No. 92-466

In The

Supreme Court of the United States

October Term, 1992

LIGGETT GROUP INC., now named Brooke Group Ltd.,

Petitioner,

vs.

BROWN & WILLIAMSON TOBACCO CORPORATION,

Respondent.

On Writ Of Certiorari
To The United States Court Of Appeals
For The Fourth Circuit

BRIEF FOR THE PETITIONER

PHILLIP AREEDA
1545 Massachusetts Avenue
Cambridge, Massachusetts
02138
(617) 495-3160
Counsel of Record

Of Counsel
CHARLES FRIED
1545 Massachusetts Avenue
Cambridge, Massachusetts
02138
(617) 495-4636

(*For Complete Appearances See Reverse Side Of Cover*)

Of Counsel

JEAN E. SHARPE
BROOKE GROUP LTD.
65 East 55th Street
New York, New York 10022
(212) 486-6100

JOSIAH S. MURRAY, III
JAMES W. DOBBINS
LIGGETT GROUP INC.
300 North Duke Street
Durham, North Carolina
27702
(919) 683-8802

WILLIAM H. HOGELAND, J
ANTHONY M. D'IORIO
MUDGE ROSE GUTHRIE
ALEXANDER & FERDON
180 MAIDEN LANE
NEW YORK, NEW YORK 10(
(212) 510-7000

GARRET G. RASMUSSEN
C. ALLEN FOSTER
KENNETH L. GLAZER
PATTON, BOGGS & BLOW
2550 M Street, N.W.
Washington, D.C. 20037
(202) 457-6000

QUESTIONS PRESENTED

In a highly concentrated industry with long maintained supracompetitive prices and profits, the jury found that respondent's admitted price discrimination had a reasonable possibility of injuring competition in violation of the Robinson-Patman Act. Substantial evidence showed that respondent succeeded in raising prices, having expressly undertaken to harm consumers by disciplining a price-cutting rival through sustained discriminatory pricing below cost, after an express and accurate analysis of how it would recoup its predatory investment. The Court of Appeals immunized these acts. In its view of "economic logic," such disciplinary pricing was implausible because only a monopolizing or conspiring predator could ever recoup its investment in below-cost disciplinary pricing. The case presents the following questions:

1. Does the Robinson-Patman Act's prohibition of price discrimination that "may substantially lessen competition or tend to create a monopoly . . . or injure . . . competition with [the discriminating seller]" retain independent force or does it address only a monopoly or conspiracy already covered by the Sherman Act?

2. May a court's theoretical speculation about the rational calculations of a hypothetical oligopolist vitiate a jury verdict based on the calculations, conduct, and success of the actual respondent?

3. Even accepting the Court of Appeals' erroneous conclusion that consumers were not injured, must actual injury to consumers -- as distinct from a reasonable threat of injury -- be demonstrated before Robinson-Patman Act liability can be found?

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page

STATUTES

MISCELLANEOUS

JURISDICTION

The Supreme Court has jurisdiction pursuant to 28 U.S.C. § 1254(1). The petition for a writ of certiorari was granted on November 16, 1992.

STATUTE INVOLVED

The statutory provision involved in this case is Section 2(a) of the Robinson-Patman Act, 15 U.S.C. § 13(a), reprinted in full at Pet. App. 54a[1], which provides in relevant part:

> It shall be unlawful for any person . . . to discriminate in price . . . where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce . . . or injure, destroy, or prevent competition with any person who . . . grants . . . such discrimination . . .

STATEMENT OF CASE

A. Summary

The jury found that price discrimination by respondent-defendant Brown & Williamson Tobacco Corp. ("B&W") had a "reasonable possibility of injuring competition in the cigarette market as a whole" in violation of the Robinson-Patman Act. J.A. 27. The instructions had defined such injury in terms of "loss-creating price cutting" with the "real possibility" that B&W could "recoup" the resulting losses "by raising and maintaining prices at higher than competitive levels" after having disciplined petitioner-plaintiff Liggett

---

[1] In this brief, Liggett's Petition for a Writ of Certiorari is cited as Pet. App. ___; the Joint Appendix filed simultaneously with this brief is cited as J.A. ___; an exhibit admitted into evidence at trial is cited as PX or DX ___; and the official transcript from the District Court is cited as Tr: (volume)-(page).

Group Inc. ("Liggett").[2] Instr. No. 12, J.A. 829-30. Substantial evidence showed that

- The cigarette industry is a highly concentrated oligopoly in which supracompetitive prices and profits on so-called full-price or full-revenue ("regular-brand") cigarettes were protected from entry by new firms but were threatened by deeply discounted cigarettes in plain "black-and-white" packages which were introduced in 1980 by Liggett, the smallest of the six oligopolists.

- To discipline Liggett, B&W offered black-and-white cigarettes and sold them for at least 18 months at discriminatory prices that were consistently below their average variable cost and that were not introductory, promotional, or intended in good faith to meet competition.

- These prices were expressly designed to inflict losses upon Liggett that would -- and did -- subsequently force it to raise its black-and-white prices, thereby allowing generic prices to rise more rapidly than regular-brand prices, narrowing the generic discount and extracting higher prices from consumers.

- B&W stated that it would signal its intentions to fellow oligopolists and expressly analyzed their prospective behavior, accurately predicting that some of them would enter the generic segment with the intention -- like that of B&W -- of managing generic prices upwards and narrowing the discount from the regular-brand cigarettes that were the industry mainstay.

---

[2] Pursuant to Supreme Court Rule 29.1, petitioner provides the following corporate information. Liggett, now named Brooke Group Ltd., is a publicly owned corporation which holds a controlling interest in New Valley Corporation and MAI Systems Inc. Brooke Group Ltd. has no parent corporation.

- The generic discount did shrink, all prices rose faster than costs or inflation, and B&W expressly took credit for slowing the growth of disruptive generics.

The District Court gave B&W judgment notwithstanding the verdict. The Court of Appeals affirmed on the ground that only an express cartel or prospective monopoly provides sufficient assurance of recoupment to make predatory pricing plausible. (In this brief, the term "predatory pricing" includes, and is used interchangeably with, "disciplinary pricing" that has the purpose or effect of pressuring a rival to behave less competitively -- as, for example, by raising prices.[3])

B. Legal Background

In order to reach anticompetitive conduct not already covered by the 1890 Sherman Act, the 1914 Clayton Act condemned certain price discrimination threatening competition between the discriminating seller and its rivals. Such "primary-line" competition continues to be a key concern of that statute as amended by the Robinson-Patman Act in 1936.[4]

This is a primary-line case. Price discrimination is unlawful when its effect "may be substantially to lessen competition or tend to create a monopoly . . . or to injure, destroy, or prevent competition with [the discriminating seller] . . . " 15 U.S.C. § 13(a). According to this Court, there is such an effect when there is a "reasonable

---

[3] B&W's economic experts also defined "predation" this way. J.A. 650, 657. *See also* Tr. 61: 229-30.

[4] *See FTC v. Anheuser-Busch, Inc.*, 363 U.S. 536, 544 (1960) ("the legislative history of [the Robinson-Patman] amendments leaves no doubt that Congress was intent upon strengthening the Clayton Act provisions, not weakening them, and that it was no part of Congress' purpose to curtail the pre-existing applicability of § 2(a) to price discriminations affecting primary-line competition.").

possibility" of injuring competition.[5] The jury was so instructed. Instr. No. 12, J.A. 829.

Through the 1960s, many courts affirmed findings of primary-line injury based upon mere evidence of price discrimination "intended" to injure competition or even competitors.[6] This Court's decision in *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685 (1967), has often been read to endorse this approach, although the Court did emphasize the defendants' below-cost prices. *See infra* p.35.

Since then, lower courts have stated that the required competitive injury may be inferred from (1) an actual worsening of competition in the market or (2) "predatory intent" which may, in turn, be inferred either from express evidence of intention or from pricing below cost. *See infra* note 21. Some courts have also insisted upon an indication that the alleged predator could "recoup" the losses resulting from below-cost pricing. *See infra* pp. 40-41. Recoupment is simply the payoff for below-cost pricing. The recoupment vehicle in most cases and in the standard model is post-predation monopoly for a single firm: A firm voluntarily incurs losses by selling a product for less than its variable cost in order to ruin rivals, gains a monopoly, charges monopoly prices, and earns monopoly profits recouping those earlier losses.

The Fourth Circuit ruled that the standard monopoly model is the only circumstance in which a defendant acting unilaterally would think recoupment likely enough to

---

[5] *See Falls City Indus., Inc. v. Vanco Beverage, Inc.*, 460 U.S. 428, 434-35 (1983); *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685, 698, 702 (1967); *Corn Products Refining Co. v. FTC*, 324 U.S. 726, 742 (1945).

[6] *See generally* F. Rowe, *Price Discrimination Under The Robinson-Patman Act 149* (1962) ("prevailing legal doctrines hold that predatory price discrimination on the part of a seller designed to destroy the competition of a smaller and weaker rival is *prima facie* illegal under Section 2(a).").

undertake unjustified below-cost pricing injurious to competition. Notwithstanding the different recoupment route described in B&W's own planning documents, the court ruled that an oligopolist's unjustified, below-cost and discriminatory price never has a "reasonable possibility of injuring competition." It so ruled without denying the substantial evidence supporting the jury finding that B&W had in fact engaged in such conduct for the purpose of injuring consumers.[7]

C. Facts

1. **The cigarette industry is a highly concentrated oligopoly with supracompetitive prices and profits and high entry barriers.** With the leading three firms (Philip Morris, R.J. Reynolds, and B&W) accounting for 82% of sales, the cigarette industry is one of the most highly concentrated oligopolies in the United States. J.A. 352, 495-98, 652, 744-45. Measured by the so-called Herfindahl-Hirschman index, its 1988 concentration of nearly 2800 far exceeds the 1800 level that the Justice Department and Federal Trade Commission regard as "highly concentrated" and thus as presenting a real danger that oligopolists can maintain supracompetitive pricing without any conspiracy.[8] J.A. 499. The cigarette industry is the textbook example of

---

[7] The party against whom a motion for judgment notwithstanding the verdict is made must be given the benefit of every legitimate inference that can be drawn from the evidence. C. Wright & A. Miller, *Federal Practice and Procedure* § 2528 at 563-64 (1971). Instead of dealing with the evidence supporting the jury verdict for Liggett, the Court of Appeals' statement of the case inexplicably emphasized, without context, the evidence most favorable to B&W.

[8] U.S. Department of Justice and Federal Trade Commission Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶ 13,104 at § 1.5 (1992). The Herfindahl-Hirschman Index is computed by squaring the shares of each firm and then adding them up -- *e.g.*, 1,000 for a market with ten 10% firms.

a stable oligopoly that does not compete on prices;[9] its history of anticompetitive conduct is well documented.[10]

For years cigarette prices have marched upward in lock-step at a rate greater than inflation and cost increases, notwithstanding falling demand. J.A. 500-09, 514-19, 524-26. In classic oligopoly fashion, one company raises its list price and the other five follow immediately. J.A. 501, 429. Prices have increased uniformly twice a year on a regular basis. J.A. 501, 386-89, 404, 425-27. This pattern is so well established that wholesalers raise their resale prices for *all* manufacturers' cigarettes as soon as *one* manufacturer increases its price to wholesalers. J.A. 427-29, 440. In the words of B&W's President, "[O]ne key on the cash register rang up all cigarette sales." J.A. 434, 273.

Cigarette profits -- among the highest of any industry -- have long been at supracompetitive levels. J.A. 481-82, 559, 610, 645. Cigarette manufacturers persistently earn profits that are approximately 50% higher than the average for firms in the broader consumer food and related products industry. J.A. 530-33. Despite falling cigarette consumption, U.S. cigarette manufacturers increased their profits per thousand from $3.80 to $11.55 between 1980 and 1988. J.A. 748. These high profits have been insulated by high barriers to entry, including the government ban on television advertising. J.A. 560-63, 713. No new firm has successfully entered the industry in decades. J.A. 559-60, Tr. 61:230.

Even B&W's economic experts agreed with Liggett's that the cigarette industry is one of the most highly concentrated (J.A. 652, 741-45, 496); that there has been list price uniformity (J.A. 718, 500-09); that there are high barriers to entry (J.A. 713, 560-63); and that there are high accounting rates of return in the cigarette industry (Tr.

---

[9] F. Scherer and D. Ross, *Industrial Market Structure and Economic Performance* 250-251 (3d ed. 1990) (J.A. 748).

[10] *United States v. American Tobacco Co.*, 221 U.S. 106 (1911); *American Tobacco Co. v. United States*, 328 U.S. 781 (1946).

100:221, J.A. 748, 529-31). B&W's expert economist testified that he could think of no explanation consistent with the theory of competition for prices to increase when demand is falling (J.A. 658-59), as happened in the cigarette industry (J.A. 513-25). The Fourth Circuit did not question any of this evidence or the ultimate conclusion that cigarette profits have persisted at supracompetitive levels for a long time.[11]

2. **The oligopoly's supracompetitive profits were threatened by Liggett's deeply discounted black-and-white cigarettes.** In 1980, Liggett -- in B&W's words -- "was on the verge of going out of business" and "made the bold

---

[11] The District Court emphasized the testimony of two senior Liggett executives who were asked -- after a series of questions inquiring whether they were engaged in fixing prices with other manufacturers -- whether the industry exhibited anticompetitive "tacit collusion." Both answered in the negative, testifying that prices were "fair" and that the industry was "competitive," especially during the "price war." Tr. 3:170-82, Tr. 11:170-74.

As the authors of a well-known text explain, "business people . . . view competition" not in its economic sense as the rivalry that eliminates supracompetitive prices and profits, but "as the conscious striving against other business firms for patronage." F. Scherer and D. Ross, *Industrial Market Structure and Economic Performance* 16 (3d ed. 1990). One of B&W's economic experts testified that he would not change his conclusion that a market exhibited supracompetitive profits merely because an industry executive testified that profits were fair and reasonable. J.A. 753-54. B&W's other expert economist explained that he did not use the term "tacit collusion" in his classroom because it was too confusing, perhaps because insufficiently distinguished from illegal conspiracies. J.A. 651.

When asked about facts rather than economic conclusions, the Liggett executives testified that the industry does not compete based on price; that all manufacturers increased the price of regular-brand cigarettes the same amount at the same time; and that the industry, not Liggett, set the price for Liggett's regular-brand cigarettes. J.A. 389-91, 396. This pattern resulted in profits that Liggett's President stated "were the biggest of any industry that I have been associated with, very much so." J.A. 392.

move" of introducing a generic cigarette in a plain black-and-white package at a substantial price discount. J.A. 127-28. B&W's senior executives noted in corporate documents that Liggett's move was "the first time that a cigarette manufacturer has used pricing as a strategic marketing weapon in the U.S. since the depression era." J.A. 128.

B&W's own economic expert acknowledged that Liggett's introduction of black-and-whites "demonstrated independence, a breaking away from the pack" and called Liggett a "maverick." J.A. 715. Liggett's black-and-white generics were deeply discounted, originally at list prices -- which, in practice, determine consumer prices -- 30% below regular-brand cigarettes. J.A. 393-94. By 1984, the discount had grown to almost 40% as Liggett declined to raise black-and-white prices on several occasions when prices rose on regular brands. J.A. 66-67, Pet. App. 6a. As a result, by mid-1984 Liggett's black-and-white cigarettes had grown to 4% of the entire cigarette market (J.A. 52), accounting for the bulk of Liggett's volume and for virtually the entire category of discounted cigarettes through at least 1984 (J.A. 73, 81).[12]

---

[12] This was the case from 1980 until B&W offered its black-and-white generics in mid-1984. (Philip Morris and R.J. Reynolds began offering black-and-whites in 1986 and 1988, respectively -- after B&W had disciplined Liggett).

In April 1984, Reynolds created the "branded generic" category by reducing the list price of its Doral brand to the black-and-white level (and offering a 16 cent rebate to wholesalers purchasing 500 cases quarterly plus, for a time, a 16 cent non-volume rebate -- amounts that never came close to B&W's high-volume rebates of 75 and 80 cents, *see infra* note 15). J.A. 117-18, 327-28. *See also infra* pp. 11-12. Over a year later (and after black-and-white prices began to rise), other manufacturers began to offer branded generics. The list prices of branded generics could more readily be raised than black-and-white prices because they did not bear the inherent discount message of black-and-whites and because they enjoy some brand loyalty. J.A. 108-09. For an account of Liggett's introduction of a so-called "subgeneric" in 1989, see *infra* note 20. →

Consumers and Liggett benefitted from Liggett's price discounting, but as B&W recognized, the other cigarette manufacturers did not. J.A. 82-83. Purchasers of black-and-white cigarettes were not new consumers, but those who previously purchased regular-brand cigarettes. J.A. 132-35, 66. In B&W's words, black-and-white cigarettes "cannibalized" regular-brand cigarette sales and profits. J.A. 107. Liggett was the spoiler threatening the highly profitable price uniformity of the oligopoly. J.A. 565. B&W wrote to its parent company that "the industry's interests -- other than [Liggett's] -- would be far better served had generics never been introduced, they are an immediate and growing threat to all other manufacturers." J.A. 83. According to B&W, "[a]ll other manufacturers face a shrinking industry and eroding share and volume as generics grow." J.A. 83.

B&W was hardest hit. J.A. 132-33. Over 20% of Liggett's generic cigarette consumers had previously patronized B&W brands, even though B&W's share of the cigarette market was 12%. J.A. 128-30. In 1984, B&W calculated that continued growth of black-and-white cigarettes could cost it as much as $350 million in lost revenue by 1988. J.A. 83.

3. **B&W entered the black-and-white segment with an express plan to injure consumers by disciplining Liggett -- a plan from which it never departed.** Lest deep discounted cigarettes continue to draw customers away from its brands and force price reductions (or constrain price increases) on regular brands, B&W executives decided in early 1984 to introduce a look-alike black-and-white cigarette with the same list prices as Liggett but with large and

---

"Generics" originally referred only to black-and-whites (including private label sales) although the term often came to cover the entire discounted category including so-called 25's -- a branded product (*i.e.*, B&W's Richland and Reynolds' Century) in packs of 25 cigarettes at the same price as regular-sized packs of 20. The effective per-cigarette list-price discount was about half (or less) than the discount on black-and-whites. B&W concluded that these "25s are not the answer to generics." Px 7; Tr. 2:199.

discriminatory rebates for wholesalers. J.A. 87-90, 61, 36. B&W did not go into black-and-whites with the objective of making a profit. Rather, it expected to pay rebates that would bring its prices below average variable cost, *see infra* p. 15, predicting that the resulting losses for Liggett would force Liggett to abandon its practice of deepening the list-price discount on generic cigarettes. *See infra* pp. 15-16. The discount had deepened because Liggett was not raising generic prices when regular-brand prices rose. J.A. 66-67. In B&W's words, "Unchallenged, [Liggett] will continue aggressive segment development since it has virtually no stake in the branded, full price market." J.A. 83.

B&W studiously avoided any list-price cuts. Instead, it chose discriminatory rebates to wholesalers as the weapon to inflict losses upon Liggett, paying them retroactively, and thereby "restricting immediate 'pass through' to the trade." [13] Px 634; Tr. 32:11. As B&W explained:

> The B&W proposal is based on offering greater discounts -- not reducing the list price. Since retail pricing is based on list prices, B&W's generics will not enhance the price/value relationship of present generics. J.A. 99, 57-58.

---

[13] True to B&W's predictions, the rebates generally were not passed on. Wholesalers testified that they did not pass on the rebates. Tr. 23: 73-75; Tr. 38:55-57; J.A. 424-25. Liggett, B&W, and Reynolds monitored the price consumers were paying for black-and-whites and observed that the rebates paid wholesalers did not affect the consumer price. J.A. 239 (B&W); Tr. 39:227-28 (Liggett); Tr. 105: 64-65 (Reynolds).

Of course, even if rebates had been passed on to retailers and thence to consumers, B&W's scheme would nonetheless have been predatory. Black-and-white volume would have expanded temporarily, and thereby increased the rebate burden on Liggett as well as on B&W. Whether kept by wholesalers or ultimately received by consumers, the below-cost rebates had the purpose and effect of bringing higher prices later.

B&W's goal was *first*, in its own words, to "prevent[ ] an increase in the percentage pricing spread between generic and branded cigarettes" *and then* to "gradually reduce[ ]" that spread." J.A. 70-72, 280. B&W expressly stated that it wanted to "manage down" demand for the very product it was introducing. J.A. 108-09. It was determined to avoid any action that would "create new consumer demand" or "accelerate segment growth." J.A. 57-58, 87-88. B&W expressly saw "no need to promote or advertise heavily to the consumer" because, rather than attract consumers to a new product, "we [B&W] would be seeking to displace Liggett" at the wholesale level in order to "gradually reduc[e the] percent difference between generics and full revenue brands" and thereby "slow our branded, higher margin losses to generics." J.A. 279, 113-15. This was its persistent objective. J.A. 70-71, 257, 279-80.

Predicting that some of the other oligopolists would enter the discounted segment, B&W analyzed their prospective reactions and concluded that they too would seek to shrink the discount. *See infra* pp. 16-18. As the consumer price of generics increased relative to those of regular brands, B&W reasoned, fewer consumers would be willing to "trade off image for price," and the cannibalization of regular brands would decline or at least not grow as rapidly. J.A. 72, 67-70.

In April-May 1984, B&W revisited -- but did not revise -- its plan when R.J. Reynolds ("RJR"), a larger competitor, lowered the list price of its existing Doral brand to generic levels and offered a small rebate. *See supra* note 12. Though anticipated by B&W, Reynolds' move confirmed B&W's realization that it could not prevent all growth of the generic segment. J.A. 75, 84-85, 141. Nevertheless, B&W reasoned that RJR's objective was consistent with its own; both before and after Doral's repositioning, B&W identified RJR's "Priority One" as

> [l]aunch[ing] a generic product line to gain control of and contain generic segment growth. RJR would strive to limit segment development since incremental generic growth will disproportionately

reduce RJR's total margins. J.A. 84 (before Doral), J.A. 164 (after Doral).

Even so, B&W concluded that its pre-existing program to "offer an equivalent line of generics to [Liggett] at the same list price but at lower net price" to wholesalers provided the "*best opportunity to contain cannibalization of its full revenue branded products and limit segment growth.*" J.A. 112, 114 (emphasis in original). It deemed entry for that purpose "imperative." J.A. 141. It continued to state its objective to be "to displace L&M as the supplier of black and white/private label generics," and repeatedly confirmed that its "plan of action to be followed is exactly as our previous proposal outlined." J.A. 121.

The following year, B&W again reaffirmed its goal to "manage segment growth and profitability by gradually reducing [the] percent difference between generic and full revenue brands." J.A. 279, 280, 257. By April 1985, B&W saw progress toward achieving its goal: "B&W's presence within the segment appears to have resulted in reduced consumer advertising by L&M and a slowing in the segment's growth rate." J.A. 257.

4. **Price discrimination was integral to B&W's plan.** According to B&W's own strategic documents, price discrimination was crucial. J.A. 58, 88-89. B&W believed that discriminatory rebates could discipline Liggett at least cost to B&W because they would "[a]chieve maximum desired volume through a minimum number" of wholesalers, thus reducing B&W's investment in its anticompetitive scheme. J.A. 50, 402-03. As B&W explained (in a textbook account of how discrimination aids predation), discriminatory rebates are "the most cost efficient and effective means" of achieving its goal. J.A. 69.

B&W began to implement its plan in June 1984, initially approaching a "hit list" of Liggett's 14 largest wholesalers, offering them unprecedentedly large rebates for purchases of 1000 or 1500 cases of black and whites per quarter -- a volume which only the very largest wholesalers could ever achieve and which were therefore discriminatory.[14] J.A. 168-69, 174, 412-13. When Liggett responded, though with lesser rebates than B&W's, B&W increased its rebates still further,[15] as it had anticipated it would (J.A. 73-75, 91-92, Px 291; Tr. 27:40), and added a special discriminatory inducement to the few super-buyers of more than 8000 cases per quarter (J.A. 328).

5. **B&W priced its black-and-whites below their average variable cost.** From the date of its first shipment in July 1984 and for the next 17 months through the end of 1985, B&W's net price to wholesalers was 30 cents per carton below its average variable cost. J.A. 339. As B&W's own expert economist conceded, B&W in fact engaged in sustained below-average-variable-cost pricing for 18 months:

---

[14] *FTC v. Morton Salt*, 334 U.S. 37, 42-44 (1948). B&W conceded that its larger discounts were available only to a few, Tr. 46:89, and B&W did not appeal the trial judge's ruling that its different prices were in fact discriminatory. B&W initially offered rebates of 20 cents per carton for customers buying at least 500 cases quarterly, 25 cents for customers buying at least 1000 cases, and 30 cents for those buying at least 1500 cases. J.A. 178-79, 327-28. B&W's per carton payments applied to all B&W black-and-white cigarettes purchased, not just the incremental purchases above the volume threshold, creating a strong inducement for a wholesaler to shift all its generic business to B&W rather than splitting its business between B&W and Liggett. J.A. 70, 180. Prior to B&W's initial offer, Liggett's highest volume offer was 13 cents for purchases above 500 cases per quarter and was conditioned on specified promotional activity. J.A. 179-80, 327, 411-12, Px 15 at 098508; Tr. 2:199. Indeed, prior to B&W's offer, no cigarette manufacturer had ever based a rebate or discount on a quarterly purchase volume nearly as large as 1500 cases. J.A. 413.

[15] J.A. 420-21. For example, when Liggett came within 10 cents per carton of B&W rebates for higher volume purchasers, B&W increased its rebates 30 cents above Liggett's. J.A. 327-28. By July 1984, when B&W made its first generic shipment, its rebates were 75 cents for buyers of 1500 cases quarterly and 80 cents for the few wholesalers buying 8000 cases quarterly. J.A. 327-28.

Q. Did B&W price above or below average variable costs in 1984 and 1985?

A. Pre-tax trading profit was negative. Therefore, if you disregard financial consequences other than direct sales revenue [i.e. reduced taxes on regular-brand cigarette profits] in what you refer to as price the answer would be that prices are below average variable cost.[16] J.A. 651.

This was no accident. Even before its entry, B&W's documents had expressed a willingness to spend its "full variable margin" on generic rebates. J.A. 68, 89-90. B&W's controller admitted that if B&W sacrificed full variable margin, it necessarily would have a negative trading profit (Tr. 98:99) which, as established in the testimony quoted above, meant below-average-variable-cost pricing. *See also* J.A. 664-66.

Nor were these below-cost prices merely introductory. B&W's senior sales manager testified that B&W's volume rebates were not an "introductory allowance." Tr. 91:42. Introductory offers to wholesalers in the cigarette business customarily last four to six weeks. J.A. 411, 416, Tr. 39:171. B&W's initial below-cost rebate offers were for one year, and were subsequently extended even after B&W had achieved its 1984 volume goals. J.A. 197, 478, 192.

---

[16] Because B&W's losses on generics partially offset company profits gained from other sales -- whether from branded cigarettes or other products -- and therefore reduced B&W's federal income taxes, it unsuccessfully urged the court and jury to count such tax savings (and other alleged income tax savings) as if they were generic revenue, which could then be presented as exceeding variable costs. *See Liggett Group Inc. v. Brown & Williamson Tobacco Corp.*, 1989-1 Trade Cas. (CCH) ¶ 68,583 (1988) at 61,107-08 ("B&W's argument for consideration of tax savings on profits generated on other products appears to be at odds with the stated goal of the average-variable-cost test. . . . This court has found no case law or legal literature that supports B&W's position.").

6. **B&W's market analysis correctly predicted that Liggett would be disciplined notwithstanding parental assets and continued profits on regular-brand cigarettes.** B&W carefully analyzed whether it could succeed in forcing Liggett to raise list prices on black-and-whites and thereby shrink the discount. It knew, of course, that Liggett would continue to earn profits on its regular brands, and that Liggett's parent company had considerable assets. But it also knew that the parent was trying to sell Liggett and would not tolerate sustained losses on generics. J.A. 200, 253, 74, 92. B&W wrote that "it is unlikely that [Liggett] can, in fact, be prepared to engage in a sustained battle . . ." J.A. 97.

B&W believed that in just the six months after B&W entered, Liggett would suffer "$35-45 [million] in lost variable margin to defend its business. . ." J.A. 91. Accordingly, it projected that Liggett "will probably attempt to raise prices as soon as possible," (J.A. 200) and that "Liggett will try to survive by: raising prices on generics" (J.A. 253). B&W knew that the losses it inflicted upon Liggett could be reduced only by Liggett raising list prices. Liggett could not cut its rebates without forfeiting its generic business.[17] J.A. 469-70. Such a forfeit was inconceivable, for B&W recognized that "[w]ithout generics, L&M's tobacco business would be irreparably damaged." J.A. 73. Thus, B&W wrote, "L&M can be expected to minimally match" B&W rebates. J.A. 91. As one Liggett executive testified, "It was a lose/lose situation for us. If we didn't pay the incentives [volume rebates] we lost the volume. If we paid the incentives, it took a tremendous amount of money

---

[17] Cutting list prices rather than following B&W in offering higher rebates was also unlikely for Liggett. As B&W wrote, "A reduction in list price by L&M is highly unlikely due to the resulting reduction of wholesaler profits" that would induce wholesalers to substitute B&W's look-alike black-and-whites for Liggett's. J.A. 171.

that we really couldn't afford. So it was lose/lose either way we went."[18] J.A. 468.

True to its prediction, B&W succeeded in disciplining Liggett. Liggett spent tens of millions responding to B&W's below-cost, discriminatory rebates to wholesalers. Tr. 39:232-35, 37:93-104. By June, 1985, Liggett made its initial surrender in the form, as B&W had predicted (J.A. 252-53), of raising its generic list price, leading to higher consumer prices. J.A. 325. A few months later, B&W matched this move.[19] In December 1985, Liggett resisted B&W's attempt to lead another price increase. However, in June 1986, December 1987, and June 1988, a disciplined Liggett followed B&W's black-and-white price increases. J.A. 295-302, 304-07. As a result, black-and-white prices, which then constituted the bulk of all generic cigarettes, rose at a faster rate than regular-brand cigarettes, narrowing the discount gap. J.A. 325, 326.

7. **B&W's market analysis correctly predicted that fellow oligopolists would enter the discounted cigarette segment but would narrow the discount after Liggett was disciplined.** B&W wrote, "Someone must put a lid on L&M -- if we do -- does someone else need to?" J.A. 61. Though doubtless preferring that one of the larger oligopolists "put a

---

[18] B&W also calculated that to the extent it could put Liggett on the defensive and "force them to defend their current business," Liggett would have fewer resources "available to support further business-building" in the generic segment. J.A. 114-15.

[19] The delay was designed to increase B&W volume so that it would be in a stronger position to manage black-and-white prices upward. B&W had explained in April 1985 that it was not yet "in a position to lead a price increase." J.A. 263. It correctly anticipated that Liggett "because of margin erosion will initiate a price increase on the order of $1.50 per [thousand] around mid-year, 1985." J.A. 263. B&W would wait for a few months to generate volume and then "initiate a price increase of $2.50," which Liggett would follow -- "again because of margin erosion." J.A. 263. *See also* J.A. 242.

lid" on Liggett, B&W concluded in its high level planning documents that the larger firms would refrain from disciplinary conduct toward Liggett for fear of antitrust liability. J.A. 76, 93. As for itself, B&W estimated how much it could save by disciplining Liggett. J.A. 83. Its unilateral investment in below-average-variable-cost pricing turned out to be $14.9 million (J.A. 338, Tr. 49:55), which is far less than the $350 million that it estimated it would forego by 1988 unless the growth of generics were slowed down (J.A. 83).

B&W considered the likely reactions of the other oligopolists and concluded that they would not interfere with its effort to narrow the discount gap. B&W reasoned (1) that they would not forsake the industry's long-standing oligopoly pricing (J.A. 131-32) and (2) that they had no incentive or desire to keep prices as low as Liggett at the expense of their very large market shares of regular-brand cigarettes (J.A. 83).

B&W's plan did not depend on the assumption that other manufacturers would remain on "the sidelines." To the contrary, B&W forecast that they might enter in order to "gain control of and contain generic segment growth." J.A. 84. B&W's post-Doral "Strategic Conclusions" discussed two options for the other manufacturers -- remaining on the sidelines versus entering the generic segment -- and concluded:

> The latter appears to be the most predictable approach. . . . It is quite likely that manufacturers will introduce branded generics, develop loyal franchises and then gradually raise prices over the longer term. J.A. 132.

In particular, B&W predicted that industry leader Philip Morris "will not take a leadership position in low margin brand marketing." J.A. 249. And R.J. Reynolds "would strive to limit the [generic] segment development since incremental generic growth will disproportionately reduce RJR's total margins." J.A. 84.

To ensure this result, B&W also wrote that it would "signal [its] intent to competition" that its entry and rebates would "not expand [the] segment." J.A. 61. Its discriminatory rebates to wholesalers had that effect, because they did not generally lead to lower consumer prices. *See supra* p. 10. The other manufacturers did not misread B&W's intentions. No one interfered with B&W's efforts to discipline Liggett. When B&W entered black-and whites in mid-1984, no one else entered the so-called rebate war -- for example, Reynolds did not adjust the rebates it was offering on its Doral brand. Tr. 105: 64-65. And most importantly, all cigarette prices rose along with rising black-and-white prices. J.A. 326.

8. **The discount shrank, all prices rose and B&W concluded that its plan succeeded.** As B&W intended, the list-price differential between generic and regular-brand cigarettes declined from almost 40% in 1985 to 26.8% in 1989.[20] Pet. App. 6a, J.A. 325-26. A Reynolds executive testified that, by 1987, the industry was managing generic prices and profitability upward. J.A. 758-59. By the time of trial in 1989, the prices of both regular-brand cigarettes and generics had increased dramatically in classic oligopolistic fashion (J.A. 326), greatly outstripping increased promotional activities such as retail couponing, known as "stickering" (J.A. 509-10). Although price-discounted brand-name cigarettes (branded generics) accounted for 10.66% of the cigarette market by the end of 1989, they obviously did not provide an effective brake on increasing

[20] Consumer prices reflect manufacturer list prices. J.A. 99-100. Consumers thus lost the benefit of the larger discount during at least 1986, 1987 and 1988. In December 1988, Liggett introduced a new "subgeneric" brand, Pyramid, with a list price approximately 50% below regular brands; two other manufacturers responded with competing entries. J.A. 326. At the time of trial in 1989, subgeneric sales ("third price point") were less than 1% of all cigarette sales. Dx 8888 at 2, 12; Tr. 108:143. Liggett thus was able to reintroduce some measure of price competition at a time when renewed predation was unlikely in view of the District Court's denial of B&W's motion for summary judgment.

cigarette prices. *See* J.A. 326. In 1988, black-and-white and branded-generic prices were higher than regular-brand prices had been at the time B&W entered the generic segment -- a phenomenon that cannot be attributed to increased costs or inflation. J.A. 748, 514-25. Indeed, one year after entering the generic segment B&W informed its parent corporation that its strategy apparently had succeeded in "a slowing in the segment's growth rate." J.A. 257.

D. Proceedings Below

1. **Jury Instructions and verdict.** The jury was instructed that B&W had engaged in price discrimination in the sale of its black-and-white generic cigarettes. Instr. No. 4, J.A. 824. It was asked to decide whether that price discrimination had a reasonable possibility of injuring competition in the cigarette market as a whole. J.A. 27-28. Instr. No. 5, J.A. 823.

In accord with Robinson-Patman Act precedent,[21] the jury was instructed that a reasonable possibility of competitive injury could be inferred either from (1) "market analysis that Brown & Williamson's price discrimination in the sale of black-and-white cigarettes actually injured competition in the cigarette market" or from (2) "predatory intent" that in turn could be inferred either from (a) below-average-variable-cost pricing or from (b) "direct evidence of Brown & Williamson's statements, documents, or conduct." Instr. Nos. 16 and 18, J.A. 832, 834.

---

[21] *Double H Plastics, Inc. v. Sonoco Prods. Co.*, 732 F.2d 351, 354 (3d Cir.), *cert. denied*, 469 U.S. 900 (1984); *O. Hommel Co. v. Ferro Corp.*, 659 F.2d 340, 347 (3d Cir. 1981), *cert. denied*, 455 U.S. 1017 (1982); *D.E. Rogers Assoc., Inc. v. Gardner-Denver Co.*, 718 F.2d 1431, 1439 (6th Cir. 1983), *cert. denied*, 467 U.S. 1242 (1984); *Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc.*, 824 F.2d 582, 596 (8th Cir. 1987), *cert. denied*, 484 U.S. 1010 (1988); *Henry v. Chloride, Inc.*, 809 F.2d 1334, 1344 (8th Cir. 1987). *See also Pacific Engineering & Prod. Co. v. Kerr-McGee Corp.*, 551 F.2d 790, 798 (10th Cir.), *cert. denied*, 434 U.S. 879 (1977).

Predatory intent was carefully defined. The jury was told that the only intent relevant to this case would be a B&W plan "to discipline and exclude . . . rivals . . . so that it can earn higher than competitive profits. . . ." Instr. No. 19, J.A. 835. Moreover, the fact to be inferred from predatory intent -- that is, "a reasonable possibility of competitive injury" -- was explicitly defined in terms of "loss-creating price cutting" with the "real possibility" of "recoup[ing] losses by raising and maintaining prices at higher than competitive levels." Instr. No. 12, J.A. 829. The jury was warned not to infer injury to competition from predatory intent if its common sense indicated that there was no such possibility of recoupment.[22] Instr. Nos. 20 and 12, J.A. 835, 829.

The jury was further instructed that "[i]f you find that Brown & Williamson reasonably believed that its average variable cost would not exceed its net prices, but, that for unforeseen reasons, its average variable cost actually did exceed its net prices, then you must find that Brown & Williamson did not price below its reasonably anticipated average variable cost." Instr. No. 26, J.A. 841. Nor was any inference of injury to competition permitted to be drawn from below-average-variable-cost pricing if B&W was "attempting to gain entry into a new portion of the cigarette business and offered net prices below reasonably anticipated average variable cost on an introductory basis only." Instr. No. 27, J.A. 841. Furthermore, the jury was told B&W lawfully could price its black-and-white cigarettes below average variable cost if it was engaged in a "good faith"

---

[22] The jury also was cautioned that "mere diversion of business from one competitor" is not unlawful, and that "the Robinson-Patman Act was designed to protect 'consumer welfare' rather than just competitors." Instr. Nos. 10 and 12, J.A. 828, 829. As an additional burden on Liggett, the instructions required it to show that B&W possessed some measure of "market power" in either the whole cigarette market or in a well-recognized submarket, if any, for generic cigarettes. Instr. Nos. 13 and 15, J.A. 830, 832. In all events, the instructions made clear that B&W was liable only if it threatened competition in the whole cigarette market. Instr. No. 12, J.A. 829.

effort to "meet competition."[23] Instr. Nos. 33 and 34, J.A. 846-847.

The jury returned a verdict for Liggett.

2. **JNOV decision.** The District Court granted B&W judgment notwithstanding the verdict. The District Court found that the evidence of B&W's anticompetitive purpose was "more voluminous and detailed than any other reported case," revealing an intent to harm both Liggett and consumers. Pet. App. 31a. Nevertheless, the court held that B&W "could not have had a reasonable possibility of injuring competition" because there was no "economically plausible way to recoup its losses." Pet. App. 32a. The District Court did not challenge the possibility of recoupment in an oligopoly setting. Rather, it declined to credit the detailed economic evidence that profits were supracompetitive, because Liggett's executives had denied "tacit collusion" and had testified that cigarette profits were not "excessive." Pet App. 34a-35a. *See supra* note 11. The District Court reasoned that without supracompetitive profits, disciplining

---

[23] The jury was also instructed that "if you find that the reasonable possibility of injury to competition resulted merely from low prices, then you must find that Brown & Williamson's price discrimination did not create any reasonable possibility of injury to competition." Instr. No. 31, J.A. 844. To find for Liggett, the jury had to find that "price discrimination facilitated or made possible predatory conduct by Brown & Williamson." Instr. No. 31, J.A. 844.

Finally, the jury was instructed it could not award damages to Liggett unless it found that Liggett "was in fact injured in its property or business" as a result of B&W's violation of the Robinson-Patman Act. Instr. No. 35, J.A. 848. Specifically, the jury was told to consider whether Liggett was injured by B&W's below-cost price discrimination rather than by "competition by other cigarette manufacturers, falling demand for cigarettes" or "Liggett & Myers' own management shortcomings." Instr. No. 37, J.A. 849. In determining the amount of damages the jury was required to "separate damages to Liggett & Myers from the lawful competitive activities of Brown & Williamson and the other cigarette manufacturers. . . ." Instr. No. 38, J.A. 850.

Liggett would merely cause B&W to lose money without ever achieving a payoff. The District Court also declined to credit the evidence that the larger cigarette oligopolists shared B&W's interest in stabilizing and then narrowing the gap between regular-brand and generic cigarettes and in preserving supracompetitive regular-brand profits. Pet. App. 36a.[24]

The District Court stated that its jnov decision was "based upon interpretations of the applicable law" rather than upon any quarrel with the evidence or instructions. Pet. App. 19a note 6. It said that no new trial would be necessary -- and thus that judgment should be given on the jury verdict -- if "an appellate court applied legal standards more favorable to Liggett." Pet. App. 19a note 6.

3. **Court of Appeals decision.** The Fourth Circuit affirmed, though by different reasoning. It ruled that recoupment by an oligopolist is never a realistic possibility. Without denying the factual basis for the jury's conclusion that B&W acted predatorily to discipline Liggett and injure consumers, the court ruled as a matter of law that it would be irrational for an oligopolist to act in this way. According to the court's "economic logic," only a monopolist (actual or prospective) or a member of an organized cartel could ultimately profit from charging below-cost prices to discipline a rival: An oligopolist's below-cost investment in disciplinary pricing could never pay off because fellow oligopolists would never be "certain" that the predator was disciplining a maverick rather than attempting to expand its own market share. Pet. App. 11a. According to the Fourth Circuit, the other oligopolists would be more likely to respond

[24] In addition, the District Court held that (i) because all B&W black-and-white prices were below their costs such that the high price did not subsidize the low price, the difference between those prices (the "discrimination") did not "cause" any injury to competition that may have occurred (Pet. App. 38a-42a) and, in any event, (ii) B&W's below-cost prices on generics were irrelevant and could not cause "antitrust injury" because they were offset by profits on regular-brand product (Pet. App. 42a-49a).

competitively, undermining oligopolistic price discipline. Pet. App. 12a. The Fourth Circuit believed that its "theoretical suspicions" were confirmed in "hindsight" by the growth of the generic sector, Pet. App. 12a, notwithstanding the reduced generic discount and higher prices for both generic and regular-brand cigarettes. Pet App. 6a.

SUMMARY OF ARGUMENT

The decision below rests on two fundamental errors of law. *First*, the Fourth Circuit erroneously limited the Robinson-Patman Act to monopoly or cartel cases, thus making it redundant of the Sherman Act. But the Robinson-Patman Act was specifically enacted to have greater scope; it uses express language that applies to unilateral conduct by firms lacking any prospect of single-firm monopoly. The court rested its narrowing application of the Act on its own "theoretical suspicions" that an oligopolist acting unilaterally would never price below cost to discipline a rival because it could never be "assured" of a payoff in supracompetitive prices. Pet. App. 12a, 14a. The court's speculations were faulty economics and bad law. It is widely recognized that oligopolists can reap and reasonably expect to maintain monopoly-level prices and profits without any express conspiracy. Moreover, the court misread *Matsushita Electric Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), as permitting it to substitute its own "economic logic" for the jury finding of anticompetitive conduct by an actual oligopolist. That finding was supported by proof meeting the strictest test of the statutory language and is fully consistent with antitrust policy.

The Fourth Circuit's immunization of unilateral conduct by an oligopolist -- no matter how anticompetitive -- cannot be defended as a statutorily authorized "bright line" needed to forestall a flood of challenges to procompetitive pricing. No such flood could pass through all the filters that, in cases like this one, allay any genuine concern that procompetitive pricing may be mistaken for disciplinary predation. Substantial, unjustified and discriminatory prices below average variable cost with a reasonable prospect of recoupment suffice to show the reasonable possibility of injuring competition that violates the Robinson-Patman Act.

Second, as erroneous support for its first conclusion or possibly as an alternative to it, the court below insisted that any otherwise unlawful predatory plan had been unsuccessful. In an error of law, the court deemed the predatory plan unsuccessful simply because the generic market segment had expanded, ignoring the increase in all cigarette prices as the gap between regular brands and generics narrowed. Higher prices, which were acknowledged, suffice in and of themselves to establish injury to competition. In any event, improper price discrimination undertaken with a reasonable potential for injuring competition violates the Robinson-Patman Act even if not ultimately successful.

ARGUMENT

I. THE FOURTH CIRCUIT ERRONEOUSLY RESTRICTED THE SCOPE OF THE ROBINSON-PATMAN ACT -- CONTRARY TO ITS LANGUAGE AND PURPOSE, TO PRECEDENT, TO SOUND ECONOMICS, AND TO THE WELL-SUPPORTED JURY VERDICT.

A. The Robinson-Patman Act is Not Limited To Single-Firm Monopoly or Conspiracy Already Covered by the Sherman Act.

The effect of the Fourth Circuit ruling was to limit the Robinson-Patman Act proscription of predatory and disciplinary pricing to monopolies and conspiracies, classes of conduct already forbidden by Sherman Act §§1-2. By thus granting *per se* immunity for disciplinary price discrimination in the absence of actual or prospective monopoly or express cartelization, the court disregarded the language and purpose of the Robinson-Patman Act. By its own terms, the statute applies to a single firm's price discrimination the effect of which "may be substantially to lessen competition or tend to create a monopoly . . . or to injure . . . competition with [the discriminating seller]. . . " Pet. App. 54a. The Act's reference to single-firm conduct is inconsistent with any conspiracy requirement, and the disjunctive language obviates any monopoly requirement. Indeed, it was Congress' intent that this statute reach conduct "not covered by the [Sherman Act]."[25]

To be sure, the Robinson-Patman Act and Sherman Act §2 share a common goal of protecting consumers who may ultimately be injured by predatory pricing.[26] Cases under both Acts employ a common test for distinguishing proper from improper prices[27] and recognize that consumers are directly injured by the creation or perpetuation of

---

[25] S. Rep. No. 698, 63d Cong. 2d Sess. 2 (1914). Sixty years later, a special House subcommittee recommended against limiting the Robinson-Patman Act's primary-line scope to that of the Sherman Act, for "no one has articulated a sound basis for radically limiting the Act's primary-line competition reach." Ad Hoc Subcommittee on Antitrust, The Robinson-Patman Act and Related Matters, Recent Efforts to Amend or Repeal the Robinson-Patman Act, H.R. Rep. No. 1738, 94th Cong. 2d Sess. 76 (1976).

[26] *See William Inglis & Sons Baking Co. v. ITT Continental Baking Co.*, 688 F.2d 1014, 1042 (9th Cir. 1981), *cert. denied*, 459 U.S. 825 (1982) ("In primary-line Robinson-Patman Act cases . . . the distinction between vigorous, but honest, price competition and predatory assaults on the competitive process is just as important as it is to Sherman Act cases brought under its section 2."); *O. Hommel Co.*, 659 F.2d at 348-50 ("A focus on detrimental effects on competition rather than a concern with individual competitors is fundamental to a reconciliation of the Robinson-Patman Act with overall antitrust policies.").

[27] *International Air Indus., Inc. v. American Excelsior Co.*, 517 F.2d 714, 720 n.10 (5th Cir. 1975), *cert. denied*, 424 U.S. 943 (1976); *Henry*, 809 F.2d at 1345; *Pacific Engineering & Prod. Co.* 551 F.2d at 798; *Janich Bros. v. American Distilling Co.*, 570 F.2d 848, 855 (9th Cir. 1977), *cert. denied*, 439 U.S. 829 (1978); *D.E. Rogers Assoc.*, 718 F.2d at 1439; *O. Hommel Co.* 659 F.2d at 348-50; *William Inglis & Sons Baking Co.*, 668 F.2d at 1042; *McGahee v. Northern Propane Gas Co.*, 858 F.2d 1487, 1493 n.9 (11th Cir. 1988), *cert. denied*, 490 U.S. 1084 (1989).

supracompetitive prices through which the investment in a predatorily low price is recouped. Thus, the prospect of recoupment indicates that competition is genuinely threatened and reassures the tribunal that an unjustified below-cost price is truly predatory.

Notwithstanding these shared goals and techniques, the statutes are not coterminous.[28] By its own terms, the Sherman Act requires conspiracy or actual or prospective monopoly, while the Robinson-Patman Act reaches price discrimination where the effect "may be to substantially lessen competition," whether or not accompanied by monopoly or conspiracy. Congress used the very same "effect" language in Clayton Act §7, which recognizes that mergers without any prospect of single-firm monopoly or conspiracy with others can illegally bring about or reinforce supracompetitive oligopoly prices. As elaborated in Section B *infra*, an oligopoly's supracompetitive prices can provide the payoff for below-cost pricing designed to ruin or discipline a disruptive rival.

Given that risk, Congress's concern in the Robinson-Patman Act with primary-line price discrimination threatening competition -- even absent single firm monopoly or an illegal cartel -- was not misplaced. Price discrimination allows a predator to target its price cuts, thereby lowering its investment in below-cost pricing and making recoupment more likely. In B&W's words, a predatory oligopolist can "[p]ut the money where the volume is." J.A. 402. B&W targeted its largest discounts to Liggett's largest 14 customers, thereby inflicting maximum disciplinary pressure upon Liggett at least cost to itself. *See supra* pp. 12-13.

This straightforward way in which price discrimination can threaten competition is sometimes misunderstood. For example, the District Court suggested that the higher of the discriminatory prices ("high price") must subsidize the lower

---

[28] *See, e.g.*, *William Inglis & Sons Baking Co.*, 668 F.2d at 1042 ("[w]e do not hold that there exists a complete substantive synchronization of the Sherman and Robinson-Patman Acts.").

of the discriminatory prices ("low price") before discrimination can "cause" injury to competition. Pet. App. 38a-42a. In a standard illustration, a normal above-cost (or even monopolistic) price in one geographic market accompanies a predatory below-cost price in a different geographic market to which the victim is confined. However, that high price does not make the low price profitable, currently or ever: If the lower price is predatorily below cost, it can benefit the predator only by destroying or disciplining a rival and thereby helping achieve or maintain supracompetitive prices in the victim's region. True, the normal price in one region can provide the cash that the predator invests in the predatorily low price, but "it does not ordinarily matter whether the money to pay for the resulting temporary loss comes from a bank account, a legacy, a lottery prize, or the proceeds of a price fixing conspiracy in respect to another product."[29] True also, the victim of predatory price discrimination might outlast the attack if it also sells to the high-price customers -- as when it operates in both regions or when the discrimination is non-geographic -- but not when, as in the present case, the high price is itself below average variable cost and the predator expressly and accurately predicts that the losses it inflicts upon the target will be insufferable.

In sum, price discrimination can endanger competition by facilitating predatory pricing. Thus, there is no reason to resist the express language of the Robinson-Patman Act in its coverage of all improper discrimination (whether or not geographic) and all improper discriminators (whether or not monopolists or conspirators). This accords with the statute's express language and with the purpose declared in its legislative history to reach conduct beyond that reached by the Sherman Act.

---

[29] *Clamp-All Corp. v. Cast Iron Soil Pipe Institute*, 851 F.2d 478, 485-86 (1st Cir. 1988), *cert. denied*, 488 U.S. 1007 (1989) (Breyer, J.; Sherman Act).

B. Economic Theory Does Not Require Conspiracy or Single-Firm Monopoly as a Predicate for Predatory Pricing.

It is widely recognized that oligopolists can reap monopoly-level prices and profits without any express conspiracy. By "'oligopolistic interdependence' . . . in contrast to the explicit collusion of the formal cartel or its underground counterpart," sellers might "coordinate their pricing without conspiring in the usual sense of the term."[30] Though it may be "profoundly anticompetitive"[31] and able to "reap supracompetitive prices" merely as a result of rivals observing and following each other,[32] the non-conspiratorial oligopoly is not itself illegal. Nevertheless, maintaining supracompetitive profits can provide the recoupment rewarding a predatory oligopolist.

To be sure, destroying all one's rivals eliminates all present competition while rivals remain after an oligopolist disciplines a maverick. This difference between monopolistic and oligopolistic predation has two implications. *First*, if predation is successful, the monopolist alone reaps its fruits, while an oligopolist must share the fruits with surviving oligopolists, and the smaller oligopolist may benefit less from reinforced supracompetitive prices than the larger ones. In this case, B&W believed that the larger firms feared antitrust liability and that therefore they would not discipline Liggett. J.A. 76, 93. B&W wrote that if it "put the lid on L&M," no one else would have to. J.A. 61. Although doing so would benefit fellow oligopolists too, B&W calculated that it alone would benefit enough -- up to $350 million by 1988 -- to

---

[30] R. Posner, *Antitrust Law* 40 (1976). *See also* 6 P. Areeda, *Antitrust Law* ¶ 1410b at 66 (1986). B&W's economic expert also acknowledged that consumers faced with a tightly-knit oligopoly are likely to pay elevated prices. J.A. 741-42.

[31] *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 367 n.43 (1963).

[32] *Eastman Kodak Co. v. Image Technical Serv. Inc.*, ___ U.S. ___, 112 S. Ct. 2072, 2086 n.21 (1992).

make its investment in disciplining Liggett pay off handsomely. J.A. 83. When the gains to be achieved are large enough relative to the costs of disciplining a maverick,[33] predation becomes an entirely rational strategy for an oligopolist. Indeed, this Court has recognized that predation is plausible when an investment in below-cost sales can be more than paid back either by obtaining "future monopoly profits" (where rivals are to be eliminated) or by protecting "future undisturbed profits" (where rivals are to be disciplined) -- defining "monopoly profits" as "enough market power to set higher than competitive prices." *Matsushita Electric Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 589-90 (1986).

A *second* difference between predatory monopoly and oligopoly is that a predator anticipating entry-resistant monopoly hopes that it alone will set the post-predation price, while an oligopolist such as B&W knows that future prices depend upon the choices of fellow oligopolists. Because fellow oligopolists and a would-be predator could not be "certain" and "assured" of each other's motives and reactions, the Fourth Circuit ruled oligopolistic predation irrational. Pet. App. 11a, 14a.

That court's demand for certainty requires the impossible -- whether a predator is an aspiring monopolist, a cartel, or an oligopolist. A would-be monopolist cannot be certain that it will actually obtain a monopoly or that the monopoly price will be high enough and last long enough without new entry to recoup the predatory investment. Certainty is similarly impossible in an express cartel, whose members may "cheat."[34] If certainty were a prerequisite to threatened impairments of competition, antitrust law would have no occasion to fear the mergers that create oligopoly or

---

[33] From the predator's viewpoint, relatively speedy discipline requires a smaller investment in below-cost pricing than slower destruction.

[34] *See* F. Scherer and D. Ross, *Industrial Market Structure and Economic Performance* 238 (3d ed. 1990).

the practices that facilitate its supracompetitive pricing. Yet, antitrust law does prohibit mergers that create or reinforce oligopoly[35] as well as practices that facilitate oligopoly pricing.[36] Competition can be harmed not because oligopolists are certain of their rivals' reactions, but because each can calculate the gains to be achieved if rivals react in a specified way and then estimate the probabilities that rivals will so behave.

Not only were the Fourth Circuit's "theoretical suspicions" unwarranted for the generality of cases, they were singularly misplaced in the present case. In the cigarette industry, there was little risk (1) that oligopoly pricing would break down or (2) that the oligopolists would misperceive disciplinary price-cutting as promotional and respond with aggressive price cuts of their own, thereby frustrating the maintenance of supracompetitive prices. As to the first, the court failed to mention the record evidence that this industry has long been the textbook example of long-maintained supracompetitive prices and profits.[37] *See supra* pp. 5-7. The likelihood that the cigarette market would continue to behave as the classic oligopoly it has been for decades was far greater than the prospect that, for example,

---

[35] U.S. Department of Justice and Federal Trade Commission Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶ 13,104 (1992) at 20,571, are founded on the recognition that "in some circumstances, where only a few firms account for most of the sales of a product, those firms can exercise market power, perhaps even approximating the performance of a monopolist by either explicitly or implicitly coordinating their actions."

[36] *See, e.g., United States v. Container Corp.*, 393 U.S. 333 (1969).

[37] *See* F. Scherer and D. Ross, *Industrial Market Structure and Economic Performance* 250-51 (3d ed. 1990) (describing successful price disciplining in the 1930s and the 1980s' experience when despite "the reappearance of low price brands, and falling consumption, the leading U.S. cigarette manufacturers raised prices sufficiently to increase their profits from $3.80 to $11.55 per thousand cigarettes sold between 1980 and 1988.") (read into record at J.A. 748).

members of the express OPEC cartel would refrain from cheating or that a would-be monopolist would gain and keep a monopoly.

As to the potential reactions of the other oligopolists, the Fourth Circuit acknowledged, "Oligopolists might indeed all share an interest in letting one among them discipline another for breaking step and might all be aware that all share this interest." Pet. App. 11a. However, in the court's view,

> The oligopolist on the sidelines would need to be certain at least that it could trust the discipliner not to expand the low-price segment itself during the fight or after its success. Of course, all the oligopolists on the sidelines would need to be certain that the others were also confident on this point. Such confidence must be rare, indeed, when the form that the discipline takes is a price-war, which must strike fear in the heart of any oligopolist hoping to protect market share and high prices. More likely, when members of an oligopoly are faced with a competitor's decision to break step, drop prices, and expand market share, they would react competitively. Pet. App. at 11a-12a.

In fact, B&W did not believe the other oligopolists would "react competitively," and it was right. B&W examined each rival in turn and analyzed how each would react to Liggett's conduct and to B&W's projected plan to discipline Liggett. J.A. 83-87. Directly contrary to the Fourth Circuit's "theoretical suspicions," B&W memoranda explained that it would "signal [its] intent to competition" that its entry and rebates would "not expand [the] segment." J.A. 61. Discriminatory rebates -- as distinct from list-price reductions reaching consumers -- have that effect. B&W concluded (correctly) that its rivals most likely would "enter the new segment" but would be eager "to manage prices and profitability upward" to the detriment of the consumer. J.A. 131-32.

Furthermore, B&W's "war" was limited to black-and-whites, hurting Liggett rather than the other oligopolists, who (unlike Liggett) did not rely on black-and-whites for either volume or profits. The "war" did not extend to list-price reductions that would draw additional consumers away from the regular brands of fellow oligopolists. Indeed, no other manufacturer was drawn into the "price war." For example, Reynolds did not change its small Doral rebate during the 1984 war of escalating black-and-white rebates. Tr. 105: 64-65. In sum, the Fourth Circuit's "theoretical suspicions" were logically flawed and so, unsurprisingly, were belied by the facts.

C. Using Economic Theory To Immunize Actual Predatory Conduct As Found By The Jury Contradicts Precedent and Good Sense.

Beyond misunderstanding economics and failing to consider the language and purpose of the statute, the court below erred fundamentally in its methodology. Notwithstanding a fully developed record and jury verdict, the court held that its abstract speculations about the profit-maximizing choices of a hypothetical oligopolist made it unnecessary to consider the conduct and market analyses of the actual and highly sophisticated defendant before it. To be sure, economic theory, at least when well-founded, can indicate what evidence would be helpful and can illuminate both evidentiary ambiguities and legal standards. However, once conduct has been proven to occur, it is illogical and legally improper to immunize it on the ground that "theoretical suspicions" suggest that such conduct is unlikely to occur.[38]

---

[38] The Fourth Circuit did not deny that a reasonable jury could find that B&W's prices were unjustified, were below average variable cost, were designed to and did in fact discipline Liggett, and that consumer prices rose as a result of B&W's conduct. If the Fourth Circuit rested on the belief that B&W's anticompetitive conduct did not succeed in injuring competition, it made two errors of law. *See infra* Section II p. 43.

The Fourth Circuit defended its approach with a patent misreading of *Matsushita Electric Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986). *Matsushita* held that the existence of a conspiracy to engage in predatory pricing could not be inferred from circumstantial evidence when there would have been no economically plausible means for the alleged conspirators to recoup any losses from conspiratorial low prices. However, *Matsushita* recognized that judicial doubts about the chances of success must be set aside once there is evidence that the defendants have actually engaged in the alleged conduct. *Id.* at 597. Moreover, *Matsushita* declared that "direct evidence of below-cost pricing is sufficient to overcome the strong inference that rational businesses would not enter into conspiracies such as this one." *Id.* at 585 n.9. Contrast the Fourth Circuit's erroneous statement that

> the Court in *Matsushita* held that a conspiracy, which could not hope to recoup its expenses incurred from alleged below-cost pricing and was therefore economically senseless, did not violate the antitrust laws. Pet. App. 9a.

The Fourth Circuit thus declared that *actual* below-cost pricing by a sophisticated actor reasonably intending to discipline a rival, to injure consumers, and to obtain recoupment from the industry's persistent supracompetitive profits -- key factors under the Robinson-Patman Act and analogous to the Sherman Act conspiracy factor in *Matsushita* -- is not unlawful because the court deemed success unlikely and therefore concluded that B&W would have been irrational to do what it was proven to have done.

The Fourth Circuit's error is demonstrated *a fortiori* by *Eastman Kodak Co. v. Image Technical Serv., Inc.*, ___ U.S. ___, 112 S.Ct. 2072, 2082 (1992), which "focus[ed] on the 'particular facts disclosed by the record'" to illuminate "market realities." Disapproving summary judgment for defendant in that case, this Court relied on limited evidence of liability that tended to contradict a compelling chain of economic reasoning supporting the defendant.[39] In stark contrast, the Fourth Circuit rejected a well-supported finding of liability that was *consistent with* a compelling and well-accepted concern with supracompetitive oligopolistic pricing. That jury finding accords with an economic proposition pervading antitrust law -- that supracompetitive pricing can occur without illegal conspiracy in highly concentrated markets. *See supra* p. 28. The jury was surely entitled to believe that cigarettes constituted such a market. *See supra* pp. 5-7.

The Fourth Circuit also ignored this Court's instruction in *Chicago Board of Trade v. United States*, 246 U.S. 231, 238 (1918) (Brandeis, J.), that "knowledge of intent may help the court to interpret facts and to predict consequences." The court below ruled in effect that its speculations about the workings of the cigarette market were so far superior to the sophisticated defendant's own judgments about that market that B&W's market analyses and predictions could be disregarded. Although one might disregard the fantasy of an irrational or uninformed person, B&W is neither. A reasonable tribunal must surely weigh heavily B&W's own high-level documents explaining the way this market works, the nature and function of B&W's pricing, and its predictions that Liggett would be forced to raise prices and that fellow oligopolists would not interfere.[40] The speculation of

---

[39] In that tying case, liability depended on proof of Kodak's power over a tying product of distinctive repair parts for its machines. Because Kodak lacked power in the machine market and because sophisticated buyers would take account of repair prices when buying machines, Kodak argued that its power over repair parts could never exceed its non-existent power over machines. Acknowledging that Kodak might be able to offer facts supporting its reasoning, the Court pointed to evidence suggesting that some buyers were unsophisticated and therefore required further exploration before approving summary judgment that had terminated the case after only truncated discovery.

[40] *See Appalachian Coals, Inc. v. United States*, 288 U.S. 344, 372 (1933); L. Sullivan, *Handbook of the Law of Antitrust* 195 (1977) ("The actors in the marketplace will often be themselves the best

lawyers and judges about the workings of a particular market is no substitute for a sophisticated defendant's own carefully designed market analysis and unambiguous plan. "Wisdom lags far behind the market . . . . [L]awyers know less about the business than the people they represent. . . . . The Judge knows even less about the business than the lawyers." Easterbrook, *The Limits of Antitrust*, 63 Tex. L. Rev. 1, 5 (1984).

D. The Most Demanding Standard for Robinson-Patman Act Liability Was Met.

This Court last addressed primary-line injury to competition in *Utah Pie Co. v. Continental Baking Co*, 386 U.S. 685 (1967), which approved a jury verdict condemning both geographic and nongeographic price discrimination.[41] There was no element of monopoly or conspiracy. The defendants in *Utah Pie* were three national firms that sold frozen pies in Utah at prices below cost and below their prices in other markets. One defendant had identified plaintiff as an "unfavorable factor," sent an industrial spy into Utah Pie's plant, and accepted "substantial losses" in Utah that a jury might rationally attribute to its low prices there. *Id.* at 697. Another defendant's Utah prices were "less than its direct cost plus an allocation for overhead" during several two-week periods. *Id.* at 698. And the third

---

judges of what they are capable of achieving, and if they are aimed at wrongful acts we may logically treat their purposes as a guide to what they will accomplish."); 7 P. Areeda, *Antitrust Law* ¶ 1506 at 393-94 (1986).

[41] Earlier primary-line cases addressed other issues -- defining price discrimination in *FTC v. Anheuser-Busch, Inc.*, 363 U.S. 536 (1960), and interstate commerce in *Moore v. Mead's Fine Bread Co.*, 348 U.S. 115 (1954). But *Anheuser-Busch* did note that "it might be argued that the existence of predatory intent bears upon the likelihood of injury to competition, and that a price reduction below cost tends to establish such an intent," *Anheuser-Busch*, 363 U.S. at 552 (footnote omitted), while *Moore* suggested that elimination of a rival satisfies the Act's effects clause, *Moore*, 348 U.S. at 118.

defendant's price was for a time "admittedly well below its costs, and well below the other prices prevailing in the market." *Id.* at 701. In sum, "with respect to each" defendant, "there was some evidence of predatory intent," which supported an inference of injury to competition when supplemented by evidence of defendants' downward pressure on prices in a "highly competitive market" and the resultant "drastically declining price structure." *Id.* at 702-03. The Court held such evidence sufficient to support a finding of injury to competition as to each of the defendants, because "the Act reaches price discrimination that erodes competition as much as it reaches price discrimination that is intended to have immediate destructive impact." *Ibid.*

Lower courts have read *Utah Pie* to allow juries to infer injury to competition from a "drastic[]" market impact and/or "predatory intent" and to infer the latter either from direct evidence of the defendant's purpose or from below-cost pricing.[42] At the same time, the lower courts have refined the *Utah Pie* standard to accommodate subsequent decades of antitrust development. They clarified the relevant intent, analyzed price-cost relationships, and recognized that the prospect of recoupment -- connecting present below-cost prices injuring rivals with the achievement or maintenance of high prices injuring consumers -- helps distinguish predatory from competitive pricing. B&W's pricing in this case is unlawful by any and all of these tests.[43]

Intention. An extreme reading of *Utah Pie* and of some earlier lower court precedent allows a jury to view aggressive conduct toward a smaller rival as threatening to

---

[42] This reading produced the now-conventional "double inference" instruction given (and supplemented) in this case. *See supra* p. 19.

[43] Entirely misleading, therefore, is the Fourth Circuit's suggestion that Liggett defends the verdict on the ground that B&W's realized intent to injure Liggett itself suffices for illegality under *Utah Pie*. Pet. App. 7a-8a.

competition.[44] By that standard, of course, B&W's liability is demonstrated *a fortiori*.

More recent cases have wisely sought to link "predatory intent" with an improper attack on the marketplace and have defined it as the intent to "sacrific[e] present revenues with the purpose of achieving monopoly profits in the future," *O. Hommel Co. v. Ferro Corp.*, 659 F.2d 340, 348, *cert. denied*, 455 U.S. 1017 (1982), not simply the desire to injure competitors. *Accord International Air Indus., Inc. v. American Excelsior Co.* 517 F.2d 714, 723 (5th Cir. 1975), *cert. denied*, 424 U.S. 943 (1976) ("By 'predatory' we mean that [defendant] must have at least sacrificed present revenues for the purposes of driving [plaintiff] out of the market with the hope of recouping the losses through subsequent higher prices."); *Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc.*, 824 F.2d 582, 596 (8th Cir. 1987), *cert. denied*, 484 U.S. 1010 (1988) ("the predatory intent . . . must relate to the market as a whole.").

In the present case, the evidence disclosed B&W's anti-consumer, as well as its anti-Liggett, state of mind. It expressed an unambiguous, sophisticated analysis of the market, calculating precisely how it could force Liggett to raise its black-and-white prices. It also analyzed how it could profit from disciplining Liggett, even though fellow oligopolists were significant in the cigarette market. This is the kind of evidence that best illustrates how "knowledge of intent may help the court to interpret facts and to predict consequences." *Chicago Board of Trade v United States*, 246 U.S. 231, 238 (1918). In no other reported decision is a predatory plan so clearly set forth in the defendant's own memoranda -- a fact acknowledged by the District Court itself. Pet. App. 31a.

---

[44] *See, e.g.*, *National Dairy Prods. Corp. v. FTC*, 412 F.2d 605, 618-20 (7th Cir. 1969). To avoid such extreme readings, many lower courts largely ignore *Utah Pie*, as the Fourth Circuit did here, or arbitrarily confine it to geographic discrimination, as in *O. Hommel* and *Barr Labs., Inc. v. Abbott Labs.*, 978 F.2d 89 (3d Cir. 1992).

Below-Cost Pricing. Although many lower courts use the rubric of predatory intent, they infer that intent from below-cost pricing. *See supra* p. 19. *Utah Pie* itself saw the significance of price-cost relationships long before later authorities elucidated which cost measures were most relevant -- a task that *Utah Pie* had not attempted.[45] In that case, the Court spoke only of prices below average total cost. By that standard, B&W's liability is again established *a fortiori*.

Today, some courts admit the possibility of predation even when prices exceed average variable cost[46] or average total cost.[47] In any event, all the lower courts would find at least presumptive impropriety when prices persistently fail to cover average variable costs.[48] That presumption is well

---

[45] *See William Inglis & Sons Baking Co.*, 668 F.2d at 1041 n.48 ("there is no indication that the [*Utah Pie*] Court meant to establish average total cost as the immutable dividing line in all Robinson-Patman Act cases."); *Ashkenazy v. I. Rokeach & Sons, Inc.*, 757 F. Supp. 1527, 1550 (N.D. Ill. 1991) (*Utah Pie's* concern was "to root out predatory pricing, and therefore more reliable measures of cost developed subsequently can (and should) be substituted without upsetting the holding or reasoning of *Utah Pie*.").

[46] *Henry*, 809 F.2d at 1346; *McGahee*, 858 F.2d at 1503-04; *William Inglis & Sons Baking Co.*, 668 F.2d at 1041; *Instructional Systems Development Corp. v. Aetna Casualty & Surety Co.*, 817 F.2d 639, 648 (10th Cir. 1987) (Sherman Act); *Chillicothe Sand & Gravel Co. v. Martin Marietta Corp.*, 615 F.2d 427, 432 (7th Cir. 1980) (same).

[47] *Transamerica Computer Co. v. International Business Machines*, 698 F.2d 1377, 1388 (9th Cir.), *cert. denied*, 464 U.S. 955 (1983) (Sherman Act); *International Air Industries, Inc.*, 517 F.2d at 724. *Contra Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227 (1st Cir. 1983) (Sherman Act); *McGahee*, 858 F.2d at 1503; *Arthur S. Langenderfer, Inc. v. S.E. Johnson Co.*, 729 F.2d 1050, 1056 (6th Cir.), *cert. denied*, 469 U.S. 1036 (1984) (Sherman Act).

[48] *Henry*, 809 F.2d at 1346; *McGahee*, 858 F.2d at 1504; *William Inglis & Sons Baking Co.*, 668 F.2d at 1041; *Janich Bros.*, 570 F.2d at 858; *Pacific Engineering & Prod. Co.*, 551 F.2d at 797; *D.E. Rogers*,

founded, for every such sale *increases* the seller's losses. Such a price is so low that "one would know that the firm cannot rationally plan to maintain this low price . . . [I]t would do better to discontinue production." *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 232 (1st Cir. 1983) (Sherman Act). "There is no reason consistent with an interest in efficiency for selling a unit at a price lower than the cost that the seller incurs by the sale." Posner, *Exclusionary Practices and the Antitrust Laws*, 41 U. Chi. L. Rev. 506, 519 (1974).

In the present case, B&W sold black-and-whites well below their average variable cost for 18 months. J.A. 338-39. To infer predatory intent from below-cost pricing, the jury was instructed that it had to find that B&W priced below its average variable costs.[49] Instr. No. 18, J.A. 834. The jury was also specifically instructed to absolve B&W if its prices were introductory, promotional, or adopted in good faith to meet competition. Instr. Nos. 26, 27, and 33, J.A. 841, 846.

True, B&W continued to earn supracompetitive profits on regular brands such that its revenues exceeded its costs for cigarettes as a whole. However, branded profits do not make loss-creating prices on black-and-whites promotional or

---

718 F.2d at 1436-37; *In the matter of International Telephone & Telegraph Corporation*, 104 F.T.C. 280, 403-04 (1984); *Northeastern Tel. Co. v. American Tel. & Tel. Co.*, 651 F.2d 76, 88 (2d Cir. 1981), *cert. denied*, 455 U.S. 943 (1982) (Sherman Act); *Kelco Disposal, Inc. v. Browning-Ferris Industries*, 845 F.2d 404, 407 (2d Cir. 1988), *aff'd on other grounds*, 492 U.S. 257 (1989) (Sherman Act); *Chillicothe Sand & Gravel Co.*, 615 F.2d at 432 (Sherman Act). *See also Barry Wright Corp.*, 724 F.2d at 242 (1st Cir. 1983).

[49] Accordingly, this Court can repeat here what it said twice before: "[I]n this case . . . we find it unnecessary to 'consider whether recovery should *ever* be available . . . when the pricing in question is above some measure of incremental cost." *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104, 117 n.12 (1986), quoting *Matshushita*, 475 U.S. at 585 n.9.

otherwise legitimate.[50] The danger posed to competition in the cigarette market was that supracompetitive profits on regular-brand cigarette sales would be preserved by weakening or eliminating the deep-discounted, black-and-white generic cigarettes promoted by Liggett. That threat to competition was hardly offset by the existence of the very supracompetitive profits on regular-brand cigarettes that B&W's conduct had the purpose and effect of protecting.

While profits on regular-brand cigarettes may bear on how long B&W and Liggett would tolerate losses on black-and-whites, Liggett's regular-brand sales were a much smaller share of its total sales. In any event, B&W itself accurately predicted that the losses it inflicted on Liggett would force Liggett to raise list prices on black-and-whites. Thus, B&W's below-average-variable-cost prices on black-and-whites had the requisite potential to injure competition.[51]

Recoupment. *Utah Pie* did not ask whether the challenged low price presaged the achievement or maintenance of higher prices -- a question that came to be expressed a decade or more afterward as the prospect of recoupment. Today, some courts include a prospect of recoupment within the definition of predatory intent,[52] as in

---

[50] Contrast a grocery store's "loss-leader" below-cost milk price. It brings into the store additional customers who will buy something else while there. It thus increases overall sales and *short-run* profits -- an *immediate* profit-increasing strategy that rivals can match with milk or something else. B&W made no claim that its losses on generics promoted the sale of any other product and their opposite effect on sales of regular brands is conceded. Moreover, the jury necessarily found that B&W's pricing was not introductory or otherwise legitimate. Instr. Nos. 27, 28 and 33, J.A. 841, 842, 846.

[51] The identical point can be expressed this way: In the circumstances of this case, black-and-whites are the relevant universe in which to compare prices and costs in order to apply the average-variable-cost-test.

[52] *See Henry*, 809 F.2d at 1344, 1347.

the present case, or make proof of plausible recoupment a predicate for undertaking price-cost comparisons.[53] Requiring a recoupment potential serves, as in *Matsushita*, to eliminate implausible inferences drawn from ambiguous circumstantial evidence: When recoupment is patently impossible, predation is irrational, and the defendant is either acting on fantasy or pricing properly.

As discussed above, however, recoupment is entirely plausible in oligopolies such as the highly concentrated cigarette industry, and surely the jury was reasonable in finding it a genuine prospect here, given persistent supracompetitive prices and high entry barriers, $350 million of threatened regular-brand revenue which provided a source of recoupment, and careful, explicit, and unambiguous market analysis in B&W's sophisticated, high-level documents.

E. Liability Here Would Not Impair Legitimate Price Competition.

Antitrust law must, of course, be sensitive to the danger of mischaracterizing competition as predation and thereby chilling price competition, especially in those oligopolies where price competition is already fragile. Competitors might too often respond to procompetitive price reductions with a lawsuit. Perhaps an unstated concern about such potentially unjustified claims moved the Fourth Circuit to draw its bright line excluding all cases of predation outside of monopoly or cartel settings, though such an exclusion is

---

[53] *See Ashkenazy*, 757 F. Supp. at 1549 (in light of *Matsushita* and *Cargill*, "the threshold determination of the economic plausibility of a predatory pricing scheme should be included in predatory pricing analysis under *Utah Pie* and should end the inquiry if market conditions are not found to support the economic rationality of predatory behavior."). *But see A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1403-06 (7th Cir. 1989), *cert. denied*, 494 U.S. 1019 (1990) (plausible recoupment required to show predation under Sherman Act but not to show threat to competition under *Utah Pie* and the Robinson-Patman Act).

contrary to the statute's own language. But any such concern would be misplaced, for it wrongly assumes that the courts must choose one of two extreme rules: allow a primary-line Robinson-Patman Act suit only when a monopoly or cartel is involved or allow juries to find liability on baseless claims of disciplinary pricing. Either of these choices will harm consumers. Immunizing all predatory or disciplinary price discrimination in every oligopolistic market invites disciplinary conduct bringing about higher prices, just as undue hospitality to predation suits discourages lower prices.

There is no danger that imposing liability in the present case would bring a flood of baseless verdicts. No baseless claim could successfully pass all the filters through which this case has passed:

1. Price-discrimination that neither is cost-justified nor meets competition in good faith.

2. Sustained prices that are below average variable cost and that are not introductory, promotional, or otherwise legitimate.

3. Express and unambiguous proof of a motive to force a rival to raise prices -- that is, to injure consumers.

4. Express, unambiguous, and accurate market analysis by the alleged predator of how it can discipline the rival.

5. Express, unambiguous, and accurate market analysis by the alleged predator of how fellow oligopolists will behave so as to bring about higher market prices.

6. Express calculation by it of the amount and source of recoupment in a highly concentrated market with a history of supracompetitive prices and entry barriers.

No plausible construction of the Robinson-Patman Act could require more.[54] Indeed, the conventional instruction given the jury in many circuits was supplemented in this case by language expressly conditioning liability on B&W's pricing below cost with a reasonable prospect of recoupment through supracompetitive prices.[55] Instr. No. 12, J.A. 829.

This Court should rule that substantial, unjustified, and discriminatory pricing below average variable cost with a reasonable prospect of recoupment suffices to show the reasonable possibility of injuring competition that violates Robinson-Patman Act §2(a).[56]

---

[54] Although actual detrimental effects are not required, higher consumer prices resulted. *See* Part II of this brief.

[55] The conventional instruction allows the requisite injury to competition to be inferred from either (1) actual diminished competition in the market place or (2) "predatory intent" which in turn may be inferred from (a) direct evidence of intent or (b) pricing below average variable cost. The first prong might seem to be triggered by, say, increased concentration even though discriminatory prices greatly exceeded costs; the second prong may direct undue attention to state of mind. In actual application, however, courts often emphasize pricing below average variable cost with a reasonable prospect of recoupment. *See, e.g.*, *Lomar Wholesale Grocery, Inc.*, 824 F.2d at 597-99.

A simpler and clearer instruction would state which of the six factors listed in the text need to be found. However, the instruction given in the present case was satisfactory because the conventional terms were supplemented as just stated in the text.

[56] A reasonable prospect of recoupment can be inferred from the likelihood of effective oligopolistic pricing at supracompetitive levels, from a history of such pricing, or from the clear market analysis of a sophisticated and informed defendant.

II. THE FOURTH CIRCUIT ERRED, AS A MATTER OF LAW, IN DEFINING ANTICOMPETITIVE EFFECTS AND/OR IN REQUIRING THEM.

The Fourth Circuit believed its "theoretical suspicions" were "confirmed" by the "perfect vision of hindsight," which saw a larger market share for discounted cigarettes notwithstanding a shrunken discount and higher prices for both generic and regular-brand cigarettes. The court may have meant merely that its theory of impossible oligopolistic predation was borne out by events. Or it may have intended an alternative holding that the absence of consummated injury to consumers absolves otherwise predatory conduct. In either event, it erred as a matter of law. The price rise that actually occurred constituted injury to consumers. Moreover, substantial, unjustified, and discriminatory pricing below average variable cost with a reasonable prospect of recoupment violates the statute whether or not prices rise.

The court below led itself astray by misdefining B&W's objective as stopping the growth of the generic sector, rather than merely slowing that growth by managing prices upward -- that is, by stabilizing and then shrinking the gap and thus weakening the generic brake on rising cigarette prices generally. It is clear that higher prices themselves count as an actual injury to competition and consumers. *E.g.*, *NCAA v. Board of Regents of University of Oklahoma*, 468 U.S. 85, 106-07 (1984). Moreover, a reasonable jury could conclude that the generic segment would have been even larger in the absence of B&W's predatory conduct.[57]

---

[57] B&W's own economic expert acknowledged that competition is injured by inducing a rival to reduce its competitive efforts (J.A. 650), and the District Judge said in denying B&W's request for a directed verdict:

> A year after Brown & Williamson's entry, they recognize - and their executives recognize - that plaintiff's consumer advertising had been reduced, and the growth of the category appeared to have slowed. The slowing of the growth of the

Compounding its misconception of what constitutes an anticompetitive effect, the Fourth Circuit also erred if it intended to hold that actual injury to consumers is a prerequisite to the violation. Imposing such a prerequisite is contrary to the statute, which condemns discriminatory pricing where the effect "*may be* substantially to lessen competition . . ." (emphasis added). It is also wrong in principle, because conduct should be judged as of the time it occurs. Doing so educates would-be predators as to their duties under the statute and thus protects the market from unjustified conduct posing a genuine threat to competition. Genuinely dangerous conduct should be prohibited notwithstanding its abandonment after a legal challenge or lack of success. Substantial, unjustified, and discriminatory pricing below average variable cost with a reasonable prospect of recoupment creates the reasonable possibility of injuring competition, as forbidden by the statute and found by the jury in this case.

The lower courts generally understand the point. For example, the Eighth Circuit requires "some reasonable expectation on the part of the alleged predator that it will succeed" while recognizing that "predatory intentions need not be accomplished." *Henry v. Chloride, Inc.*, 809 F.2d 1334, 1345 n.9 (8th Cir. 1987). *See also International Air Indus. Inc. v. American Excelsior Co.*, 517 F.2d. 714, 720 n.10 (5th Cir. 1975), *cert. denied,* 424 U.S. 943 (1976) ("Under the Robinson-Patman Act, of course, it is not necessary to show actual damage to competition, it is only necessary to show that there is a reasonable possibility that

---

category gives recoupment in the branded sales retained, and a slowing of the growth of the segment can lessen the downward pull on the branded prices. And, in fact, the gap did narrow between branded and generic [prices] according to the evidence thus far before the court. Tr. 67:63.

And the ability of [Liggett] to compete and to offer consumers a lower price or a lower price choice had been compromised. [B&W] recognized this in their own documents in evidence. Tr. 67:64.

the discrimination may have that effect. *See Corn Prods. Refining Co. v. FTC*, 324 U.S. 726 (1945).").

The same is true even under the more demanding tests of Sherman Act §2. While nearly all the circuits assess the market before finding a "dangerous probability" of monopoly, they usually make clear that conduct is to be judged at the time it was undertaken in the light of market circumstances as they then appeared to the actors. E.g., *Multiflex, Inc. v. Samuel Moore & Co.*, 709 F.2d 980, 992 (5th Cir. 1983), *cert. denied*, 465 U.S. 1100 (1984) (relevant time is "when the acts occur"; "hindsight" cannot "exonerate an antitrust violator who did cause damage to the plaintiff."); *United States v. American Airlines, Inc.*, 743 F.2d 1114, 1118 (5th Cir. 1984), *cert. dismissed*, 474 U.S. 1001 (1985) ("[W]e do not rely on hindsight but examine the probability of success at the time the acts occur.").[58]

In short, the Fourth Circuit was wrong to think that the actual state of the cigarette market at the time of trial confirmed its "theoretical suspicion" that oligopolistic predation is impossible. Nor does the state of the market provide an alternative ground for disregarding the jury verdict.

---

[58] Even if consumers had not actually been injured, B&W's violation undoubtedly caused Liggett actual injury. Liggett's injury is "antitrust injury;" it is the kind that an antitrust law against predatory pricing is designed in the first instance to prevent in order to protect consumers from the ultimate harm of supracompetitive prices. *See Multiflex, Inc.*, 709 F.2d at 994 (plaintiff's injury is antitrust injury when it actually results from conduct that violates the antitrust laws because it is the kind of conduct that, if success "had materialized, would have caused the type of market damage the antitrust laws seek to prevent."); P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 340.2b (1992 Supp.).

CONCLUSION

The judgment of the Court of Appeals should be reversed.

Respectfully submitted,

Phillip Areeda
Counsel of Record
1545 Massachusetts Avenue
Cambridge, MA
(617) 495-3160