therefore evidence of such conduct would be a basis for violation of Section 2 of the Sherman Act.

The appeals court also suggested that the *Brooke Group* analysis would not apply when the supply of a product is insensitive to price, or price inelastic. Because of this inelasticity, the court reasoned, Weyerhaeuser was able to bid up the price of the logs and reduce the quantity of this resources available to its competitors. Consequently, the Ninth Circuit affirmed the district court's decision not to instruct

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the jury on the *Brooke Group* factors. The court also affirmed the instructions to find liability if Weyerhaeuser purchased more logs than needed, paid a higher price than necessary, and prevented Ross-Simmons from obtaining logs at a fair price. Finally, the court affirmed the verdict based on Weyerhaeuser's conduct in purchasing the logs, its intent to monopolize, and the dangerous probability of achieving monopoly power in the relevant market.

Weyerhaeuser has asked the Supreme Court to reverse the Ninth Circuit and hold that *Brooke Group* is applicable to a case of buyer-side predatory bidding. The petitioner's principal argument is that the two-prong test provides some clarity to predatory pricing claims and that the lower court's distinction between predatory selling and predatory buying is inconsistent with the policy rationale of *Brooke Group* and the trend in antitrust jurisprudence on predatory pricing claims.

Weyerhaeuser's first argument is that clear rules are needed in order to distinguish predatory behavior from aggressive, and beneficial, competition. A theme running through Weyerhaeuser's arguments is the dangers of punishing competitive behavior that can benefit consumers and the marketplace. The two-factor test of *Brooke Group* provides a clear, understandable approach to distinguish beneficial competition from predation and to prevent "false positives," or successful antitrust claims against beneficial conduct. The first requirement that the plaintiff show that the defendant's costs exceeds its revenues is evidence that the defendant is engaging in non-profit maximizing behavior that is entered into to deter competition. The second requirement that the defendant can recoup its lost profits supports the argument that the defendant is using a future monopoly position to offset the losses of predatory conduct. Absent either of these elements, however, the case for predation cannot be made.

Weyerhaeuser contrasts the *Brooke Group* approach with the Ninth Circuit's "fair price" approach that tends to penalize legitimate competition since it provides no guidance for juries in determining predation. The Ninth Circuit approach, as characterized by Weyerhaeuser, punishes efficient conduct by a firm that attempts to acquire inputs on the marketplace and rewards inefficient firms that could not compete in the market for the inputs. The "fair price" approach rests on assessing when the defendant has crossed the line in acquiring too much of an input that results in unfair prices for competitors. By deterring effective competition, the Ninth Circuit's approach forecloses beneficial competition among buyers that can promote the interest of consumers in the marketplace.

Ross-Simmons's brief rested on its allegation that Weyerhaeuser was engaged in a scheme to monopolize the alder sawlog market in the Pacific Northwest, of which predatory bidding was only one part. According to Ross-Simmons, Weyerhaeuser's conduct has been clearly harmful to consumers and competition and poses significant risk to innovation and growth in the marketplace. Although Weyerhaeuser's practice of bidding up the price of alder sawlogs had benefitted suppliers, these gains are short term and will be offset in the future when Weyerhaeuser monopolizes the market and drives down the price of alder sawlogs paid to suppliers and raises the price of finished lumber paid by consumers. Critical to Ross-Simmons's argument are the high barriers to entry in the market, coupled with limited raw materials, and Weyerhaeuser's bidding practices and dominance in the marketplace, all of which make the alder sawlog market particularly susceptible to monopolistic practices.

The *Brooke Group* precedent received much attention in Ross-Simmons's argument. The 1993 Supreme Court precedent is based on the premise, derived from the economics literature, that predatory pricing is economically irrational and rarely successful. Furthermore, predatory pricing theory, which states that a firm lowers prices below costs to drive out competitors with the intent of monopolizing a market, contradict basic principles of competition that lowering prices is good for consumers and stimulates competitive pressures on incumbent firms. Given the skepticism with which scholars and practitioners have traditionally greeted predatory pricing claims, the two-factor test in Brooke Group was designed to make it difficult for plaintiffs to pursue predatory pricing claims by heightening the legal requirements.

Predatory buying claims, however, are distinguishable from predatory pricing claims because of the absence of benefits either to consumers or to the competitive process. A predatory buying theory rests on a firm bidding up the price of a resource used in production and then stockpiling that resource in order to make it difficult for competitors to produce the final product and supply the market. Consumers do not benefit from the higher price for the resource used to produce the final product. The main beneficiaries are the suppliers of the resource. But, as Ross-Simmons

points out, these benefits are short term and inure to a small group of existing suppliers. In a situation in which the supply of the resource is inelastic and insensitive to price, the increase in the price of alder sawlogs will not lead to new loggers entering the marketplace or to innovations in the industry. Instead, Ross-Simmons contends, Weyerhaeuser's bidding practices will reduce the supply of logs available to other sawmills, which will be forced out of the marketplace as Ross-Simmons was. Consequently, the two-part *Brooke Group* test is completely inappropriate to the facts of a predatory buying claim, and the Ninth Circuit's decision should be affirmed.

The heart of the argument before the Supreme Court is the parallel between predatory pricing and predatory bidding theories under the Sherman Act. Weyerhaeuser is urging identical treatment while Ross-Simmons advocates different approaches. Each argument invokes the policies of the Sherman Act to promote competition and benefit consumers, the logic of predatory pricing and bidding practices, and the economics of the alder sawlog market.

SIGNIFICANCE

The Supreme Court's decision will be watched closely. Not only will it provide some insight on the direction of the law governing predatory pricing claims, but it will also illustrate how the Roberts Court will embrace the last 30 years of Supreme Court antitrust jurisprudence with its pro-business perspective informed by economics. Weyerhaeuser's arguments ask the Court not only to test the scope of its *Brooke Group* precedent, but also to articulate its methodology in approaching antitrust claims.

The foremost issue is the scope of the *Brooke Group* decision. If the Court follows Weyerhaeuser's argument and treats predatory pricing and predatory bidding claims identically, the Court will have upheld its precedent, but, in the process, will have ignored the substance of the claims. As the district court and the Ninth Circuit each emphasized, predatory pricing and predatory buying have different implications, and the policies that make the former a suspect theory does not necessarily apply to the latter. Whether the Supreme Court will delve into the underlying economics is revealing about the direction of the Court.

Recent cases demonstrate that the Court may be of two minds on this point. In *Trinko v. Bell Atlantic Corp.,* 540 U.S. 398 (2004), the Supreme Court was adamant in not second guessing how Congress intended to structure the telecommunications industry and allowing an antitrust claim that would upset that balance. In *Trinko,* the Court was hesitant to allow a plaintiff to challenge the underlying economics through a Sherman Act claim. However, in *Illinois Tool Works v. Independent Ink,* 126 S.Ct. 1281 (2006), the Court was willing to acknowledge economic thinking and analysis on the question of whether ownership of patent conferred market power. However, the Court's embrace of economic analysis was the basis for a decision that made it more difficult to bring a Sherman Act claim. The *Weyerhaeuser* case asks the Court to embrace economics in a situation in which it would be easier to bring an antitrust action. It will be interesting to see if the Court will be symmetric in how it uses and addresses economic arguments in settling antitrust disputes.

In addition, the case will offer some insight into how the Court views its own precedent. In *Illinois Tool,* the Court was very forthcoming in both rejecting and clarifying its precedent in the areas of antitrust and intellectual property. If the Court follows Weyerhaeuser, it may be signaling its reluctance to abandon its precedent absent strong justification. Such an approach would be consistent with Justice Roberts's comments about how some precedents are stronger than others and are a kind of "super precedent." If the Court follows one implication may be that antitrust precedent on predatory market practices is a super precedent. On the other hand, if the Court affirms the Ninth Circuit, it will be instructive to see how the Court distinguishes its own precedent. The Court's approach will signal its attitude toward antitrust law and its particular balance between formal rules and particularized facts.

Finally, antitrust practitioners will look to the Court's decision to see if it takes a more liberal or restrictive approach to antitrust litigation, whether based on theories of predation or other claims. Following Weyerhaeuser would mean that the Court is wary about antitrust claims, especially ones that some have argued are being brought by a failed business that is seeking to use antitrust law for vindication. However, following Ross-Simmons would indicate a willingness to consider antitrust claims that challenge existing precedent and blend economic and legal perspectives. The Court's opinion in this case that so intriguingly blends legal and economic arguments should promote heated discussion and continue the debate on the proper treatment of predatory behavior under the Sherman Act.

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