92-466

No. 92-

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.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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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?

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Liggett Group Inc. ("Liggett"), now named Brooke Group Ltd.[1], petitions the Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fourth Circuit is reported at 964 F.2d 335 (4th Cir. 1992), and reprinted at Petitioner's Appendix ("Pet. App.") 1a. The opinion of the United States District Court for the Middle District of North Carolina granting judgment notwithstanding the verdict for respondent Brown & Williamson Tobacco Corporation ("B&W") is published at 748 F. Supp. 344 (M.D.N.C. 1990), and reprinted at Pet. App. 17a. The opinion of the District Court denying summary judgment for B&W is published at 1989-1 Trade Cas. (CCH) ¶68,583 (1988).

JURISDICTION

The Court of Appeals entered judgment on May 11, 1992 and denied petitioner's petition for rehearing and suggestion for rehearing *in banc* on June 18, 1992. Pet. App. 15a. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

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), which provides in relevant part:

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[1] Pursuant to Supreme Court Rule 29.1, petitioner provides the following corporate information. Brooke Group, Ltd. is a publicly owned corporation which holds a controlling interest in New Valley Corporation. Brooke Group, Ltd, has no parent corporation.

> 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

This case presents the issue of whether respondent's admitted price discrimination had a reasonable possibility of injuring competition. The Fourth Circuit held that, absent a conspiracy, an oligopolist could never be sufficiently certain of a pay off to threaten competition. It therefore limited liability under the Robinson-Patman Act for predatory price discrimination to instances where the defendant is a monopolist or conspirator. The Fourth Circuit disregarded both a sophisticated defendant's own analysis that its below-cost price discrimination paid off and Congress' explicit judgment that competition could be hurt by price discrimination by a firm that is neither a monopolist nor conspirator. By substituting an idiosyncratic and illogical view of economic theory for the mandate of the Robinson-Patman Act, the Fourth Circuit decision conflicts with decisions of this Court and other circuits. By immunizing an oligopolist's price discrimination, which is an effective tactic for disciplining maverick price cutters, the Fourth Circuit invites disciplinary pricing.

1. *Legal Context*. Although amended by the Robinson-Patman Act in 1936 (mainly in other respects), the statutory provision at issue here was part of the 1914 Clayton Act, which was designed to condemn conduct not already reached by the 1890 Sherman Act. The original Clayton Act provision focused on a seller's price discrimination that might impair "primary line"

competition -- that is, competition between a seller and its rivals.[2] This is a primary-line case. The test of legality is whether the effect "may be substantially to lessen competition or tend to create a monopoly." 15 U.S.C. §13(a). According to this Court, price discrimination with a "reasonable possibility of injury to competition" is unlawful. *See Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685, 698, 701 (1967). The jury was instructed accordingly.

Through the 1960s, claims of primary-line injury were usually left to juries under vague instructions inviting them to condemn price discrimination "intended" to injure competition.[3] *Utah Pie* endorsed this approach.

Beginning in the late 1970s, lower courts came to understand that price cuts are often a means of legitimate competition and that even discriminatory cuts do not injure competition among manufacturers unless they are "predatory." Since then, courts have typically tested prices against costs -- usually average variable costs -- to distinguish improper pricing from legitimate competition under both the Robinson-Patman Act and Sherman Act § 2.[4] Those courts stating the Robinson-Patman test in terms of

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[2] The much criticized 1936 amendment focused on "secondary-line" competition among the recipients of discriminatory prices; it sought to discourage a supplier from favoring chain stores and other large retailers over the smaller dealers competing with them.

[3] For a summary of such Robinson-Patman cases, see generally E. Kintner and J. Bauer, 3 *Federal Antitrust Laws* at 276-289 (1983).

[4] Sherman Act §2, 15 U.S.C. §2, makes it unlawful for any person to "monopolize, or attempt to monopolize ... any part of trade or commerce among the several states." Sherman Act § 2 is reprinted in full at Pet. App. 54a.

predatory intent infer it from below-cost pricing,[5] and some courts have supplemented price-cost tests with intent evidence.[6]

Recently some courts have also asked whether it is possible for the alleged predator to "recoup" the losses resulting from below-cost pricing.[7] Recoupment is simply the payoff for below-cost pricing. In the standard monopoly predation model, one firm voluntarily incurs losses by selling a product for less than its variable cost in order to ruin rivals, gain a monopoly, charge monopoly prices, and earn monopoly profits recouping those earlier losses. This case poses the questions (i) whether, as a matter of law, only a monopolist (or organized cartel) would think recoupment likely enough to undertake unjustified below-cost pricing, and, therefore, (ii) whether an oligopolist's sustained and unjustified discriminatory prices below average variable cost never creates a "reasonable possibility of injuring competition."

2. *Factual background*. Until 1980, all cigarettes were sold at the same price by the six cigarette manufacturers. A5605-08, A5774, A5777, A5923-4.[8] In the words of B&W's President, "[o]ne key on the cash register rang up all cigarette sales." A2204, A5948-49. In classic oligopolistic fashion, one company would raise its prices and the other five would follow immediately. These lock-step price increases happened regularly and often, even when the demand for cigarettes and the price of tobacco fell. A5608-09, A5791-93, A5946-47, A6003-05, A6324-33. Profits

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[5] *E.g.*, *Double H. Plastics, Inc. v. Sonoco Products Co.*, 732 F.2d 351, 354 (3d Cir.), *cert. denied*, 469 U.S. 900 (1984); *William Inglis & Sons Baking Co. v. ITT Continental Baking Co.*, 668 F.2d 1014, 1040-41 (9th Cir. 1981), *cert. denied*, 459 U.S. 825 (1982).

[6] *E.g.*, *McGahee v. Northern Propane Gas Co.*, 858 F.2d 1487 (11th Cir. 1988), *cert. denied*, 490 U.S. 1084 (1989).

[7] *E.g.*, *Henry v. Chloride, Inc.*, 809 F.2d 1334 (8th Cir. 1987). *Cf. A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F. 2d 1396 (7th Cir. 1989), *cert. denied*, 494 U.S. 1019 (1990) (Sherman Act § 2).

[8] These and subsequent factual citations, beginning "A," are to the Fourth Circuit Appendix.

have been supracompetitive and among the highest of any industry, and entry barriers have precluded successful new entry for more than fifty years.[9] A6357-78, A6381-87, A3216.

In 1980, plaintiff Liggett -- in defendant B&W's words -- "was on the verge of going out of business" and "made the bold move" of introducing a generic cigarette in a black-and-white package at a substantial price discount. *Id.* 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." A1417. Liggett's black-and-white generics were deeply discounted, originally at prices 30% below branded cigarettes. By mid-1984, the discount grew to 40% as Liggett declined to raise black-and-white prices as fast as regular cigarette prices. A1295; Pet. App. 6a.

By mid-1984, Liggett's black-and-white cigarettes accounted for 4% of the entire cigarette market (A3049), 97% of all reduced-price cigarettes (A1221), and about 60% of Liggett's total sales (A1335).[10] The other cigarette manufacturers, according to

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[9] B&W's economic experts agreed with most of the evidence upon which Liggett's expert relied for this conclusion, A6334-35, A6344-56, A6386-88, A7010-11, A7006-08, A7764-66, which was also supported by scholarly writings in the record. *See* note 19 *infra*. Without discussing this market's non-competitive history, the opinion below noted the testimony of Liggett executives that the industry was "competitive" during the "price war." But "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).

[10] During the relevant time period, reduced-price cigarettes were almost entirely black and white. As for the others:

In 1983 two companies, B&W and Reynolds, started including 25, instead of 20, cigarettes in each pack of their respective Richland and Century brands, which were sold at full price. As B&W noted, these so-called "25s" are "not a direct, effective defense against generic growth."

B&W's internal analysis, were concerned that black-and-whites would not attract new buyers but would "cannibalize" high-profit brand name sales. A2066. They were also concerned that "unchallenged, [Liggett] will continue aggressive segment development since it has virtually no stake in the branded, full price market." A1341.

B&W was hardest hit. Over one-fifth of Liggett's generic cigarette consumers had previously patronized B&W brands, even though B&W's share of the cigarette market was 12%. A1420-21. B&W calculated prior to its entry that continued growth of black-and-white cigarettes would cost it $350 million in lost revenue by 1988. A1341.

On May 31, 1984, B&W announced that it would introduce a black-and-white cigarette by mid-July. A4410. That cigarette was intentionally packaged to look as much like Liggett's as possible. A1272, A1213. B&W's stated goal was to "gradually reduce [the] percent difference between generics and full revenue

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A1346. B&W's president did not even consider 25s to be generic cigarettes. A2211. Another B&W document stated, "25s are not the answer to generics." At the time of trial in 1989, 25s represented less than 1% of all cigarette sales. A5389.

In May 1984, R.J. Reynolds reduced the list price of one of its brands, Doral. However, Doral did not become significant until 1985, when its market share reached 1.3%. A2966. Doral, and other "branded-generic" cigarettes introduced in and after 1986, were not considered as threatening to profits as black-and-whites: Reduced-price brand-name cigarettes carry less of a price-discount message than black-and-whites and have greater brand loyalty, and thus their price can be more easily increased. A1420. For example, Reynolds did not think it necessary for Doral to follow B&W rebates on black-and-whites.

Although Philip Morris and Reynolds ultimately introduced black-and-white generics in 1986 and 1988 respectively, they focused on private label sales, and their combined black-and-white market share was less than one-half of one percent at the time of trial. A5928-29, A5399.

brands."[11] A2403. *See also* A1270-1271, A6130-35, A1321. Once that price gap was reduced, B&W reasoned, consumers would be less willing "to trade-off image for price." A1322. B&W planned to bring about higher prices by offering discriminatory rebates targeted at Liggett's largest wholesale customers and thus forcing Liggett to offer comparable rebates, thereby suffering large losses until it raised list prices, which would mean higher consumer prices. A1827, A1676, A1813. B&W calculated that Liggett lacked "the financial resources of others in the industry," is thus "unlikely" to "engage in a sustained battle," and therefore "will try to survive by raising prices on generics." A1363, A1865. B&W accurately predicted that Liggett's parent company, which was trying to sell Liggett, would not tolerate indefinite losses and eventually would raise list prices as the only way to return to profitability. A1827, A6229. B&W's strategy was not necessarily to destroy Liggett or kill generics, but to weaken Liggett's commitment to hold down black-and-white list

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[11] Although it is customary and convenient to refer to B&W's intent as reflected in the documents prepared and used by B&W's senior officials, petitioner does not contend that B&W's anticompetitive motive in itself violates the statute. Rather, the "intent" evidence resolves any ambiguity in B&W's conduct; it has told the court what it is up to. The "intent" evidence reveals a sophisticated actor's own market analysis and predictions about how that market works and the potential for a profitable payoff from disciplinary pricing. *See Chicago Board of Trade v. United States*, 246 U.S. 231, 238 (1918) ("knowledge of intent may help the court to interpret facts and to predict consequences").

According to the District Court, anticompetitive intent was documented more clearly than in any known case. Pet. App. 31a. The Fourth Circuit opinion said nothing about B&W's intent except twice to quote the same sentence from a B&W document, implying that B&W may have abandoned any previous anticompetitive intent when R.J. Reynolds introduced a generic-priced cigarette named Doral. Pet. App. at 4a-5a. However, B&W stated after the introduction of Doral that its intent had not changed and that its entry would be "alike in every way to the original proposition. . .," and subsequent B&W documents reiterated B&W's anticompetitive intent. A1412, A1667, A1769. *See also Liggett Group, Inc. v. Brown & Williamson Tobacco Corp.*, 1989-1 Trade Cas. (CCH) ¶68,583 (1988) (providing a comprehensive summary of the B&W intent documents).

prices. With Liggett's commitment thus reduced, B&W would then be free to raise black-and-white prices, and thus "reduce" the "percent difference between generics and full revenue brands." A6130, A4376. As a result, consumers would pay higher prices for all cigarettes, both branded and generic.

For eighteen months after its entry, B&W repeatedly paid large volume-based rebates on black-and-white cigarettes, resulting in net prices that varied discriminatorily among wholesalers and that were well below B&W's average variable cost, as B&W had planned from the outset.[12] A7003, A7799. For eighteen months in 1984 and 1985, B&W's generic revenues were $14.9 million (30¢ per carton) below its average variable costs. A6547, A6704, A3094-3196, A6272. The jury found that B&W's below-cost pricing was not legitimately introductory or promotional. Instruction No. 27, A7952.

According to B&W's own strategic documents, price discrimination was integral to its predatory plan. A1248, A1348, A1745. It assured its parent company that its pricing of black-and-whites to wholesalers would not have the undesired effect of expanding demand for generic cigarettes. A1244. Rather than reduce list prices, B&W explained, it would grant discriminatory rebates to wholesalers, who would be unlikely to pass the savings on to consumers and who mainly did not do so. A1765. The rebates were often paid months after the cigarettes to which they applied had been resold. A4420. As B&W explained:

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[12] The Fourth Circuit quoted a B&W document planning to sacrifice no more than "full variable margin." Pet. App. 5a. However, under B&W's accounting system, sacrificing full variable margin meant a price below average variable cost. A7044-48. Moreover, both B&W experts conceded that on a pre-tax basis B&W priced its black-and-whites below their average variable cost for eighteen months in 1984 and 1985. Because these losses partially offset company profits gained from other sales -- whether branded cigarettes for B&W or biscuits -- 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*, 1989-1 Trade Cas. (CCH) ¶ 68,583 (1988) at 61,107-08 ("The Court has found no case law or legal literature that supports B&W's position").

> [T]he 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. A1765, A1244.

Moreover, B&W believed that discrimination could discipline Liggett at least cost to B&W because it would "[a]chieve maximum desired volume through a minimum number of customers," thus reducing B&W's investment in its anti-competitive scheme. A5742.

B&W carefully analyzed the likely responses of its fellow oligopolists. It concluded (1) that its larger rivals would not price below cost in order to discipline Liggett for fear of antitrust liability (A1335, A1353, A1354); (2) that they would not forsake the industry's long-standing oligopoly pricing (A1419-20); (3) that they had no incentive or desire to keep prices as low as Liggett at the expense of their very large shares of higher priced cigarettes (A1341-42); and, therefore, (4) that disciplining Liggett would pay off (A1341). To be sure, B&W forecast that other manufacturers would be "quite likely" to "introduce branded generics, develop loyal franchises, and then gradually raise prices over the longer term" so that they could "participate" in the generic segment "in order to manage prices and profitability upward."[13] A1419-20. To ensure that Philip Morris and R.J. Reynolds did not mistake B&W's goal and unintentionally interfere with B&W's objective of managing the price of generic cigarettes upward, B&W decided to "signal intent to competition" that its entry would "not expand segment." A1278. Rebates rather than lower list prices have that effect.

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[13] For example, B&W predicted that R.J. Reynolds would enter the segment but "would strive to limit the [generic] segment development since incremental generic growth will disproportionately reduce RJR's total margins." A1345. B&W also believed that the industry leader, Philip Morris, "will not take a leadership position in the low margin brand marketing." A1862.

True to its prediction, B&W succeeded in disciplining Liggett. Liggett spent $89.6 million trying to meet B&W's below-cost, discriminatory rebates to wholesalers. A6149-60. By June, 1985, Liggett could no longer afford the losses thus inflicted on it, but neither could it afford to forfeit its remaining generic business by ceasing its efforts to meet B&W's rebates. A6241-42, *see also* A5906-19. B&W wrote, "Liggett will try to survive by raising prices of generics." A1865. Just as B&W predicted, Liggett raised the list price of its generics, and consumer prices rose. A1865. B&W matched that price increase in October 1985.[14] In December 1985, Liggett resisted B&W's attempt to lead price increases. Thereafter, a disciplined Liggett followed B&W's price increases on black-and-whites.

In June 1986, December 1987, and again in June 1988, B&W led generic prices up at a faster rate than general cigarette price increases. A2887, A2889-90, A2893, A2896, A2898. Although other manufacturers entered the black-and-white segment in 1986 and 1987, as B&W predicted, they were happy to shrink the discount, and B&W's internal documents take credit for disciplining Liggett and reducing the attractiveness of generics. A1667. As an R.J. Reynolds executive testifying at B&W's behest admitted, the industry was managing prices and profitability upward by 1987. A7896-97. The price differential between generics and brand-name cigarettes declined from almost 40% in 1985 to 26.8% in 1989.[15] Pet. App. 6a, A4312, A4280-81. As a result, the prices of both brand-name cigarettes and generics increased dramatically in classic oligopolistic fashion. In 1988,

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[14] The delay, according to B&W documents, was designed to increase its volume so that it would be in a stronger position to manage black-and-white prices upward. A2182.

[15] 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. A4312. At the time of trial in late 1989, subgeneric sales were less than 1% of all cigarette sales. A5389, A5399. Although Liggett thus reintroduced price competition in December 1988 -- when renewed predation was unlikely because this case was underway -- B&W's conduct at least reduced the discounts available to consumers during 1986, 1987 and nearly all of 1988.

generic prices were higher than brand-name prices had been at the time B&W entered the generic segment -- a phenomenon that cannot be attributed to increased costs or inflation. A7817-18, A6334-35, A6344-56.

B&W informed its corporate parent approximately one year after entering the generic segment, that its strategy had succeeded in slowing the rate of growth of the generic segment. A1667, A1767. By the time of trial in late 1989, the black-and-white segment had dropped to 2.7% of total cigarette sales. A4274. Although reduced-price brand name cigarettes (branded generics) accounted for 10.66% of the cigarette market by the end of 1989, they did not provide an effective brake on increasing cigarette prices. *See* A5399, A4312. Just as B&W had predicted, the other manufacturers did not interfere with B&W's efforts to reduce the discount from brand-name prices because the other manufacturers had the same desire as B&W "to manage prices and profitability upward." A1419-20. B&W recognized that the "future growth of generics will be driven by consumer demand" responding to the price discount and "not by the number of manufacturers who supply those products." A1370.

3. *Proceedings below*. The jury returned a verdict for Liggett. As required under Instruction No. 12, the jury found that B&W engaged in "loss creating price cutting," that there was a "real possibility" of "recoup[ing] such losses" from "prices higher than competitive levels," and thus that B&W's discriminatory, below-cost pricing had a "reasonable possibility of injuring competition in the cigarette market as a whole." A7940-42. The jury was specifically instructed that "[t]he Robinson-Patman Act was designed to protect competition rather than just competitors" and that Liggett "cannot satisfy this element simply by showing that they were injured by Brown & Williamson's conduct." *Id.*

In August 1990, 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. Although the District Court recognized the theoretical possibility that recoupment could take place in an oligopoly setting, it did not credit the jury verdict that profits were supracompetitive, and it reasoned that without supracompetitive profits, disciplining Liggett would merely cause B&W to lose money without any payoff. Pet. App. 33a. The District Court further concluded that there was insufficient "alignment of interest" among the cigarette oligopolists to allow the price gap between branded and generic cigarettes to narrow. Pet. App. 36a.

The Fourth Circuit affirmed, though on 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 have been irrational for an oligopolist to have so acted. According to the court's "economic logic," only a monopolist (actual or prospective) or a member of an organized cartel could profit from charging below-cost prices to discipline a rival: An oligopolist's below-cost investment in disciplinary pricing could never pay off because an alleged predator could never be "certain" that fellow oligopolists would (1) understand that it was disciplining a maverick rather than attempting to expand its own market share, (2) refrain from trying to expand their own market shares, or (3) continue the preceding oligopolistic pricing pattern of prior decades. Pet. App. 11a. The Fourth Circuit believed that its theoretical speculation was confirmed in "hindsight" by the growth of the generic sector, notwithstanding the reduced generic discount and resulting higher prices for both generic and brand-name cigarettes. Pet. App. 12a.

REASONS FOR GRANTING THE PETITION

If the Fourth Circuit decision is permitted to stand, targeted discriminatory price disciplining by oligopolists will be immune from antitrust liability even when there is evidence of anticompetitive intent, conduct, and effect. In conflict with this Court and with other circuits, the Fourth Circuit created a rule of *per se* legality for discriminatory, below-cost pricing by a sophisticated oligopolist undertaken for the express predatory purpose and with the demonstrated effect of raising prices to the detriment of consumers.[17]

Ignoring B&W's carefully analyzed prediction that its disciplinary pricing would be amply recouped through the supracompetitive profits long maintained in the highly concentrated cigarette industry, the Fourth Circuit invoked its own "theoretical suspicions" to conclude as a matter of "economic logic," unsupported by the record, that only a single-firm monopolist or a cartel could be "certain" below-cost pricing would pay off. Pet. App. 12a. By requiring either single-firm monopoly or a conspiracy, the court made the Robinson-Patman Act's prohibition of primary-line injury redundant of the Sherman Act. This judicial curtailment is directly contrary to the language and carefully stated purpose of the 1914 Congress "to prohibit and make unlawful certain trade practices, which...are not covered by the Sherman Act." S. Rep. No. 698, 63d Cong., 2d Sess. at 2. Indeed, as shown below, p.14-15, disciplinary predatory pricing by an oligopolist may be a greater threat to competition than predation by a monopolist.

By requiring "certainty" of recoupment, the Fourth Circuit seriously misread *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986) (Pet. App. 13a), as permitting the court to substitute its own theorizing for the reasonable expectations of a sophisticated market participant and for the well-supported findings of the jury.

Relying on its view of "economic logic," the court reasoned that an oligopolist could not succeed in recouping its investment, and thus was driven to conclude that success had not occurred (notwithstanding both shrinkage in the generic discount and higher prices). This counterfactual conclusion implicitly holds that lack of success immunizes otherwise unlawful pricing below average variable cost.

[17] Respondent was concerned that Liggett's lower-priced generics would cut into existing markets for higher-priced cigarettes, rather than attract new smokers. The relative inelasticity of demand for cigarettes means that higher prices generally cause smokers to pay more for cigarettes rather than reduce smoking.

These issues of law are important to antitrust policy. While few consumer markets are as concentrated as this one, other high-volume consumer products also bear supracompetitive oligopolistic prices. Oligopolists will be prompt to accept the invitation of the Fourth Circuit to discipline price cutters at the expense of consumers. This Court should grant certiorari to direct that statutory language, policy, and the precedents of this Court not be displaced by dubious economic speculations; and to resolve conflict regarding administration of the Robinson-Patman Act. With a fully developed record and jury verdict, this case is well-framed to focus these questions regarding the role of economic theory to implement, rather than subvert, legislation.

1. *The Fourth Circuit misapplied economic theory to restrict the scope of Robinson-Patman Act liability, violating the Act's language and purpose and conflicting with other courts.*

a. *Unlike the Sherman Act, the Robinson-Patman Act is not limited to conspiracy or single-firm monopoly. Per se* immunity for disciplinary price discrimination in the absence of actual or prospective monopoly or express cartelization is inconsistent with the language and purpose of the Robinson-Patman Act. By its own terms, the statute applies to one firm's price discrimination that "may substantially lessen competition or tend to create a monopoly . . . or injure . . . competition with [the discriminating seller]." The Act's reference to single-firm conduct is inconsistent with any conspiracy requirement, and the disjunctive language obviates any monopoly requirement. While Congress thus intended this statute to reach conduct "not covered by the [Sherman Act],"[18] the Fourth Circuit limited Robinson-Patman

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[18] S. Rep. No. 698, 63d Cong. 2d Sess. at 2 (1914). A special House subcommittee established in 1975 to consider proposed amendments to the Robinson-Patman Act which would have limited the Act's reach to that of the Sherman Act, as the court below did, found:

> "[t]he predatory price discrimination application of Robinson-Patman reaches those practices which are beyond the scope of the Sherman Act. The proposed revision would emasculate Robinson-Patman in this respect. However, no one has articulated a sound basis for radically limiting the Act's primary-line competition reach."Ad Hoc Subcommittee on

Act coverage of predatory and disciplinary pricing to monopolies and conspiracies already forbidden by Sherman Act §§ 1-2.

Congress' concern with primary-line price discrimination was not misplaced. Disciplinary price discrimination in stable oligopolies cannot be dismissed as a trivial problem. It is *more* likely to occur than monopoly predation. *First*, highly concentrated oligopoly is more frequent than monopoly. *Second*, an industry history of persistent supracompetitive prices without new entrants provides better assurance of a payoff than is available to a would-be monopolist guessing about future entry after prices have become supracompetitive. *Third*, disciplining a competitor is probably quicker than destroying it and thus requires a smaller investment in below-cost pricing. *Fourth*, price discrimination allows a predator to target its price cuts, thereby lowering its investment in below-cost pricing and making recoupment more likely. As B&W put it, a predatory oligopolist can "put the money where the volume is." A-5742. The Fourth Circuit decision encourages just such pricing by any oligopolist that thinks it can profit from it -- without fear of legal liability.

b. *Economic theory does not require conspiracy or single firm monopoly as a predicate for predatory pricing*. The Fourth Circuit panel stated that, in the absence of monopoly or organized cartel, an oligopolist could never be certain that losses from below-cost pricing would pay off and, therefore, it would be irrational to do what B&W did in this case. The court alluded to two possible mechanisms that would prevent such recoupment in an oligopoly: (1) conscious parallelism of an oligopoly is less reliable and more likely to break down than an express conspiracy, and (2) fellow oligopolists might misperceive disciplinary price cutting as promotional and respond with aggressive promotional pricing of their own, frustrating the achievement or maintenance of supracompetitive prices. As to the first, the court did not

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> Antitrust, The Robinson-Patman Act and Related Matters, Recent Efforts to Amend or Repeal the Robinson-Patman Act, H.R. Rep. No. 94-1738, 94th Cong. 2d Sess. at 76 (1976).

The Subcommittee recommended to Congress that it "should not consider favorably nor take any action on proposals or legislative measures to weaken, emasculate, or repeal the Robinson-Patman Act. . . ." *Id.*

mention the record evidence that, apart from two brief outbreaks of price competition -- one in the 1930s and the other Liggett's black-and-whites -- which were both effectively disciplined, this industry has long been the textbook example of long-maintained supracompetitive prices and profits achieved and maintained without conspiracy.[19] As to the second, 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 panel's view, an oligopolist would never act on such a shared interest because "[t]he oligopolist on the sideline would need to be certain that the others were also confident on the point. Such confidence must be rare . . . . More likely, [the other oligopolists] would react competitively." *Id.*

Requiring certainty is misconceived. Not even a monopolist can be certain of successfully recouping by preserving its monopoly. Certainty is also impossible in an express cartel, whose members may "cheat."[20] If certainty were a prerequisite to threatened impairments of competition, antitrust law would have no occasion to fear the mergers that create oligopoly or the practices that facilitate its supracompetitive pricing. Yet, antitrust law does prohibit mergers that create or reinforce oligopoly as well as practices that facilitate oligopoly pricing.[21]

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[19] *See* F. Scherer and D. Ross, *Industrial Market Structure and Economic Performance* 250-251 (3d ed. 1990) (A7817-7818) (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 manufactures raised prices sufficiently to increase their profits from $3.80 to $11.55 per thousand cigarettes sold between 1980 and 1988").

[20] *See id.* at 238.

[21] *See, e.g.* U.S. Department of Justice Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶13,104 (1992) at 20,571 ("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"); R. Posner, *Antitrust Law* 40 (1976) ("sellers

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. In this case, B&W examined each major rival in turn and analyzed how each would react to Liggett's conduct and to B&W's projected plan to discipline Liggett. Directly disposing of the Fourth Circuit's "theoretical suspicions," moreover, B&W memoranda explained that it would "signal [its] intent to competition" that its entry and rebates would "not expand [the] segment." A1278. 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 to manage prices and profitability upward" to the detriment of the consumer. A1419-20. B&W memoranda also explained how any losses from below-cost pricing -- which turned out to be some $15 million -- would be more than offset by additional revenues from consumers of $350 million over the next four years. A1341. As this Court itself recognized in *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 589 (1986), predation is plausible when an investment in below-cost sales can be more than paid back *either* by obtaining "future monopoly profits" or by protecting "future undisturbed profits."[22]

The Fourth Circuit said nothing about B&W's own market analysis and predictions that differed dramatically from the court's

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might be able to coordinate their pricing without conspiracy in the usual sense . . . . There is . . . 'oligopolistic interdependence' . . . in contrast to the explicit collusion of the formal cartel or its underground counterpart"); *United States v. Container Corp.*, 393 U.S. 333 (1969).

[22] Quoting R. Bork, *The Antitrust Paradox* 145 (1978). While the Court spoke of "monopoly profits," it did so in the sense of "enough market power to set higher than competitive prices." *Matsushita*, 475 U.S. at 590. *See also Cargill Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104, 119 n.15 (1986) (acknowledging the plausibility of a nondominant firm engaging in predatory pricing if there was collusion, not just an unlawful conspiracy); *Eastman Kodak Co. v. Image Technical Serv. Inc.*, _____ U.S. _____, 112 S. Ct. 2072, 2086 n.21 (1992) (an oligopolist can "reap supracompetitive prices" by observing and following its rivals).

"theoretical suspicions." *See* Pet. App. 12a. The speculation of lawyers and judges about potential profits is no substitute for a sophisticated defendant's own carefully designed market analysis and unambiguous plan.[23]

c. *Immunizing actual conduct as "implausible" for a hypothetical oligopolist in a generalized, hypothetical market offends Matsushita and good sense.* The Fourth Circuit completely misunderstood this Court's *Matsushita* decision and then based its erroneous conclusion in this case on that misunderstanding. *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 an express conspiracy would have been illegal regardless of speculations about its chances of success or about its "rationality" for the defendants. 475 U.S. 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's 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 designed to injure consumers (a key element under the Robinson-Patman Act -- analogous to the Sherman Act conspiracy element 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. Contrary to

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[23] "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).

the Fourth Circuit, a recoupment requirement serves to eliminate claims grounded on implausible inferences based on ambiguous circumstantial evidence, not to ignore strong evidence.

That a Court of Appeals would so misunderstand *Matsushita* highlights the need to instruct the lower courts that although economic theory can indicate what evidence is required and can therefore illuminate both ambiguous evidence and legal standards, judicial theorizing that conduct is implausible does not trump clear evidence that it actually occurred. *Eastman Kodak Co. v. Image Technical Serv., Inc.*, ___ U.S. ____, 112 S. Ct. 2072 (1992).[24] While theory offers several hypotheses about oligopoly behavior, the workings of any particular oligopoly market can be understood only by examining it -- which the Fourth Circuit conspicuously failed to do. Other circuits have not misunderstood *Matsushita* in this regard,[25] and this Court should make clear that those other courts represent the authoritative understanding of that case.

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[24] In *Kodak*, this Court refused to accept the "theory" that a defendant's lack of power in a machine market *necessarily* precluded power over its unique repair parts. Instead, the Court noted other theoretical explanations of how the defendant without power over machines might obtain supracompetitive prices for its unique repair parts from at least some machine users. 112 S.Ct. at 2085-87. Because the summary judgment record was consistent with the latter theory, the Court found a triable issue. By contrast, the Fourth Circuit held that its theory of impossible recoupment in oligopoly trumped the rival theory *that was supported by the evidence and verdict*. At the very least, therefore, this Court should grant certiorari, vacate the judgment below, and remand for reconsideration in the light of *Kodak*, which appeared after the opinion below, though before denial of reconsideration.

[25] *E.g.*, *Arnold Pontiac-GMC, Inc v. Budd Baer, Inc.*, 826 F.2d 1335, 1338-39 (3d Cir. 1987) (where strong direct evidence exists *Matsushita* has "little or no applicability"); *McLaughlin v. Liu*, 849 F.2d 1205 (9th Cir. 1988) ("It is clear from the *Matsushita* opinion that the Court was not speaking of direct evidence, but of circumstantial evidence. *Matsushita* authorizes an inquiry on summary judgment into the 'implausibility' of inferences from circumstantial evidence, particularly in antitrust conspiracy cases, not an inquiry into the credibility of direct evidence").

d. *The Fourth Circuit's conception of economic logic conflicts with other courts, which are already in disarray.* This Court has never required actual or prospective monopoly or a cartel for a primary-line Robinson-Patman Act violation. It last addressed primary-line injury in *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685 (1967). The Court condemned price discrimination without proof of single-firm monopoly or conspiracy and with far less threat to competition than in the present case.[26]

Utah Pie has not fared well in the lower courts. Indeed, the Seventh Circuit saw "widespread civil disobedience in the judiciary" to that ruling. *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396 (7th Cir. 1989), *cert. denied*, 494 U.S. 1019 (1990). *Utah Pie* has been criticized for excessively weighing intent to harm a rival. The lower courts responded, as did the jury instructions in the present case, by requiring intent to harm consumer interests and by directing jury attention to whether prices were below average variable cost. However, it is only the Fourth Circuit that finds *Utah Pie* so "difficult to understand in the light of recent economic theory," as to demand monopoly or conspiracy for a Robinson-Patman offense. Pet. App. 8a.

Indeed, the contrast between the Fourth Circuit's decision in this case and the Seventh Circuit in *A.A. Poultry* and the Ninth Circuit in *William Inglis & Sons Baking Co. v. Continental Baking Co.*, 942 F.2d, 1332 (9th Cir. 1991), *modified on other grounds,*

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[26] There, modest evidence of intent to harm a rival by planting a spy in its plant and referring to it as an "unfavorable factor in the market"; here, overwhelming evidence of unambiguous intent to harm both a rival and consumers, an express and sophisticated analysis of how to succeed in doing so, and a declaration of actual success. There, prices below some measure of cost for short periods; here, non-introductory, non-promotional prices below average variable cost for at least eighteen months. There, no entry barriers or persistent oligopoly with supracompetitive prices or other source of recoupment anticipated by defendants or otherwise; here, some $350 million of recoupment sources by defendant's own calculation. There, no evidence that deteriorating prices injured consumers; here, the relative price of the generic product rose and all prices rose more than costs or inflation. A7817-18, A6334-35, A6344-56.

1992-2 Trade Cas. (CCH) ¶ 69,929 (9th Cir. 1992), reveals a conflict in construing the Robinson-Patman Act. Although the plaintiffs ultimately lost for other reasons in those cases, both *A.A. Poultry* and *Inglis* were entirely ready to find a violation notwithstanding the absence of any monopoly or conspiracy. Moreover, in *USA Petroleum Co. v. Atlantic Richfield Co.*, 1992-2 Trade Cas. (CCH) ¶69, 928 (9th Cir. 1992) at 68,450, the Ninth Circuit held that proof of pricing below cost can establish predation without regard to any monopoly or conspiracy.[27]

If allowed to stand, the Fourth Circuit decision will create even greater confusion in this area of the law. In doubting the likelihood of predation in the absence of prospective recoupment, courts have spoken in terms of recoupment through post-predation monopoly -- because monopoly is the recoupment route apparent in most cases. *E.g., Henry v. Chloride, Inc.*, 809 F.2d 1334, 1345 (8th Cir. 1987); *O. Hommel Co. v. Ferro Corp.*, 659 F.2d 340, 348 (3d Cir. 1981), *cert. denied*, 455 U.S. 1017 (1982). Courts also have adopted a uniform price-cost test for presumptively illegitimate prices under both the Robinson-Patman and Sherman Acts. *Id.* These correct decisions when coupled with the Fourth Circuit's erroneous decision invite a complete coalescence of the two statutes contrary to the intent of Congress and sound antitrust policy.

Liggett does not ask this Court to side with those circuits emphasizing unjustified below-cost pricing alone. Here, the present jury found -- in accord with the instructions, evidence, and economic theory -- below-cost pricing with a prospect of recoupment through supracompetitive prices. Liggett asks this Court to resolve the conflict among the circuits as to the need for the prospect of recoupment under the Robinson-Patman Act and to recognize that recoupment can occur outside of a monopoly or

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[27] While the Ninth Circuit emphasized an alleged vertical conspiracy fixing maximum resale prices in *USA Petroleum*, that kind of conspiracy cannot aid recoupment when substantial interbrand competition remains both at the supplier and dealer level. The concept of predation was in issue notwithstanding an alleged *per se* violation under Sherman Act §1, because this Court had held that the particular plaintiff could not proceed without proving predation. *Atlantic Richfield Co. v. USA Petroleum Co.*, 459 U.S. 328 (1990).

conspiracy, depending upon the circumstances of the particular market.

Whether or not this Court chooses to retain the full force of *Utah Pie*, this case provides an important opportunity twenty-five years after its last decision in this area to define primary-line injury to competition in the light both of contemporary economic understanding and of a fully developed record. Here, a sophisticated oligopolist (1) expressly undertook to harm consumers by shrinking the price gap between generics and regular brands, (2) accomplished that result by disciplining an admitted price maverick through sustained pricing below average variable cost, (3) after expressly calculating that B&W's investment in such discipline would be recouped out of otherwise threatened $350 million of brand-name revenue in a concentrated market with long-continued supracompetitive prices and profits and without threat of new entry, and (4) after carefully analyzing the prospective behavior of fellow oligopolists and concluding that they would not interfere with the planned payoff. If this case does not create a reasonable possibility of injuring competition under the Robinson-Patman Act, then any oligopolist is legally free to discipline a price cutter through sustained discriminatory pricing below average variable cost.

e. *"Policy" should be debated, not hidden behind false economics*. Perhaps the Fourth Circuit's rule of *per se* legality in the absence of monopoly or a cartel could be defended as a bright line that sacrifices Liggett and the consumers hurt by B&W's predatory conduct. They would be sacrificed in order to avoid burdening the courts and the economy with ill-founded claims in other non-monopoly, non-conspiracy situations. However, such an important policy decision should be subject to explicit scrutiny of the pros and cons of limiting Robinson-Patman Act liability to the same coverage as the Sherman Act, and not be obscured by a holding that some notion of economic theory precludes the possibility of disciplinary price discrimination by oligopolists and does so as a matter of law.

2. *Requiring actual injury to consumers for a Robinson-Patman Act violation wrongly constrains that law and conflicts with other circuits*. The Fourth Circuit's view that consumers

were in fact unhurt (notwithstanding higher prices[28]) has legal significance only if actual injury to consumers is a prerequisite to the violation. Such a prerequisite would be wrong and conflict with other circuits. It would be contrary to the statute, which condemns discriminatory pricing where the effect "*may be* substantially to lessen competition..." (emphasis added). It would also be wrong in principle because protecting consumers justifies the condemnation of dangerous conduct even if such conduct is abandoned when it is legally challenged or it turns out to be unsuccessful because the predator miscalculated. A sophisticated actor's express intent to harm consumers and its actual harm to a rival through unambiguously improper conduct creates the "reasonable possibility" of injuring consumers forbidden by the statute and found by the jury in this case.

The Fourth Circuit's requirement of actual effects conflicts with other circuits. For example, the Second Circuit and the Fifth Circuit have ruled under the stricter standards of Sherman Act §2 that the legality of conduct is to be judged at the time it was undertaken in the light of market circumstances as they then were and as they appeared to the actors. *Kelco Disposal, Inc. v. Browning Ferris Industries, Inc.*, 845 F.2d 404, 406 (2d Cir. 1988) (falling market share did not immunize predatory pricing), *aff'd on other grounds*, 492 U.S. 257 (1989); *United States v. American Airlines, Inc.*, 743 F.2d 1114 (5th Cir. 1984), *cert. denied*, 474 U.S. 1001, 1119 (1985) ("it is no defense that the plan proved to be impossible to execute"). And the Eighth Circuit has recognized that "predatory intentions need not be accomplished" although there "must be some reasonable expectation on the part of the alleged predator that it will succeed." *Henry v. Chloride, Inc.*, 809 F.2d 1334, 1345 n.9 (8th Cir. 1987). This conflict deserves resolution.

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[28] The Fourth Circuit did not deny that the black-and-white discount below regular brands has declined, that the black-and-white segment has contracted, and that all cigarette prices have risen more than costs or inflation. That the generic sector (broadly defined) grew is fully consistent with the reasonableness of B & W's belief that it could benefit from higher prices, that it so benefited, or that its pricing had the desired disciplinary effect.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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September 15, 1992

APPENDIX
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UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

LIGGETT GROUP, INCORPORATED,
now named Brooke Group, Limited,

Plaintiff-Appellant,

v.

BROWN & WILLIAMSON TOBACCO
CORPORATION,

Defendant-Appellee,

and

GENERIC PRODUCTS CORPORATION,

Defendant.

Nos. 90-1851; 90-1854;
90-49 122

Appeals from the United States District Court
for the Middle District of North Carolina, at Durham.
Frank W. Bullock, Jr., District Judge.
(CA-84-617-D-C)

Argued: February 3, 1992

Decided: May 11, 1992

Before ERVIN, Chief Judge, and HALL and NIEMEYER,
Circuit Judges.

OPINION

NIEMEYER, Circuit Judge:

Liggett Group, Inc., charges Brown & Williamson Tobacco Corporation with pursuing a primary-line predatory pricing scheme in the sale of generic cigarettes during the period 1984-85 in violation of § 2(a) of the Robinson-Patman Act, 15 U.S.C. §13(a). Liggett contends that Brown & Williamson charged below-average-variable-cost prices[1] to force Liggett either to raise the prices of its generic cigarettes or to cease selling them, with the expectation of preserving high profits theretofore earned on sales of branded cigarettes by the industry-wide oligopoly.[2]

Following a 115-day trial, a jury returned a verdict in favor of Liggett in the amount of $49.6 million which the district court trebled for a judgment of $148.8 million. The district court, however, granted Brown & Williamson's motion for judgment notwithstanding the verdict, 748 F. Supp. 344 (M.D.N.C. 1990), and this appeal followed. We now affirm.

I

Cigarettes in the United States have been manufactured in recent years primarily by six companies, Philip Morris, Inc., R.J.

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[1] Variable costs are typically considered to be those costs incurred directly in the manufacture of a product, which vary with the number of units manufactured, such as the cost of materials used in the product, labor directly used in its manufacture, and per unit license fees. Variable costs are distinguished from fixed costs that remain constant regardless of the number of units produced. The average variable cost of a product is the sum of all variable costs divided by the number of units produced. *See* Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices under Section 2 of the Sherman Act*, 88 Harv. L. Rev. 697, 700 (1975).

[2] Whereas a monopoly is the control of a market by one seller, an oligopoly is a market condition that results when there are but a few sellers.

Reynolds Tobacco Corporation, Brown & Williamson, Lorillard, Inc., American Tobacco Company, and Liggett. Philip Morris and R.J. Reynolds, with respectively over 40% and 28% of the market at the time of trial, held the two largest market shares throughout the 1980's. During the relevant period Brown & Williamson's sales never represented more than 12% of the market. Prior to 1980, cigarettes were sold by these companies to distributors at the same price, and when one company increased the price, the others followed. Liggett has characterized this market as "one of the most highly concentrated oligopolies in the United States," which has produced what Liggett's economist has characterized as "supracompetitive profits."[3]

In 1980 when Liggett's share of the cigarette market in the United States had declined to 2.3%, a level that threatened its viability, it introduced a line of generic cigarettes in black and white packaging. Liggett discounted these generic cigarettes and offered volume rebates to yield an effective price to distributors about 30% lower than that charged for branded cigarettes. By 1984 Liggett's share of the total cigarette market in the United States increased to over 5% and its generics became the fastest growing segment of the market, in which overall sales of cigarettes were declining.

Other manufacturers began responding in 1983. In July of that year, R.J. Reynolds introduced "Century" cigarettes. It sold this brand in cartons of nine packs containing 25 cigarettes each, for the same price as other branded cigarettes sold in cartons of 10 packs containing 20 cigarettes each. These "25s" thus cost consumers 12.5% less than other brands. Brown & Williamson followed suit later that year with "Richland," its own brand of 25s.

Nonetheless, in the 1983-84 period, Brown & Williamson began to observe that it was losing more sales to generic cigarettes, proportionally, than were other manufacturers, and that

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[3] Profits are supracompetitive when they are unrestrained by competition.

it sustained a "variable margin loss"[4] of over $50 million in 1983 alone. It concluded that "unchallenged, [Liggett] could continue its total dominance of this segment..., becoming the third largest company in the U.S. cigarette market." A Brown & Williamson memorandum introduced at trial stated about the Liggett activity:

> Stipulating 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. Competitive counter-actions are essential and inevitable.

After examining each company's capacity and expected response to Liggett's introduction of generic cigarettes, Brown & Williamson determined to enter the generic segment to recapture the sales lost to Liggett. It described the opportunity as follows:

> Generics represent B&W's most immediate opportunity to increase volume. This volume can be achieved within current manufacturing capacity, without incremental manpower and without negatively impacting trading profit. No other option offers similar potential to recover lost volume/share with such minimal investment risk. This is true because our goal is to capture existing demand[,] not create new consumer demand.

The same market memorandum revealed a pricing strategy that was intended to produce "a full variable margin" in excess of $4 per thousand cigarettes. But it went on to state:

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[4] In its internal memoranda Brown & Williamson used "variable margin" to mean the difference between sales revenue and direct manufacturing costs (or variable costs).

> B&W is prepared to spend up to net variable margin as a first step response to competitive counter-offers; if required, we are also prepared to go up to, but *not* beyond, full variable margin to gain entry into the generics market.
>
> * * *
>
> If [Liggett] goes below full variable margin, Brown & Williamson would not plan to match their offer.

In May 1984, before Brown & Williamson implemented its plan, R.J. Reynolds "repositioned" its brand "Doral," cutting the list price to that charged by Liggett for its generic cigarettes. Brown & Williamson reanalyzed its strategy in light of the Doral move, concluding in the final strategic memorandum,

> B&W believes that branded generics will enhance the growth of the economy segment and will draw volume from popular priced brands.
>
> * * *
>
> The earlier concern of expanding the economy segment is no longer tenable, given RJR's recent action. It is clear that the economy segment is significant, and growing. Accordingly, recognizing the importance of minimizing increased cannibalization and concomitant share erosion, as well as maintaining trading profit targets, it is imperative that B&W enter this segment.

Shortly thereafter, in July 1984, Brown & Williamson introduced its line of generic cigarettes in black and white packages to compete directly with Liggett's black and white packaged generics. Liggett responded immediately with this lawsuit alleging initially that Brown & Williamson violated the trademark laws. The complaint was amended to add the Robinson-Patman claims that are the subject of this appeal. Liggett also responded by increasing rebates and other incentives to its distributors. During the rest of the summer, the two manufacturers traded moves and counter-moves four more times in setting prices, offering rebates, and otherwise promoting black and white generic cigarettes. The incentive schemes established when the dust settled in August remained in force until June 1985, when Liggett raised its list price for generics. Brown & Williamson matched the rise in October of that year.

By 1988 all other market participants, except for Lorillard, were selling generics and discounted branded cigarettes, and both R.J. Reynolds and Philip Morris added a black and white generic line. By the time of trial, Lorillard too was in that segment of the market. With the exception of an aborted attempt by Brown & Williamson in December of 1985, no manufacturer raised the price of black and white cigarettes until the summer of 1986. Since then, generic cigarette prices have risen twice a year, in tandem with those of branded cigarettes, reducing the proportional price discount between branded and generic cigarettes from a high of 40% in 1985 to 27% in 1989.

While the United States market for cigarettes has been generally declining, the growth of discounted cigarettes has been dramatic. In 1981 Liggett, which held 97% of the generic sales, sold 2.8 billion cigarettes, representing .4% of the United States cigarette market. By 1988 it sold over 9 billion generic cigarettes. The total sales of generic and discounted cigarettes during the same period increased from 2.8 billion cigarettes to 61.6 billion, representing 11.1% of the entire United States cigarette market. By trial all manufacturers were selling generics and discounted cigarettes, and yearly sales had reached nearly 80 billion cigarettes, representing 15% of the United States cigarette market. The percentage of the market represented strictly by black and white generics peaked in 1985 with 4.7% and was continuing to decline at the time of trial.

No one denies that after Brown & Williamson introduced its black and white generic cigarettes in 1984, the companies fought "tooth and nail" and that the market "got very competitive." Liggett's president confirmed that "competition had substantially increased in the total cigarette market." When all was said and done, Liggett ended up with 3.25% of the market for cigarettes in the United States and Brown & Williamson with 11.36%.

Liggett contends that from June 1984 to the end of 1985, Brown & Williamson sold black and white cigarettes at prices below its "average variable cost," although it acknowledges that Brown & Williamson realized profits in the overall sale of cigarettes in the United States, the agreed upon relevant market. Its Robinson-Patmen Act claim focuses on Brown & Williamson's pricing activity for that period, which it contends was predatory, designed to force Liggett to raise its prices for generic cigarettes and thereby to destroy or limit the generic cigarette segment.

After a 115-day trial, the jury returned a verdict in favor of Liggett on its Robinson-Patman Act claim in the amount of $49.6 million, which the district court trebled under 15 U.S.C. §15 for judgment of $148.8 million. On Brown & Williamson's motion for judgment notwithstanding the verdict, the district court, after thoroughly analyzing the wide range of issues presented, set aside the judgment and entered judgment in favor of Brown & Williamson.

II

Section 2(a) of the Robinson-Patman Act makes it unlawful for a person engaged in commerce "to discriminate in price between different purchasers of commodities of like grade and quality...where the effect of such discrimination may be substantially to lessen competition...or to injure, destroy, or prevent competition" with the person charging the discriminatory prices. 15 U.S.C. §13(a). The requirement to show that the effect of pricing "may be substantially to lessen competition" may be satisfied by proof of predatory pricing.[5]

Liggett contends that this case is unusual because Brown & Williamson's intent to destroy competition from Liggett's sales of generic cigarettes is so clearly stated in corporate memoranda that, when coupled with evidence that its pricing plan in fact caused

[5] While predatory pricing generally refers to loss-producing pricing pursued to harm competition and later to realize monopoly profits, as is discussed more fully below, its precise definition for application of the antitrust laws is unsettled.

injury to Liggett, liability is established. It relies on *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685 (1967).

While *Utah Pie* is difficult to understand in light of recent economic theory and has been the subject of some criticism over the years, *see, e.g.*, *A. A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1404 (7th Cir. 1989), *cert. denied*, 494 U.S. 1019 (1990), we are confident that it does not require reversal in this case. In *Utah Pie*, national competitors, using economic muscle from sales in markets other than Salt Lake City, had subsidized below-cost pricing in the Salt Lake City area. The Supreme Court concluded, contrary to the court of appeals, that the plaintiff had adduced sufficient evidence for a jury to infer the requisite possibility of injury to competition, observing that "there was some evidence of predatory intent with respect to each [defendant]" and of a "drastically declining price structure." 386 U.S. at 702-03. The Court did not, however, purport to discuss in detail what evidence was sufficient to infer predatory intent, noting only, "[A]lthough the evidence in this regard against [one defendant who used industrial espionage against the plaintiff] seems obvious, a jury would be free to ascertain a seller's intent from surrounding economic circumstances, which would include persistent unprofitable sales below cost and drastic price cuts themselves discriminatory." *Id.* at 696 n.12. We understand *Utah Pie* to have left for later cases a statement of what more precisely constitutes predatory pricing.

Since *Utah Pie*, the Supreme Court has confirmed that "a firm cannot claim antitrust injury from nonpredatory price competition on the asserted ground that it is 'ruinous.'" *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 338 n.7 (1990). "[N]onpredatory price competition for increased market share, as reflected by prices that are below 'market price' or even below the costs of a firm's rivals, 'is not activity forbidden by the antitrust laws.'" *Id.* at 340 (quoting *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104, 116 (1986)). However, the line between legitimate competitive pricing, encouraged by the policy of free market competition, and predatory pricing, that is destructive of competition, is murky, and agreement on the distinction has not been reached. See *Cargill*, 479 U.S. at 117 n.12. While pricing "below some appropriate measure of cost" must be shown to establish it as predatory, see *Matsushita Elec.*

Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 585 n.8 (1986), questions remain about the definition of "below-cost" pricing. *See Atlantic Richfield*, 495 U.S. at 341 n.10, *Cargill*, 479 U.S. at 117 & n.12. It is sufficient for this case, however, to observe that predatory pricing must involve, in addition to some level of below-cost pricing that is harmful to competition, the rational expectation of later realizing monopoly profits. The failure to show this additional aspect is fatal. Thus 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. *See Matsushita*, 475 U.S. at 597-98. The Court explained,

> A predatory pricing conspiracy is by nature speculative. Any agreement to price below the competitive level requires the conspirators to forego profits that free competition would offer them. The foregone profits may be considered an investment in the future. For the investment to be rational, the conspirators must have reasonable expectation of recovering, in the form of later monopoly profits, more than the losses suffered....The success of any predatory scheme depends *on maintaining monopoly power for long enough both to recoup the predator's losses and to harvest some additional gain.*
>
> * * *
>
> These observations apply even to predatory pricing by a single firm seeking monopoly power.

Id. at 588-89, 590 (emphasis changed). See also Areeda and Turner, *supra* note 1, at 698 ("[P]redation in any meaningful sense cannot exist unless there is a temporary sacrifice of net revenues in the expectation of greater future gains.").

Turning to this case, Liggett has not advanced a theory that Brown & Williamson could ever obtain or maintain monopoly power for any period of time, much less a period sufficient to reap the harvest of its alleged below-cost pricing, since Brown & Williamson never had more than 12% of the agreed-upon market. Liggett's theory rests on the notion that following the fight in which Brown & Williamson would effectively contain or destroy the generic segment, Brown & Williamson and the other four manufacturers with successful branded cigarettes would, as an oligopoly, reap profits which Liggett predicts would be restored to a "supracompetitive" level.

On the basis of the testimony of its economic expert, William Burnett, Liggett contends that for years the cigarette market in the United States had been an oligopoly. Pointing to historical price increases, it observes that the six members raised prices in lockstep regardless of the amount of increases or even decreases in the cost of tobacco, and without the entry of any significant new competitor in several decades. When Liggett, in 1980, began offering generic cigarettes at prices 30% below those of branded cigarettes, purchasers switched from branded cigarettes to the generic cigarettes offered by Liggett, thereby denying to members of the oligopoly the assertedly supracompetitive prices they had previously enjoyed. Liggett argues that in response to Liggett's success Brown & Williamson developed and implemented a detailed, two-pronged counterattack to contain expansion of or destroy the generic segment. As outlined by Burnett, on the one hand Brown & Williamson removed any disincentive for distributors of generic cigarettes to switch entirely from Liggett to Brown & Williamson by offering their generic cigarettes in a black and white package which consumers would confuse with Liggett's. On the other hand, to lure these distributors away, Brown & Williamson directed discriminatory rebates at Liggett's highest-volume customers, structured to encourage them to pocket the rebates rather than pass them on as price cuts to consumers. Because consumers would not see two competing generic cigarettes or lower prices, consumer demand for generics would not increase and thereby cut further into sales of branded cigarettes. The higher cost of access to its distributors, however, would force Liggett either to raise its overall income by raising list prices to consumers, or to cease selling generic black and white cigarettes entirely.

In either case, asserted Burnett, Brown & Williamson would recoup its losses and make additional gains from the increased sales of its branded cigarettes at the supracompetitive prices established by the historical parallel pricing in the oligopolistic market. According to Burnett, the other members of the oligopoly would not intercede, because they would similarly benefit from decreased "cannibalization" of the sales of their own branded cigarettes.

Shorn of its details, Liggett's theory depicts Brown & Williamson as an oligopolist attempting to discipline another oligopolist for breaking a pattern of parallel pricing, by driving up the offender's costs using finely-tuned predatory pricing of its own. The theory relies upon an expectation that all the other oligopolists would, out of their self-interests, simply stand by and refrain from also selling generics or other low-cost products which would eat into sales of branded cigarettes. Absent such assurance, Brown & Williamson might well drive Liggett out or its prices up, but continue to lose sales of its more profitable branded cigarettes to cannibalistic sales of generics by the other oligopolists. There is no evidence, however, of any conspiratorial agreement among the oligopolists to stay their hands. Liggett's theory therefore amounts to substituting the conscious parallelism of an oligopoly for conspiratorial agreement or actual monopoly power as the reason Brown & Williamson might rationally expect to be able to recoup its investment in disciplining Liggett.

We are aware of no case in which the predicted economic behavior of an oligopoly was relied on to provide a rational means of recoupment of the losses sustained in a predatory pricing scheme, and economic logic as well as actual experience in this case belie such a holding. 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. One would conclude, however, that this shared interest would not itself be enough to convince a rational oligopolist facing losses of market share to a competitor's price-cut not to match the cut with its own grab for market share. 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.

The facts in this case remove any doubt that no rational oligopolist would be confident that neither Brown & Williamson nor any of the other manufacturers would expand its own sales of low-priced cigarettes at the expense of full-priced branded cigarettes. Brown & Williamson may have intended its disciplinary actions not to affect consumer prices, but outside observers might well not have recognized this plan in the complex and furious rebate war which ensued in the summer of 1984. More importantly, however, Brown & Williamson had already expanded its sales of low-priced cigarettes, when it introduced in 1983 its brand "Richland" at an effective discount of 12.5% to consumers, and R.J. Reynolds, of course, had done the same, first with "Century" and later when it cut the price of its brand "Doral" to the same level as Liggett's generic black and white cigarettes.

Any rational observer would have known that sales of Richland, Century, and Doral would most likely further erode the sales of full-priced branded cigarettes, regardless of Brown & Williamson's success in disciplining Liggett for introducing generic black and while cigarettes. But we need not merely impute rationality to Brown & Williamson. The very memoranda upon which Liggett relies so heavily as evidence of Brown & Williamson's predatory intent not only predict similar actions as occurred, but conclude after the introduction of Doral that "[t]he earlier concern of expanding the economy segment is no longer tenable...."

The perfect vision of hindsight confirms Brown & Williamson's conclusion and our theoretical suspicions. Soon after the events of 1984, most cigarette manufacturers were offering various types of low-priced cigarettes, including generics, and by trial all were vigorously competing with differing devices and approaches. Sales of low-priced cigarettes increased from 2.8 billion cigarettes in 1981 to nearly 80 billion in 1989. Their proportional share of the overall cigarette market in the United States grew from .4% to 15%.

In the end, Liggett asked the jury to leap from the fact that the cigarette market is a concentrated oligopoly with a history of parallel pricing to the conclusion that the oligopoly would act uncompetitively when one of its members made a competitive move, suggesting some perniciousness in the oligopoly itself. Yet, in the absence of an agreement among the oligopolists, which nobody contends is the fact in this case, membership alone in an oligopoly provides no basis for proof of illegal conduct. Thus no case suggests that mere participation in an oligopolistic market constitutes conduct illegal under the antitrust laws. As the court stated in *E.I. duPont de Nemours & Co. v. Federal Trade Commission*, 729 F.2d 128, 139 (2d Cir. 1984):

> The mere existence of an oligopolistic market structure in which a small group of manufacturers engage in consciously parallel pricing of an identical product does not violate the antitrust laws. *Theater Enterprises, Inc. v. Paramount Film Distributing Corp.*, [346 U.S. 537, (1954)]. It represents a condition, not a "method;" indeed it could be consistent with intense competition.

While the parallel but not agreed upon conduct of an oligopoly may be a characteristic of a mature market, as we noted above, such parallelism cannot rationally be assured when an act of competition is undertaken by one participating member. To rely on the characteristics of an oligopoly to assure recoupment of losses from a predatory pricing scheme after one oligopolist has made a competitive move is thus economically irrational. As the Supreme Court pointed out six years ago, "'the predator must make a substantial investment with no assurance that it will pay off.' For this reason, there is consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful." *Matsushita*, 475 U.S. at 589, (quoting Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. Chi. L. Rev. 263, 268 (1981)).

In short, Brown & Williamson controlled only 12% of the relevant market and could not be assured, when it began its alleged below-cost pricing to suppress competition from Liggett, that the other manufacturers would not also respond competitively. Consequently, the pricing policies undertaken by Brown & Williamson, while perhaps intended to injure Liggett, could not be found to be predatory because they did not provide an economically rational basis "to recoup...losses and to harvest some additional gain." Because we conclude that Liggett is unable to demonstrate that it satisfied an essential element of proving a primary-line pricing scheme in violation of the Robinson-Patman Act, we need not reach the other questions decided by the district court. The judgment of the district court is affirmed.

AFFIRMED

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

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

Plaintiff - Appellant,

v.

BROWN & WILLIAMSON TOBACCO
CORPORATION,

Defendant - Appellee,

and

GENERIC PRODUCTS CORPORATION

Defendant.

June 18, 1992
On Petition for Rehearing with
Suggestion for Rehearing In Banc

The appellant filed a petition for rehearing with suggestion for rehearing in banc. No member of the Court requested a poll on the suggestion for rehearing in banc, and the original judicial panel voted to deny the petition for rehearing.

The Court denies the petition for rehearing with suggestion for rehearing in banc.

Entered at the direction of Judge Niemeyer, with the concurrence of Chief Judge Ervin and Judge Hall.

For the Court,

/s/ Bert M. Montague

Clerk

LIGGETT GROUP, INC., Plaintiff,

v.

BROWN & WILLIAMSON TOBACCO CORPORATION, Defendant.

Civ. No. C-84-617-D.

United States District Court,
M.D. North Carolina,
Durham Division

Aug. 27, 1990

MEMORANDUM OPINION

BULLOCK, District Judge

Liggett Group, Inc., ("Liggett") brought this private antitrust suit to recover treble damages against Brown & Williamson Tobacco Corporation ("B&W") alleging predatory price discrimination in violation of Section 2(a) of the Clayton Act, as amended by the Robinson-Patman Act, 15 U.S.C. § 13(a).[1] Liggett also charged that B&W violated the unfair

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[1] The Robinson-Patman Act states in pertinent part:

> It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimination are in commerce, . . . and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such

competition section of the Lanham Trade-Mark Act, 15 U.S.C. § 1125(a),[2] as well as various state common law and statutory unfair trade Practices.[3]

After a lengthy trial,[4] the jury returned a verdict in favor

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discrimination, or with customers of either of them.

[2] Section 1125(a) states in relevant part:

> Any person who shall affix, apply, or annex, or use in connection with any goods or services, or any container or containers for goods, a false designation of origin, or any false description or representation, including words or other symbols tending falsely to describe to represent the same, and shall cause such goods or services to enter into commerce, and any person who shall with knowledge of the falsity of such designation of origin or description or representation cause or procure the same to be transported or used in commerce or deliver the same to any carrier to be transported or used, shall be liable to a civil action by any person doing business in the locality falsely indicated as that of origin or in the region in which said locality is situated, or by any person who believes that he is or is likely to be damaged by the use of any such false description or representation.

[3] Liggett's complaint alleges a statutory claim under the North Carolina unfair trade practices statute, N.C. Gen.Stat. § 75-1 *et seq.*, and state common law claims under the North Carolina Common law of trademarks and the North Carolina common law of unfair competition. All these claims stem from B&W's alleged infringement of Liggett's quality seal ("Q-seal") closure by B&W's oval closure seal.

[4] The jury heard evidence and arguments for 115 days, and considered 2,884 exhibits, 85 deposition excerpts, and testimony from 23 live witnesses. The verdict was returned after nine days of deliberations. The court's instructions to the jury on the antitrust claim were generally consistent with the legal position and theory espoused by Liggett. Some of the same issues and contentions had been considered by the court at summary judgment and/or the directed verdict stage of the trial, and resolved in Liggett's favor. In a complex case such as this, however, development of a complete record is sometimes necessary in order for the

of Liggett on the Robinson-Patman Act claim in the amount of $49,600,000.00. When trebled pursuant to 15 U.S.C. § 15(a), Liggett's award totals $148,800,000.00, excluding post-judgment interest and attorneys' fees. The jury found that Brown & Williamson was not liable to Liggett on the trademark unfair competition claims.

B&W has moved for judgment notwithstanding the verdict (JNOV) under Federal Rule of Civil Procedure 50(b) and, alternatively, for a new trial under Federal of Civil Procedure 59 on the antitrust portion of the case.[5] Liggett has moved for a new trial under Federal Rule of Civil Procedure 59 on its trademark and unfair competition claims. After careful consideration, the court will set aside the antitrust verdict and grant B&W's motion for judgment notwithstanding the verdict. The court will deny B&W's alternative motion for a new trial.[6] Liggett's motion for

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court to have a thorough understanding of the issues and facts in controversy. An ever expanding court docket does not always provide an atmosphere conducive to pre-trial analysis of complex economic and legal issues.

[5] A different standard applies to a JNOV motion pursuant to Fed. R.Civ.P. 50(b). *see infra* p. 341, than to a motion for a new trial pursuant to Fed.R.Civ.P. 59, *see infra* p. 355.

[6] A court may in its discretion grant a JNOV motion and deny an alternative motion for a new trial. *See* Fed.R.Civ.P. 50(c)(1); *Stone v. First Wyoming Bank*, 625 F.2d 332, 349-50 (10th Cir. 1980); *Reagin v. Terry*, 675 F.Supp. 297, 304-05 (M.D.N.C. 1986), *aff'd* 829 F.2d 36 (4th Cir.1987). The court's JNOV rulings on competitive injury, causation, and antitrust injury are based upon interpretations of the applicable law. If these interpretations are found to be erroneous and an appellate court applies legal standards more favorable to Liggett, this court does not believe that an examination of the weight of the evidence, the credibility of witnesses and any alleged errors in the admission or rejection of evidence or instructions to the jury would justify granting B&W a new trial. The only remaining significant issue concerns the sufficiency of Ligget's damage evidence. If antitrust injury is proven, courts are lenient in assessing the proof required to support a damage award. *See Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 265-66

a new trial on the trademark and unfair competition claims will be denied.

I. FACTS

The cigarette industry in the United States during the mid-1980's provides the setting for this dispute. Six major manufacturers form this industry.[7] Phillip Morris and R.J. Reynolds Tobacco Corp. ("RJR") are the industry giants. The other cigarette manufacturers hold substantially smaller market shares. Liggett and B&W compete for wholesale and retail customers across the United States. Both companies sell branded[8] and generic[9] cigarettes. At year-end 1985, B&W's total cigarette

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S.Ct. 574, 580-81, 90 L.Ed. 652 (1946); *Story Parchment Co. v. Patterson Parchment Paper Co.*, 282 U.S. 555, 563-64, 51 S.Ct. 248, 250-51, 75 L.Ed. 544 (1931). Liggett presented two damage theories and extensive evidence from the testimony of two experts and other witnesses. The court believes there was sufficient evidence to support the jury's damage award.

[7] The six major cigarette manufacturers are Phillip Morris, Inc., R.J. Reynolds Tobacco Corp., B & W, Lorillard, Inc., American Tobacco Co., and Liggett. A few other domestic and foreign firms have sold cigarettes in the United States during the 1980's, but none has attained any significance in the marketplace.

[8] The term "branded cigarettes" describes full-price cigarettes targeted to the image-conscious cigarette consumer. Branded cigarettes are advertised heavily and packaged in containers with distinctive designs. Well-known branded cigarettes include Newport, Pall Mall, Kool, Winston, and, of course, Marlboro -- America's most popular branded cigarette by a wide margin.

[9] The term "generic cigarettes" refers to a catch-all category of cigarettes priced significantly lower than branded cigarettes. Within this category, sometimes called the price-value category, there are different types of generic cigarettes. This dispute centers around one such type -- black and white cigarettes. Black and white cigarettes are sold in plain-looking white packages with black lettering indicating the nature of the product contained within (*e.g.*, "Filter Cigarettes"). These packages look

sales in the United States were about double Liggett's, although Liggett still sold more generic cigarettes than B&W.

The market shares of both companies have declined in recent years. Since 1975 when its market share was nearly seventeen percent (17%), B&W's sales have steadily declined. Liggett has had even less success. Years ago, Liggett was a major force in the cigarette industry, enjoying market shares exceeding twenty per cent (20%). However, Liggett's sales declined precipitously for many years. By 1980, Liggett's market share stood at 2.33%, and the company was close to going out of business. Out of desperation, Liggett became the first major cigarette manufacturer to sell generic cigarettes.[10] Liggett encouraged its customers to buy large quantities of generic cigarettes by offering volume rebates so that the more a customer bought the less the customer paid on a per carton basis.

Generic cigarettes were an unqualified success for Liggett. The segment grew steadily, and by mid-1984 generic sales accounted for 4.1% of the total United States cigarette business with Liggett holding ninety-seven percent (97%) of the segment. The popularity of generic cigarettes attracted other major cigarette manufacturers. In 1983, both RJR and B&W introduced "25's" in response to the success of generic cigarettes.[11] In May 1984,

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like other generic products on the grocery shelf so that consumers can quickly identify them as lower-priced cigarettes. Another category of generic cigarette is "branded generics." Branded generics are cigarettes in branded packaging but priced in the black and white cigarette range.

[10] Liggett was not the first cigarette company to sell generic cigarettes. Both U.S. Tobacco Co. and G.A. George Georgopulo & Co., smaller cigarette manufacturers with no significant market share, sold generic cigarettes prior to Liggett. However, once Liggett entered the generic category it became the dominant player and was responsible for the segment's initial growth.

[11] "Twenty-five's" ("25's") are cigarettes priced and packaged like branded cigarettes but with twenty-five cigarettes contained in each package instead of the standard twenty. RJR introduced Century and B&W introduced Richland as entries in the "25's" category.

RJR also introduced "branded generics."[12] Later that month, B&W announced it would start selling black and white cigarettes positioned to compete directly with Liggett. B&W offered prospective customers volume rebates similar to Liggett's, only higher. Liggett responded by increasing its volume rebates. The rebate war between the companies continued for several more rounds. When the dust settled, B&W's published volume rebates were greater than Liggett's published volume rebates.[13] This rebate activity took place before B&W began selling generic cigarettes in July 1984, giving rise to this lawsuit in which Liggett alleges that, until the end of 1985, B&W engaged in a predatory pricing campaign designed to "kill" the generic cigarette category.

Today generic cigarettes are a fixture in the cigarette market. Five of the six major cigarette companies have significant entries in the category[14] and growth has been steady. The growth of generic cigarettes has encouraged additional

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[12] RJR repositioned Doral, a brand which had previously been unsuccessful competing with other branded cigarettes, by lowering the price to generic levels. Since May 1984, Doral's market share has grown considerably.

[13] B&W's published volume rebates from mid-1984 to the end of 1985 ranged from sixty to eighty cents per carton depending on the number of cartons a customer brought from the company. B&W's rebate schedule on a per carton basis was as follows: 60¢ rebate for customers who bought 0-499 cases per quarter; 65¢ rebate for customers who bought 500-999 cases per quarter; 70 ¢rebate for customers who bought 1,000-1,499 cases per quarter; 75¢ rebate for customers who bought 1,500-7,999 cases per quarter; and 80¢ rebate for customers who bought 8,000 or more cases per quarter.

[14] Lorillard is the only major cigarette manufacturer without a significant presence in the generic cigarette segment.

competition, primarily in the form of couponing and stickering,[15] on branded cigarettes.

II. THE ANTITRUST ISSUES

B & W's JNOV motion may be granted only if, taking all the evidence in the light most favorable to Liggett, there is no substantial evidence to support the jury's verdict. *Evington v. Forbes*, 742 F.2d 834, 835 (4th Cir.1984). Evidence is substantial if it is "of such quality and weight that reasonable and fair-minded men in the exercise of impartial judgment could reasonably return a verdict for the nonmoving party." *Wyatt v. Interstate & Ocean Transp. Co.*, 623 F.2d 888, 891 (4th Cir.1980). However, a mere scintilla of evidence is insufficient to sustain a verdict. *Austin v. Torrington Co.*, 810 F.2d 416, 420 (4th Cir.), *cert. denied*, 484 U.S. 977, 108 S.Ct. 489, 98 L.Ed.2d 487 (1987). Therefore, in order to warrant JNOV, B & W must show that Liggett has failed to prove an essential element of its claim.

Liggett's antitrust claim is a private, primary-line,[16] non-geographic[17] Robinson-Patman Act suit. Except for the issue of

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[15] Coupons are a form of price competition in which money-off vouchers on cigarette cartons and packs are distributed to consumers through newspapers and other mediums. Stickering is a form of price competition in which money-off stickers are attached to cigarette cartons, and sometimes even individual packs. Although the list price of couponed and stickered cigarettes does not change, the amount of money the consumer has to pay at the cash register is lessened by the value of the coupon or sticker.

[16] In Robinson-Patman Act cases, courts distinguish the probable impact of the price discrimination upon competitors of the seller (primary-line injury), the favored and disfavored buyers (secondary-line injury), or the customers of either of them (tertiary-line injury). *See* 3 E. Kintner & J. Bauer, *Federal Antitrust Law* § 20.9, at 127 (1983).

[17] Non-geographic means that the United States is the relevant market as opposed to any particular city, state, or region.

price discrimination, the jurisdictional elements are undisputed.[18] Despite the connotations of the term "discrimination," there is nothing illegal *per se* about a company discriminating in price. Price discrimination means price difference and nothing more. *See Texaco Inc. v. Hasbrouck*, ___ U.S. ____, 110 S.Ct. 2535, 2544, 110 L.Ed.2d 492 (1990). B & W discriminated in price by charging different net prices[19] to different purchasers via volume rebates in actual black and white cigarette transactions. The other elements[20] --competitive injury, causation, and antitrust injury-- have been vigorously contested throughout the entire litigation. The court believes that Liggett's evidence falls short in each of these categories.

A. *Competitive Injury*

The Robinson-Patman Act prohibits only price discrimination the effect of which "may be substantially to lessen competition." 15 U.S.C. § 13(a). This statutory language has been interpreted to proscribe only that price discrimination which has a reasonable possibility[21] of injuring competition in the

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[18] The parties do not dispute that at least one of the sales of B & W black and white cigarettes was made across a state line; that each pertinent sale of B & W black and white cigarettes was for use and resale in the United States; that the black and white cigarettes sold by B & W were physical items; that the black and white cigarette sales being compared were made by B & W at about the same time; and that the B & W black and white cigarettes involved in the sales being compared were of like grade and quality.

[19] Net price equals list price minus all discounts to the customer.

[20] Antitrust injury is a requirement in all antitrust actions for monetary damages brought by private parties. 15 U.S.C. § 15(a). The other elements of Liggett's claim are part of the Robinson-Patman Act. 15 U.S.C. § 13(a).

[21] A few courts have used a reasonable probability of injuring competition standard instead of reasonable possibility. *See, e.g., Holleb & Co. v. Produce Terminal Cold Storage Co.*, 532 F.2d 29, 35 (7th Cir.1976). This is a distinction of form over substance. *See*

relevant market. *Falls City Indus., Inc. v. Vanco Beverage, Inc.*, 460 U.S. 428, 434-35, 103 S.Ct. 1282, 1288-89, 75 L.Ed.2d 174 (1983). Prior to trial, the parties stipulated that the relevant market in which to examine competitive injury was the entire United States cigarette market. Therefore, Liggett must prove that B & W's price discrimination in the sale of its black and white cigarettes had a reasonable possibility of injuring competition in the United States cigarette market as a whole.

The competitive injury requirement of the Robinson-Patman Act in the context of this primary-line, non-geographic claim is not fundamentally different from an attempted monopolization claim under Section 2 of the Sherman Act. 15 U.S.C. § 2. Of course, the standards to evaluate competitive injury are different. The Robinson-Patman Act requires a showing of reasonable possibility of injury to competition while the Sherman Act requires a dangerous probability that the attempt to monopolize will be successful. *See Indiana Grocery, Inc. v. Super Value Stores, Inc.*, 864 F.2d 1409, 1413 (7th Cir.1989). However, this difference affects only the quantum of proof needed to satisfy the respective statute's competitive injury requirements and not the type of evidence which furnishes that proof.[22] In the present case, the

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International Air Indus., Inc. v. American Excelsior Co., 517 F.2d 714, 729 (5th Cir. 1975) ("any difference between the two formulations is trivial"), *cert. denied*, 424 U.S. 943, 96 S.Ct. 1411, 47 L.Ed.2d 349 (1976). The Supreme Court in at least one case has used these standards interchangeably. *See Corn Prods. Refining Co. v. FTC*, 324 U.S. 726, 739, 742, 65 S.Ct. 961, 967-68, 969-70, 89 L.Ed. 1320 (1945).

[22] A noted authority explained the parallel competitive injury requirements of the two statutes this way:

> Once a price is shown to be below the relevant costs its effect may be substantially to lessen competition, and it is condemned precisely because it has the potential to destroy competition and, if continued, the dangerous probability of doing so. If the price does not violate the relevant predatory pricing standard, it cannot tend to lessen competition or to have the dangerous probability of doing so.

court believes that such evidence must consist of predatory pricing practices indicating a reasonable possibility of injury to competition and consumer welfare rather than evidence merely of injury to a competitor combined with bad intent. Absent some objective economic ability to injure competition conduct cannot be illegal no matter what the intent. *See Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588-93, 106 S.Ct. 1348, 1356-59, 89 L.Ed.2d 538 (1986); *Henry v. Chloride, Inc.*, 809 F.2d 1334, 1344-45 (8th Cir.1987).

Liggett fundamentally disagreed with this position at trial and argued numerous times, citing *Utah Pie Co. v. Continental Baking Co.*, 386 U.S. 685, 87 S.Ct. 1326, 18 L.Ed.2d 406 (1967), that some showing of injury to a competitor combined with bad intent satisfied the Robinson-Patman Act's competitive injury requirement. This court rejects that position in the context of Liggett's atypical primary-line, non-geographic Robinson-Patman Act claim.

The typical primary-line Robinson-Patman Act case is much different from this one, pitting a small business with a limited product-line which competes only in a single geographic region against a large national manufacturer using predatory pricing tactics to displace the local competitor. *Utah Pie* is just such a case. In *Utah Pie*, several national manufacturers of frozen dessert pies challenged a small, family-operated dessert manufacturer which sold pies in the Salt Lake City area. The national manufacturers' strategy was to lower prices below cost on dessert pies in Salt Lake City, 386 U.S. at 696-97 & n. 12, 698, 701, 87 S.Ct. at 1332-33 & n. 12, 1333 , 1335, and run the local competitor out of business. The national manufacturers could afford to do this due to profits obtained on the sale of dessert pies in other areas of the country. The local competitor could sell dessert pies only in Salt Lake City and was faced with the bleak prospect of either lowering prices to unprofitable levels or eventually losing its sales to the low-priced pies. It was in this factual setting that the Supreme Court last addressed the requirements of a primary-line Robinson-Patman Act claim.

P. Areeda & H. Hovenkamp, *Antitrust Law* 270, at 618 (Supp. 1989).

Liggett's situation is much different. Liggett, as a national manufacturer of branded and generic cigarettes, is free to compete with B & W in any area of the country over any line of cigarette products and in fact does so. It faces none of the competitive constraints of the local business in *Utah Pie*.[23] In primary-line, non-geographic, predatory pricing cases the Robinson-Patman Act's competitive injury analysis more closely mirrors Section 2 of the Sherman Act than *Utah Pie*. Whether brought under the Sherman Act or the Robinson-Patman Act, predatory pricing is predatory pricing.[24] After all, price cutting is the essence of any predatory pricing campaign and, as the Supreme Court has warned, "mistaken inferences in cases such as this one are especially costly, because they chill the very conduct the antitrust laws are designed to protect." *Matsushita*, 475 U.S. at 594, 106 S.Ct. at 1360. Although the Fourth Circuit has not addressed this issue, many other circuits have held that the competitive injury analysis in a predatory pricing case is the same under either the Robinson-Patman Act or Section 2 of the Sherman Act.[25]

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[23] Because the factual differences between geographic and non-geographic primary-line Robinson-Patman Act claims are so striking, the Third Circuit limited *Utah Pie's* competitive injury analysis to primary-line, geographic price discrimination cases. O. *Hommel Co. v. Ferro Corp*, 659 F.2d 340, 351-52 (3d Cir.1981), *cert. denied*, 455 U.S. 1017, 102 S.Ct. 1711, 72 L.Ed.2d 134 (1982).

[24] *See* P. Areeda & D. Turner, *Antitrust Law* 720, at 190 (1978) ("The basic substantive issues raised by the Robinson-Patman Act's concern with primary-line injury to competition and by the Sherman Act's concern with predatory pricing are identical.").

[25] *See McGahee v. Northern Propane Gas Co.*, 858 F.2d 1487, 1493 n. 9 (11th Cir.1988), *cert. denied*, ____ U.S. ____, 109 S.Ct. 2110, 104 L.Ed.2d 670 (1989); *Henry*, 809 F.2d at 1345; *D.E. Rogers Assocs., Inc. v. Gardner-Denver Co.*, 718 F.2d 1431, 1439 (6th Cir.1983), *cert. denied*, 467 U.S. 1242, 104 S.Ct. 3513, 82 L.Ed.2d 822 (1984); *William Inglis & Sons Baking Co. v. ITT Continental Baking Co.*, 668 F.2d 1014, 1041 (9th Cir.1981), *cert. denied*, 459 U.S. 825, 103 S.Ct. 57, 74 L.Ed.2d 61 (1982); *O. Hommel*, 659 F.2d at 346-47; *Pacific Eng'g & Prod. Co. v. Kerr-McGee Corp.*, 551 F.2d 790, 798 (10th Cir.), *cert. denied*, 434 U.S. 879, 98 S.Ct. 234, 54 L.Ed.2d 160 (1977);

That this interpretation of the competitive injury requirement has been widely followed is not surprising since it best comports with basic antitrust principles. The antitrust laws' goal is to promote consumer welfare, not to discourage aggressive price competition. Liggett cannot satisfy the competitive injury requirement by showing simply that it was injured by B & W's price discrimination. Injury to competition occurs only if a competitor is able to raise and maintain prices in the relevant market above competitive levels because this is the only situation where consumer welfare is threatened. So, in order to injure competition via price discrimination in the United States cigarette market, B & W must be able to create a real possibility of both driving out rivals by loss-creating price cutting and then holding on to that advantage to recoup losses by raising and maintaining prices at higher than competitive levels. *See Matsushita*, 475 U.S. at 589, 106 S.Ct. at 1357.

With these principles in mind, there are fatal defects in both Liggett's theory and evidence of competitive injury. Liggett's theory of competitive injury was developed by its expert economist, William Burnett. Burnett concluded that B & W's predatory pricing of black and white cigarettes had a reasonable possibility of injuring competition in the entire United States cigarette market. He based his analysis on numerous B & W internal documents and his study of the structure and history of the cigarette industry. Burnett's theory is quite complicated and requires detailed explanation.

Central to Burnett's analysis is that the cigarette market is a highly concentrated oligopoly[26] and that predatory pricing schemes make sense in such markets. The starting point for this analysis is Burnett's opinion that all of the manufacturers in the

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International Air, 517 F.2d at 720 n. 10. *But see A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881, F.2d 1396, 1404-06 (7th Cir.1989), cert. denied, ___ U.S. ___, 110 S.Ct. 1326, 108 L.Ed.2d 501 (1990); *Monahan's Marine, Inc. v. Boston Whaler, Inc.*, 866 F.2d 525, 528-29 (1st Cir.1989).

[26] Oligopoly is the economic term for a market in which few producers are present. There is nothing illegal *per se* about an oligopoly.

cigarette industry, including Liggett, enjoy monopoly profits on the sale of their branded cigarettes. He bases this opinion on six factors: (1) the degree of concentration in the domestic cigarette industry; (2) the long-time industry pattern of list-price uniformity and price leadership--that is, when one manufacturer raises the price of its branded cigarette line the others follow and raise their prices to the same level; (3) the relative price inelasticity[27] of cigarette demand; (4) the significant barriers to entry, including large capital costs and the television advertising ban, which prevent new companies from competing with the major cigarette manufacturers; (5) an analysis of the relationship between cigarette prices and costs which concluded that prices have risen in the industry during a period of declining costs; and (6) the degree to which tobacco industry accounting rates of return exceed those of companies in the domestic food and kindred products industry. Burnett thought this industry structure made it possible for the major cigarette manufacturers to tacitly coordinate[28] their prices at supracompetitive levels.

According to Burnett, B & W engaged in a campaign of predatory pricing against Liggett's black and white cigarettes to protect its monopoly profits on branded cigarettes. Burnett alleged that B & W had great economic incentive to wage such a predatory campaign. His analysis was based on the following factors. First, consumer demand for cigarettes in the United States market was no longer growing and, due to health concerns, was unlikely to grow in the future. Thus, a cigarette manufacturer could increase its market share only at the expense of a rival competitor by getting existing cigarette consumers to switch their brand loyalty. Second, Liggett was a maverick--that is, Liggett

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[27] Elasticity means the responsiveness of a dependent variable to changes in a causal factor. Burnett looked at what happened to consumer demand in the cigarette industry when prices rose. He concluded that demand for cigarettes was inelastic because consumer demand did not decrease very much despite steadily rising prices.

[28] Burnett does not contend that the major cigarette manufacturers overtly engaged in price-fixing in a smoke-filled room. Instead, he believes the major manufacturers silently agreed that price uniformity was in their best interests and, therefore, priced in lock-step fashion.

was the only major cigarette manufacturer willing to compete for consumers by offering lower prices. Liggett was not worried about its black and white cigarettes cannibalizing its monopoly profits on branded cigarettes because its branded market share was so low. Third, B & W was hurt by Liggett's entry into generic cigarettes more than the other major manufacturers. On a percentage basis, significantly more B & W branded smokers were switching to Liggett generics than were smokers of brands of other manufacturers. As a result, B & W's market share and its alleged monopoly profits were eroding quickly. This erosion gave B & W its incentive to predate.

Burnett testified that B & W came up with an ingenious scheme to kill the generic category and stop losing market share. This alleged scheme is as follows. B & W entered the generic cigarette segment by offering a look-alike black and white package designed to confuse Liggett's existing generic smokers. B & W did not want to fuel consumer demand for generic cigarettes so it focused exclusively on establishing its new business at the wholesale level. B & W captured wholesaler loyalty through significant volume rebates, targeting Liggett's highest volume customers. These rebates made the price of black and white cigarettes to wholesalers well below B & W's average variable cost.[29] B & W encouraged the wholesalers to pocket these rebates instead of passing the savings on to consumers to prevent any new demand for black and white cigarettes.

According to Burnett, B & W's plan was a "win-win/lose-lose" strategy of predation since no matter what Liggett did in response B & W's plan would be successful. Because Liggett had

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[29] Average variable cost equals the sum of all the variable costs divided by output. For a manufacturing firm such as cigarette company, costs are divided into two categories -- fixed and variable. Variable costs fluctuate with a firm's output while fixed costs are independent of output. Variable costs typically include items such as a materials, fuel, labor, maintenance, licensing fees, and depreciation occasioned by use. Fixed costs generally include management expenses, overhead, interest on debt, and depreciation accusant by obsolescence. A price below average variable cost causes a manufacturer to lose money on each unit of output of the product.

limited financial resources, if it matched B & W's rebates it would have to cut back on its black and white consumer promotional campaign. This cutback in consumer advertising would slow the growth of the generic category and eventually, without advertising, demand for generic cigarettes would decline. If Liggett refused to offer rebates or offered less lucrative deals, its wholesale customers would abandon it in favor of B & W, preventing Liggett from getting its product to the consumer. In a few years, B & W could control prices in the generic cigarette category. Then it would narrow the price gap between branded and generic cigarettes. Price stimulated consumer demand for black and white cigarettes. By raising generic prices, B & W would decrease the relative savings on black and white cigarettes, thus cutting off consumer demand.

Although predatory pricing schemes are typically very costly due to below-cost pricing, Burnett thought B & W's plan was the exception because of simultaneous recoupment.[30] By entering the generic market in the above fashion, according to Burnett, B & W slowed the growth of the generic cigarette segment and thereby slowed the rate at which B & W branded smokers switched to generics. Thus, B & W recovered predatory losses immediately by slowing the loss of sales of its branded cigarettes sold at monopoly prices.

Burnett's theory is buttressed by numerous B & W documents written by top executives. These documents, indicating B & W's anticompetitive intent, are more voluminous and detailed than any other reported case. This evidence not only indicates B & W wanted to injure Liggett, it also details an extensive plan to slow the growth of the generic cigarette segment.[31]

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[30] Burnett's only theory of recoupment was simultaneous recoupment. He did not contend that B & W's recoupment would come by raising the price of generic cigarettes.

[31] Issues of corporate ethics and morality, or the lack thereof, are not appropriate subjects for consideration by the court unless they are also violative of the antitrust, trademark, and unfair competition claims alleged.

However, despite Burnett's complicated theory and the extensive documentary evidence, Liggett still has not satisfied the competitive injury requirement of the Robinson-Patman Act with any substantial evidence. As a matter of law, B & W could not have had a reasonable possibility of injuring competition unless at the very least it had the realistic prospect of obtaining market power over the generic segment of the market[32] and an economically plausible way to recoup its losses.[33]

Market power is "the ability to raise prices above levels that would exist in a perfectly competitive market." *Consul, Ltd. v. Transco Energy Co.*, 805 F.2d 490, 495 (4th Cir. 1986), *cert.*

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[32] Many circuits have held that the competitive injury requirement of the Robinson-Patman Act cannot be satisfied unless the alleged predator has at least a reasonable prospect of obtaining market power. *See Stitt Spark Plug Co. v. Champion Spark Plug Co.*, 840 F.2d 1253, 1255-56 (5th Cir.), *cert. denied*, 488 U.S. 890, 109 S.Ct. 224, 102 L.Ed.2d 214 (1988); *Henry*, 809 F.2d at 1345; *D.E. Rogers*, 718 F.2d at 1436 (quoting *Richter Concrete Corp v. Hilltop Concrete Corp*. 691 F.2d 818, 823 [6th Cir. 1982]); *O. Hommel*, 659 F.2d at 348; *Janich Bros. Inc. v. American Distilling Co.*, 570 F.2d 848, 856 (9th Cir. 1977), *cert. denied*, 439 U.S. 829, 99 S.Ct. 103, 58 L.Ed.2d 122 (1978); *Pacific Eng'g*, 441 F.2d at 798. A few circuits have been hesitant to apply the market power concept to the Robinson-Patman Act, but this hesitance has always been in the context of geographic price discrimination claims factually distinct from the non-geographic claim alleged here. *See* A.A. Poultry Farms, 881 F.2d at 14044-05; *John B. Hull, Inc. v. Waterbury Petroleum Prods., Inc.*, 588 F.2d 24, 28 (2d Cir. 1978), *cert denied*, 440 U.S. 960, 99 S.Ct. 1502, 59 L.Ed.2d 773 (1979); *Lloyd A. Fry Roofing Co. v. FTC*, 371 F.2d 277, 284-85 (7th Cir.1966). Most importantly, the Supreme Court has indicated that "[t]he success of any predatory scheme depends on maintaining monopoly power for long enough both to recoup the predator's losses and to harvest some additional gain." *Matsushita* 475 U.S. at 589, 106 S.Ct. at 1357.

[33] For a predatory pricing scheme to injure competition the predator must be able not only to recover its initial losses, but also harvest some additional gain. *Matsushita*, 475 U.S. at 588-89, 106 S.Ct. at 1356-57. This additional gain is called recoupment, and it is only at the recoupment stage that consumer welfare is injured.

denied, 481 U.S. 1050, 107 S.Ct. 2182, 95 L.Ed.2d 838 (1987). Without the power to control market prices, a firm that raises the price of a product cannot maintain that increase because other firms will offer consumers lower prices, thereby forcing the price raising firm either to lower prices or lose sales. *See Matsushita,* 475 U.S. at 590-91, 106 S.Ct. at 1357-58 ("petitioners must obtain enough market power to set higher than competitive prices, and then must sustain those prices long enough to earn in excess profits what they earlier gave up in below-cost prices"). An avowed predator with no prospect of controlling prices is a paper tiger unable to harm consumer welfare. Burnett's theory illustrates this point. According to Burnett, for B& W's scheme to succeed it had to raise generic cigarette prices above competitive levels; otherwise, it could not narrow the price gap between branded and generic cigarettes. Without a narrowing of this gap there is no incentive for generic consumers to switch back to their old brands, and B & W's alleged scheme necessarily fails.

With at most twelve per cent (12%) of the domestic cigarette market, B & W as a matter of law could not exercise market power unilaterally in either the whole cigarette market or the generic segment. *See Cargill, Inc. v. Monfort of Colorado Inc.,* 479 U.S. 104, 119 n. 15, 107 S.Ct. 484, 494 n. 15, 93 L.Ed.2d 427 (1986). Even Burnett conceded this point, admitting that acting alone B & W could not injure consumer welfare by narrowing the price gap between branded and generic cigarettes. However, Burnett argued B & W was not acting unilaterally due to tacit collusion -- that is, silent price coordination -- among the major manufacturers regarding branded prices. According to Burnett, this tacit collusion effectively gave B & W upwards of ninety-five per cent (95%) of the cigarette market.

Tacit collusion among the major cigarette manufacturers is a dubious theory of market power. In typical cases, market power analysis is straightforward and hinges on whether a company has a large enough market share to control prices in the relevant market. Under this traditional analysis, a company with twelve per cent (12%) of the market cannot have market power.[34] Burnett theorizes, however, that even a relatively small company like B & W can exercise shared market power through tacit collusion with the other major cigarette manufacturers save Liggett. Liggett cites no Robinson-Patman Act or Sherman Act legal precedent which supports this theory of shared market power via tacit collusion. By contrast, the shared market power theory has been rejected several times in the Sherman Act context. *See H.L. Hayden Co. v. Siemens Medical Sys, Inc.*, 879 F.2d 1005, 1018 (2d Cir.1989); *Consolidated Terminal Sys., Inc. v. ITT World Communications, Inc.*, 535 F.Supp. 225, 228-29 (S.D.N.Y. 1982); *In re Kellogg Co.*, 99 F.T.C. 8, 260 (1982). Furthermore, one circuit court considering a Section 2 Sherman Act claim frankly acknowledged that there is "no case support" for the shared monopoly theory. *Harkins Amusement Enters., Inc. v. General Cinema Corp.*, 850 F.2d 477, 490 (9th Cir.1988), *cert. denied*, 488 U.S. 1019, 109 S.Ct. 817, 102 L.Ed.2d. 806 (1989). Finally, a leading antitrust authority has noted that the scenario for predatory pricing by a firm possessing a small share of the market is "highly speculative" and "presses the potential for tacit price coordination very far." P. Areeda & H. Hovenkamp, *Antitrust Law* 711.2c, at 538-39 (Supp. 1989).

Although there is little legal precedent supporting Burnett's shared market power theory, in rejecting it the court need not rule that this theory is insufficient as a matter of law. The only record evidence supporting such a theory was Burnett's opinion testimony which was contradicted by witnesses from the Liggett boardroom. Ligett's most senior executives, including the president of the company, K.V. Dey unequivocally testified at trial there was not tacit collusion on branded cigarette pricing decisions, that the

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[34] *See, e.g., United Air Lines, Inc. v. Austin Travel Corp.*, 867 F.2d 737, 742 (2d Cir.1989) (no market power with 10% of the local market and 31% of the national market); *Rutman Wine Co. v. E & J Gallow Winery*, 829 F.2d 729, 736 (9th Cir.1987) (no market power with about 33% of the national market and 25% of the local market); *Pennsylvania Dental Ass'n v. Medical Serv. Ass'n*, 745 F.2d 248, 261 (3d Cir.1984) (no market power with 32-35% of the relevant market), *cert. denied*, 471 U.S. 1016, 105 S.Ct. 2021, 85 L.Ed.2d 303 (1985).

cigarette industry has never been a collusive oligopoly, and that the industry does not reap excessive profits.

Liggett seeks to explain this obvious problem by arguing that the decision-makers at Liggett are not economists and do not understand economic terms such a s oligopoly, tacit collusion, and monopoly profits. This argument was considered at the summary judgment stage since these executives gave basically the same testimony at their depositions. The court allowed the case to go to trial in part because of affidavits from the Liggett executives stating that they were confused by the questions asked by B & W lawyers and did not mean to contradict the testimony of Burnett. However, at trial, despite having consulted extensively with Burnett and having had adequate time to familiarize themselves with concepts such as tacit collusion, oligopoly, and monopoly profits, these Liggett executives again contradicted Burnett's theory. The court realizes that at the JNOV stage all reasonable inferences must be given to Ligget, the non-moving party. However, Burnett's expert opinion testimony on these issues cannot be considered substantial evidence sufficient to survive B & W's JNOV motion in light of unequivocal and contradictory trial testimony from senior executives at Liggett who made the pricing decisions. *See Newman v. Hy-Way Heat Sys., Inc.*, 789 F.2d 269, 270 (4th Cir.1976) (experts may not "speculate in fashions unsupported by, and in this case indeed in contradiction of, the uncontroverted evidence in the case"); *Selle v. Gibbb*, 567 F.Supp. 1173, 1182 (N.D.Ill.1983) ("[T]he law does not permit the oath of credible witnesses, testifying to matters within their knowledge, to be disregarded, particularly where lay persons give testimony contradicting existence of the ultimate fact to be inferred from the opinion of an expert.") *aff'd* 741 F.2d 896 (7th Cir.1984)[35]

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[35] *Accord Miller. v. FDIC*, 906 F.2d 972, 975 (4th Cir.1990) (plaintiff's contradictory testimony insufficient to create a genuine issue of fact); *Townley v. Norfolk & W. Ry. Co.*, 887 F.2d 498, 501 (4th Cir.1989) (a party may not create an issue of fact by contradicting own testimony); *Barwick v. Celotex Corp.*, 736 F.2d 946, 960 (4th Cir.1984) (a party examined at length on deposition cannot raise an issue of fact simply by submitting an affidavit contradicting the prior testimony).

Even if Burnett's opinion testimony on tacit collusion was uncontradicted, competition could not be injured by B & W unless it could raise generic cigarette prices, thereby narrowing the price gap between branded and generic cigarettes. Yet, even Burnett denied there was tacit collusion in the generic cigarette segment. Instead, his theory relied on the supposed motivations of the other major cigarette manufacturers. Burnett contended that there was an alignment of interest among these companies to protect their branded cigarette profits. Thus, they would not disrupt B & W's attempts to slow the growth of the generic segment. If no such alignment of interest existed and any of the other major cigarette manufacturers were interested in promoting the sale of generic cigarettes, even Burnett admitted that successful predation by B & W would be impossible.

No substantial record evidence supports Burnett's alignment of interest theory. Even before B & W began selling black and white cigarettes, RJR had entered the generic segment by repositioning Doral at generic prices. Burnett conceded that RJR had no anticompetitive intent and that Doral's entry expanded the generic segment. The evidence is uncontroverted that RJR's motive for selling generic cigarettes was to regain its number one positon in the cigarette industry from Philip Morris. In order to do this RJR had to sell a lot of generic cigarettes. Furthermore, there is no evidence that any of the other major cigarette companies had an interest in slowing the growth of generic cigarettes. Today, five of the six major manufacturers sell generic cigarettes in one form or another. Most importantly, in late 1985 B & W tried to raise the price of its generic cigarettes. Neither Liggett nor RJR followed with price increases -- exactly what is supposed to happen when a company without market power unilaterally raises its price above competitive level. Had there been an alignment of interest, RJR would have followed B & W's lead.

Not only is there no substantial evidence of market power, the testimony of Liggett's decision-makers that there were no monopoly profits obtained on branded cigarettes and that branded cigarette prices were fair to consumers totally undermines any plausible theory of economic recoupment for B & W. Without some likelihood of recoupment there is no reasonable possibility of injury to competition. Typically, recoupment happens after the predatory objective has been achieved and the predator has the ability to control prices. As explained earlier, Burnett's theory of simultaneous recoupment departed from this model. However, if there were no monopoly profits from branded cigarettes then B & W could not simultaneously recoup its losses from below-cost pricing.

Even apart from this testimony, there is another problem with Burnett's recoupment analysis. There is no substantial evidence in the record indicating that wholesalers would not promote the sale of generic cigarettes. Burnett's simultaneous recoupment theory depends on wholesalers pocketing B & W's volume rebates instead of promoting generic cigarettes; otherwise, there is no mechanism to slow the growth of the segment. Yet it makes no sense for wholesalers to pocket all of these rebates. Unlike branded cigarettes, there were no guarantees for wholesalers when they bought B & W's generic cigarettes. If the wholesalers did not sell all the generic cigarettes they bought, they were stuck with the product. B & W's volume rebates were lucrative to them only if they could sell their generic cigarette allotment; otherwise, they lost money. Therefore, there was no alignment of interest between B & W and the wholesalers with respect to generic cigarettes. To the extent that wholesalers wanted to sell generics to consumers, and the only record evidence at trial indicates that they did, B & W not slow the growth of the category and consumer welfare could not be injured.

Similarly, documentary evidence alone is not substantial evidence sufficient to satisfy the competitive injury requirement of the Robinson-Patman Act absent some showing of market power and the possibility of recoupment. *See Henry,* 809 F.2d at 1345. A company with aniticompetitive intent cannot injure consumers unless it has at least a reasonable possibility of obtaining market power and recouping its losses. B & W could not achieve either of these objectives and, therefore, it does not matter what the documents say concerning its hopes and plans.

Finally, Liggett did not provide any substantial evidence of actual injury to competition via market analysis. Obviously, without even the realistic prospect of obtaining market power it is impossible for a firm to actually injure competition since prices cannot be increased above competitive levels. Furthermore, even

Liggett admits that the generic cigarette segment has grown. Five of the six major cigarette companies have significant entries in the generic category, and growth has increased from about four per cent (4%) when Liggett was alone in the segment to fifteen per cent (15%). The success of generic cigarettes has even encouraged some price competition on branded cigarettes. This court is aware of no Robinson-Patman Act verdict upheld solely on market analysis grounds. Liggett's market analysis evidence is not compelling enough for this court become the first.[36]

B. *Causation*

The Robinson-Patman Act is aimed only at price discrimination. Liggett must prove that the reasonable possibility of injury to competition was "the effect of" price discrimination, 15 U.S.C § 13(a), in order to establish "the necessary causal

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[36] Much of Liggett's market analysis focus on the steady decline of the market share of black and white cigarettes. This decline has not injured consumers because of the steady growth of branded generic cigarettes sold at the same price as black and white cigarettes. Overall, the generic segment has grown with consumers preferring branded generic cigarettes to black and white cigarettes. The rest of Liggett's market analysis is equally unconvincing. Liggett contends that B & W caused the price differential between branded and generic cigarettes to decrease. Yet, the percentage price differential has remained about thirty per cent (30%), and B & W quickly retracted the only generic cigarette price increase that it initiated because the competition did not follow. Liggett also alleges that B & W's pricing forced it to reduce its advertising, thereby slowing the segment. Still, the generic cigarette category continued to grow, fueled in part by RJR's aggressive promotion of Doral. Finally, Liggett argues that the military market provides empirical evidence of actual injury to consumers. The generic segment now accounts for over thirty per cent (30%) of the military market, as compared to approximately fifteen per cent (15%) of the civilian market. However, the age, income, and image differences in the military and the civilian sectors make such inferences suspect; the market for generic cigarettes had grown in both sectors; and without any realistic prospect of obtaining market power B & W's conduct cannot be the cause of the different market shares in the two sectors.

relationship between the difference in prices and the alleged competitive injury." *Borden Co. FTC,* 381 F.2d 175, 180 (5th Cir.1967).[37]

In a typical primary-line Robinson-Patman Act case, the injury alleged is the result of geographic price discrimination. As the Supreme Court has explained, the Clayton Act, as amended by the Robinson-Patman Act, "was born of a desire by Congress to curb the use by financially powerful corporations of localized price-cutting tactics which had gravely impaired the competitive positon of other sellers." *FTC v. Anheuser-Busch, Inc.*, 363 U.S. 536, 543, 80 S.Ct. 1267, 1271, 4 L.Ed.2d 1385 (1960) (footnote omitted).[38] Proof of causation is straightforward when the price discrimination is geographic. In these cases, a national firm can supplant local competitors confined to a specific geographic market by charging below-cost prices in that market. The local competitor is necessarily limited to competing for customers who can buy at the below-cost price offered by the national company. The national firm can subsidize its losses in the local market through profits from sales in other geographic areas. Therefore, since the national firm can remain profitable while the local competitor cannot, the difference between the national firm's below-cost prices and its profitable prices has a reasonable possibility of injuring competition. However, Liggett's primary-line, non-geographic claim differs from this scenario, and the geographic causation rationale discussed above has no persuasive force. Both B & W and Liggett competed for generic sales throughout the United States, and Liggett competed in all the markets in which B & W offered the discriminatory prices.

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[37] *Accord Stitt Spark Plug,* 840 F.2d at 1257; *Black Gold, Ltd v. Rockwool Indus., Inc.*, 729 F.2d 676, 680 (10th Cir.), *Cert. denied,* 469 U.S. 854, 105 S.Ct 178, 83 L.Ed.2d 113 (1984); *William Inglis,* 668 F.2d at 1040; *Marty's Floor Covering Co. v. GAF Corp.*, 604 F.2d 266, 270 (4th Cir. 1979), *cert. denied,* 444 U.S. 1017, 100 S.Ct. 670 L.Ed.2d 647 (1980).

[38] *Accord Stehpen Jay Photography, Ltd. v. Olan Mills, Inc.*, 903 F.2d 988, 991 & n. 5 (4th Cir.1990); *O. Hommel,* 659 F.2d at 350; *Marty's Floor Covering,* 604 F.2d at 270; *International Air,* 517 F.2d at 720-21.

Because this claim is non-geographic, Liggett has not proven causation by any substantial evidence. The Robinson-Patman Act does not proscribe low prices. B & W's net prices were generally lower than Liggett's at every volume level. Yet, if there was any reasonable possibility of injury to competition from B & W's conduct it came from the low price that B & W offered to its customers and not from the fact that these low prices varied depending on volume. *See O. Hommel*,659 F.2d at 350-51 (when price discrimination occurs only in the same geographic market in which the predator and the target compete "[s]elective price-cutting cannot possibly be more harmful to small competitors than a general price reduction to the same level") (quoting Areeda & Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 Harv.L.Rev. 697, 725-26 [1975]).[39]

Even if B & W's low prices created a reasonable possibility of injuring competition by displacing Liggett and making it possible for B & W to raise generic cigarette prices, the fact that those prices varied gave B & W no advantage over Liggett. Liggett was free to compete for sales to B & W's low volume generic customers, as well as those customers getting the best deals from B & W. Liggett was not excluded from any markets. As a result, Liggett was not disadvantaged any more by B & W's volume rebates than it would have been by one uniform low price. Liggett's complaint is that B & W was selling generic cigarettes for a lower price than it could at all volume levels. Consequently, Liggett has not met its burden of causation because low prices, not price discrimination, provide the only possible linkage to competitive injury.

Liggett disagrees. It contends that the price discrimination was a central component of B & W's predatory plan enabling B & W to make its scheme cost effective and inducing wholesalers to buy generic cigarettes exclusively from B & W. The court will consider these arguments in turn.

Ligett contends that price discrimination made B & W's plan feasible by making it less costly than if B & W offered only

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[39] *Accord Official Publications, Inc, v. Kale News, Co.*, 884 F.2d 664, 667-68 (2d Cir.1989); *Borden*, 381 F.2d at 180.

one low price. It cites several documents indicating that B & W wanted to "put the money where the volume was." There are no primary-line, non-geographic cases, that this court is aware of, in which cost efficiency satisfied the Robinson-Patman Act's causation requirement. Such an argument if accepted would read any meaningful causation requirement out of the act. As opposed to one low price set at B & W's high volume rate, volume rebates certainly saved the company money. However, the same is true of any price discrimination by any firm since price discrimination by definition requires a higher and a lower price. Furthermore, although it may have been more cost efficient for B & W, price discrimination also meant that it would cost less for Liggett to match B & W's prices. Since Liggett and B & W had access to the same customers and markets, B & W could not inflict greater injury on Liggett by charging a lower uniform price. If Liggett was not injured more by the price discrimination then neither was competition, since Burnett's competitive injury theory hinges on B & W replacing Liggett as the generic price leader.

Liggett also argues that B & W's discriminatory rebates encouraged wholesalers to buy generic cigarettes exclusively from B & W. According to Liggett, the volume rebates acts as a magnet enticing customers to buy more B & W generic cigarettes to get to the next rebate level; because higher volume purchases entitled customers to higher discounts, customers opting to allocate a portion of their generic cigarette purchases to Liggett would in effect be penalized; to avoid this penalty customers would buy exclusively from B & W; the more exclusive relationships B & W could cement with former Liggett wholesale customers the faster B & W could displace Liggett and increase generic prices.

Again, Liggett cites no primary-line, non-geographic cases which support its analysis that encouraging exclusivity satisfies the Robinson-patman Act's causation requirement. Volume discounts do not hurt Liggett, and hence competition, more than any other incentive since both companies compete for the same customers and the same markets. Liggett could respond to B & W's volume rebates by allocating the majority of its own incentives to its high-volume customers, a practice it had followed even before B & W's entry. Furthermore, the only advantage to a wholesaler from getting into B & W's highest volume category is receiving the lowest volume levels, B & W's net prices were below Liggett's, obviously an incentive for a customer to buy only from the manufacturer offering the lowest price on the same product. Therefore, the magnet enticing customers to buy generic cigarettes exclusively from B & W was that B & W's net prices were below Liggett's at every volume level and not that B & W's competitive offer to customers took the form of volume rebates.

C. *Antitrust Injury*

In a private treble damage action brought under Section 4 of the Clayton Act,[40] there is an additional causation requirement-antitrust injury. Not only must Liggett prove that B &W's price discrimination had a reasonable possibility of injuring competition, Liggett also must prove that B & W's price discrimination caused its complained-of damages.

A private plaintiff like Liggett may not recover damages simply by showing "injury causally linked to an illegal presence in the market." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489, 97 S.Ct. 690, 697, 50 L.Ed.2d 701 (1977). Instead, Liggett must prove it was injured by conduct violating the Robinson-Patman Act. *See* 15 U.S.C. § 15(a). That is, Liggett must prove the existence of "'*antitrust injury*, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful.'" *Allegheny Pepsi-Cola Bottling Co. v. Mid-Atlantic Coca-cola Bottling Co.*, 690 F.2d 411, 414 (4th Cir.1982) (quoting *Brunswick,c 429 U.S.* at 489, 97 S.Ct. at 697-98). Therefore, Liggett cannot recover damages unless it is "able to show a casual connection between the price discrimination in violation of the Act and the injury suffered." *Perkins v. Standard Oil Co.*, 395 U.S. 642, 648, 89 S.Ct. 1871, 1874, 23 L.Ed.2d 599 (1969).

Subsequent to the completion of this trial, the Supreme Court decided a case clarifying the requirements of antitrust injury. The Supreme Court held:

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[40] Section 4 the Clayton Act is a remedial provision that makes treble damages available to "any person who shall be injured in his business or property by reason of any thing forbidden in the antitrust laws." 15 U.S.C. §15(a).

> Antitrust injury does not arise for purposes of § 4 of the Clayton Act until a private party is adversely affected by an *anticompetitive* aspect of the defendant's conduct; in the context of pricing practices, only predatory pricing has the requisite anticompetitive effect. Low prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition. Hence, they cannot give rise to antitrust injury.

Atlantic Richfield Co., v. USA Petroleum Co., ___ U.S. ___, 110 S.Ct. 1884, 1892, 109 L.Ed.2d 333 (190) (citations and footnotes omitted). In the context of the present case, *Atlantic Richfield* makes clear that only evidence of predatory pricing is sufficient to prove antitrust injury. Neither incriminating documentary evidence nor an allegedly distorted market proves antitrust injury unless accompanied by proof of predatory pricing. *Id.* 110 S. Ct. at 1891 n. 7 ("a firm cannot claim antitrust injury from non predatory price competition on the asserted ground that it is ruinous").

Liggett, of course, disagrees with this interpretation of *Atlantic Richfield*, arguing that the Supreme Court's antitrust injury analysis applies only to vertical maximum resale price-fixing cases and that the decision illustrates only that Sherman Act principles are different from Robinson-Patman Act principles. It cites as proof the fact that the Supreme Court in *Atlantic Richfield* did not dismiss the Robinson-Patman Act claim since it was "misconduct not relevant here." 110 S.Ct. at 1887. In *Atlantic Richfield*, plaintiff sued defendant under various legal theories including the Sherman Act, the Robinson-Patman Act, and state law unfair competition statutes. Defendant moved for summary judgment on the Section 1 Sherman Act claim and the district court granted the motion. On appeal, both the Ninth Circuit and the Supreme Court considered only the issue of whether dismissing plaintiff's Section 1 Sherman Act claim was proper. The Robinson-Patman Act claim was not relevant to the Supreme Court's decision because that claim was not before it. This language of the Supreme Court cannot be construed to mean that antitrust injury principles under the Robinson-Patman Act are fundamentally different from those under the Sherman Act.

Liggett's interpretation of *Atlantic Richfield* is legally insupportable for several reasons. First, Ligget alleges a primary-line, non-geographic Robinson-Patman Act claim analytically similar to a Section 2 Sherman Act attempted monopolization claim. The goal of both statutes is to maximize competition. Second, Liggett's interpretation is anticompetive since it protects Liggett from non-predatory price competition by B&W despite the fact that such activity cannot injure competition. In *Atlantic Richfield*, the Supreme Court reiterated that 'cutting prices in order to increase business often is the very essence of competition,' *id*. at 1891 (quoting *Matsushita*, 475 U.S. at 594, 106 S.Ct. at 1360), and Liggett has provided no theoretical justification for distinguishing between straight price cuts and volume rebates. Also, the Supreme Court has held on numerous occasions that the Robinson-Patman Act should be conformed if at all possible to the standards governing the other antitrust laws. See *Great Atl. & Pac. Tea Co. v. FTC*, 440 U.S. 69, 80, 99 S.Ct. 925, 933, 59 L.Ed.2d 153 (1979); *United States v. United States Gypsum Co.*, 438 U.S. 422, 548-59, 98 S.Ct. 2864, 2884-85, 57 L.Ed.2d 854 (1978); *Automatic Canteen Co. v. FTC*, 346 U.S. 61,63 73 S.Ct. 1017, 1019, 97 L.Ed. 1454 (1953). Third, Section 4 of the Clayton Act, 15 U.S.C. § 15(a), provides the antitrust injury standard for both the Sherman Act and the Robinson-Patman Act. It would be odd indeed to interpret the same language of Section 4 one way under the Sherman Act and another under the Robinson-Patman Act. Fourth, and most importantly, Liggett's interpretation requires this court to ignore the plain language of *Atlantic Richfield* in which the Supreme Court clearly stated that non-predatory pricing behavior cannot give rise to antitrust injury "regardless of the type of antitrust claim involved." 110 S. Ct. at 1892.

Liggett also argues that *Atlantic Richfield* does not apply to Robinson-Patman Act claims because it is price discrimination rather than predatory prices which must cause the antitrust injury. Liggett's position is correct as far as it goes. In Robinson-Patman Act cases the price discrimination must be linked with the antitrust injury. However, this does not mean that predatory pricing is not relevant. For that position to have merit there would have to be some anticompetitive aspect of price discrimination other than the fact that one or all of the prices charged were predatory. Yet, the only anticompetitive aspect to B&W's volume rebates is that they were allegedly below cost. Burnett's theory is that B&W's below-cost, volume rebates were designed to drive Liggett out of the generic cigarette segment. The below-cost aspect of these rebates was crucial since this forced Liggett to either lose money on the sale of generic cigarettes or lose customers to B&W. For these reasons this court is convinced that in a primary-line, non-geographic price discrimination case predatory pricing is the only type of evidence which satisfies the antitrust injury requirement.

The court must examine whether Liggett has presented any substantial evidence of antitrust injury. The Supreme Court has stated that "predatory pricing may be defined as pricing below an appropriate measure of cost for the purpose of eliminating competitors in the short run and reducing competition in the long run." *Cargill*, 479 U.S. at 117, 107 S.Ct. at 493. But the Court has never defined what "cost" is relevant. *Id.* at 117 n. 12, 107 S.Ct. at 493 n.. Given this Supreme Court guidance, most circuits presume that pricing below reasonably anticipated marginal cost is predatory.[41] Because marginal costs cannot be determined easily from conventional accounting methods, average variable cost is used as a surrogate. Most cases of predatory pricing focus on average variable cost evidence, and this one is no different.[42]

Liggett's predatory pricing evidence consisted of expert testimony that B&W priced its generic cigarettes below average variable cost. B&W countered with its chief financial officer who admitted that B&W lost money on the sale of generic cigarettes but stated prices were never below average variable cost. He explained that most companies lose money when they introduce a new product and that there was nothing exceptional about that.

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[41] *See, e.g., Northeastern Tel. Co. v. AT&T Co.*, 651 F. 2d 76, 88 (2d Cir.1981) (citations collected therein), *cert. denied*, 455 U.S. 943, 102 S.Ct. 1438, 71 L.Ed.2d 654 (1982).

[42] This court used average variable cost because Liggett's evidence of predatory pricing centered on this measure; average variable cost is a conservative measure unlikely to penalize the competitive pricing activities of a more efficient competitor; and many circuits use some variant of the average variable cost test to isolate predatory pricing.

Furthermore, he stressed that B&W's overall line of cigarettes--generic plus branded--was very profitable.

In order to evaluate Liggett's predatory pricing evidence, this debate need not be resolved. The court believes that Liggett's predatory pricing evidence must show that B&W lost money in the relevant market stipulated to by the parties prior to trial--the market for all cigarettes in the United States. Liggett has not and cannot do this. The evidence is uncontroverted that B&W made money on its overall cigarettes sales--branded and generic--during the alleged predatory period.

The parties have stipulated that the relevant market is the entire cigarette market in the United States. Upon close examination, this court believes that there is no substantial economic evidence that generic cigarettes are sufficiently distinct from branded cigarettes alone.[43] Markets are determined by the substitutability of goods, and market definitions turn on these goods' cross-elasticity of demand and supply. Cross-elasticity of demand is the extent to which products are "reasonably interchangeable by consumers for the same purposes." *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395, 76 S.Ct. 994, 1007, 100 L.Ed. 1264 (1956). Cross-elasticity of supply is "the capability of other production facilities to be converted to produced a substitutable product." *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 794 F.2d 210, 218 (D.C. Cir. 1986), *cert. denied*, 479 U.S. 1033, 107 S.Ct. 880, 93

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[43] Since Liggett and B&W are full-line competitors who compete for market share across all cigarette product lines, this court instructed the jury that they could consider Liggett's below-cost pricing evidence only if they determined that generic cigarettes formed a well-defined submarket based on the practical indicia test of *Brown Shoe Co. v. United States*, 370 U.S. 294, 324, 82 S.Ct. 1502, 1524, 8 L.Ed.2d 510 (1962). The court used this concept to aid the jury in determining whether generic cigarettes were sufficiently distinct from branded cigarettes to justify applying the average variable cost test to generic cigarettes, and not as a means of deciding the appropriate market in which to evaluate competitive injury. If there are no significant economic differences between the two products there is no reason to analyze their price-cost relationship separately.

L.Ed.2d 834 (1987). There is obviously high cross-elasticity of demand between branded and generic cigarettes. In fact, Liggett's theory hinges on consumers substituting generic for branded cigarettes because the alleged reason for predating was that B&W branded smokers were switching to Liggett's generic cigarettes. There is also high cross-elasticity of supply between branded and generic cigarettes because the same machines that make branded cigarettes can easily produce generic cigarettes.

Because there is no question that generic and branded cigarettes compete with each other for the favor of consumers, there is no economic justification for analyzing one separately from the other. Where there is nothing economically distinct about a particular product line, the average variable cost test should not be applied to it. Dr. Philip Areeda, one of the fathers of that test, explains that where the predator and the target sell the same line of products the average variable cost test should be applied to an alleged predator's entire product line instead of to a particular product because "rivals generally can hardly be ruined so long as prices for the product line as a whole are compensatory." P. Areeda & H. Hovenkamp, *Antitrust Law* 1715.1a, at 592 (Supp. 1989). Numerous courts, in cases like this one where the parties are full product line competitors, have refused to apply the average variable cost test to a single product line because there could be no competitive injury in the relevant market even if that product line was priced below cost.[44]

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[44] *See Morgan v. Ponder*, 892 F.2d 1355, 1361-62 (8th Cir. 1989) (court refuses to apply a price-cost test solely to legal advertising as opposed to all commercial advertising); *Stitt Spark Plug*, 840 F.2d at 1256-57 (a relevant predatory pricing analysis must include defendant's entire line of spark plugs and not just its original equipment line); *Directory Sales Management Corp. v. Ohio Bell Tel. Co.*. 833 F.2d. 606, 614 (6th Cir. 1987) (although a telephone company gave away free first listings in its telephone book, they engaged in predatory pricing only if their "overall charges for advertising space in their yellow pages are priced below cost"); *Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc.*, 824 F.2d 582, 597-98 (8th Cir.1987), *cert. denied*, 484 U.S. 1010, 108 S.Ct. 707, 98 L.Ed.2d 658 (1988) (court refused to apply below-cost pricing test to only four of the 180 common items that competing specialty food stores sold); *Bayou Bottling, Inc. v. Dr. Pepper*

During the alleged predatory period, Liggett and B&W were both profitable, full product line competitors with access to the same customers and markets. Due to these facts, applying the average variable cost test solely to B&W's generic cigarettes would be inappropriate. An examination of price-cost relationships should be made only in reference to the dangers posed by predatory pricing. *Henry*, 809 F.2d at 1344 ("the issue of 'predatory intent' should focus on what the defendant did and whether it could lead to the evil feared"). Under Liggett's theory, the danger posed by B&W's predatory pricing was that B&W would obtain control of the generic segment, raise prices, and thereby kill-off the only low-price alternative to branded cigarettes to the disadvantage of consumers. Even assuming that this danger was real, consumer welfare could not be injured if Liggett responded by switching emphasis to its line of branded cigarettes and decreasing their price, thus charging consumers a fair price instead of a monopolistic one. This would prevent injury to both Liggett and the consumer. Liggett's market share would increase to offset its lost monopoly profits and consumers would still have a low-price cigarette alternative. Furthermore, B&W could not recoup if Liggett decreased branded prices because cost-conscious consumers would switch to the low-price Liggett brands instead of other branded cigarettes priced at monopoly rates. If the average variable cost test is applied solely to generic cigarettes and antitrust injury is inferred from this below-cost pricing, then Liggett is unjustly rewarded for failing to compete on price with its branded cigarettes. Under this scenario, Liggett's antitrust injury would come from its unwillingness to charge a competitive price for its branded cigarettes and not from B&W's price discrimination. Since Liggett has failed to introduce substantial evidence of predatory pricing to meet the antitrust injury

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Co., 725 F.2d 300, 305 (5th Cir.), *cert. denied*, 469 U.S. 833, 105 S.Ct. 123, 83 L.Ed.2d 65 (1984) (where both parties are full-line competitors, 32-ounce bottles not a relevant product to apply average variable cost test to); *Janich Bros.*, 570 F.2d at 856 (half gallon containers of gin and vodka are not relevant products for predatory pricing analysis); *Sewell Plastics, Inc. v. Coca-Cola Co.*, 720 F.Supp. 1196, 1228 (W.D.N.C. 1988) (three-liter bottles not a relevant product for predatory pricing analysis).

requirement, this provides another ground for granting B&W's JNOV motion.

III. THE TRADEMARK ISSUES

Liggett has made a motion for a new trial pursuant to Rule 59, Fed.R.Civ.P., on the trademark and unfair competition claims arising from B&W's alleged infringement of Liggett's quality seal trademark. Liggett contends that the court should order a new trial on these issues because (1) the jury verdict was clearly against the weight of the evidence, (2) B&W repeatedly relied upon prejudicial, inadmissible, and improper evidence which obtained the jury process, and (3) Liggett was precluded from using evidence which could have countered B&W's prejudicial and misleading arguments. The court finds these contentions to be without merit, and Liggett's motion will be denied.

A motion for a new trial is governed by a different standard than a JNOV motion. *Gill v. Rollins Protective Servs. Co.*, 773 F.2d 592, 594 (4th Cir.1985), *modified on other grounds*, 788 F2d 1042 (4th Cir.1986). Recently the Fourth Circuit has reiterated the trial court's duty in ruling on a Rule 59 motion for a new trial. In *Poynter by Poynter v. Ratcliff*, 784 F.2d 219, 223 (4th Cir.1989), the court explained that:

> Under Rule 59 of the Federal Rules of Civil Procedure, a trial judge may weigh the evidence and consider the credibility of the witnesses and, if he finds the verdict is against the clear weight of the evidence, is based on false evidence or will result in a miscarriage of justice, he must set aside the verdict, even if supported by substantial evidence, and grant a new trial.

See also Wyatt, 623 F.2d 888, 891-92; *Williams v. Nichols*, 966 F.2d 389, 392 (4th Cir.1959). A new trial may also be granted if the court believes it has erred in the admission or rejection of evidence, or improperly instructed the jury. *Montgomery Ward & Co. v. Duncan*, 311 U.S. 243, 251, 61 S.Ct. 189, 194, 85 L.Ed. 147 (1940).

To establish trademark infringement a plaintiff must prove that there is a "likelihood of confusion" between its mark and the defendant's mark. *Pizzeria Uno Corp. v. Temple*, 747 F.2d 1522, 1527 (4th Cir.1984). Both parties presented evidence from which a reasonable jury could have found in favor of that party on the trademark and unfair competition issues. The jury ruled for B&W. From the evidence introduced on the seven likelihood of confusion factors outlined in *Pizzeria Uno*,[45] the verdict cannot be considered contrary to the clear weight of the evidence.

The cornerstone of Liggett's position is its contention that B&W's stipulation of the validity of Liggett's quality seal trademark precluded any evidence or argument by B&W that consumers were not aware of the quality seal. Liggett couples this argument with the contention that B&W's repeated references to the results of Liggett's Conway Milken Report, a telephone survey of consumers conducted by Liggett, as proof of lack of consumer recognition of the quality seal, were improper and contrary to the court's *in limine* ruling.

Liggett's contention that the stipulation of validity of the quality seal trademark precluded evidence and argument by B&W that most consumers were not aware of the mark is contrary to the position taken by Liggett's counsel at trial. Liggett's counsel conceded on the record at the charge conference that the strength of the mark was a question for the jury, that B&W could ague that it was not recognized, and that Liggett could argue that it was recognized. Evidence of the extent of consumer awareness of a mark obviously helps a jury determine the scope of protection to be afforded the mark. However, the court clearly instructed the jury that Liggett had valid federal trademark registrations for the quality seal and that the jury must accept the quality seal as a valid trademark.

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[45] The seven factors are: (1) the strength or distinctiveness of the mark; (2) the similarity of the two marks; (3) the similarity of the goods/services identified by the marks; (4) the similarity of the facilities the two parties use in their businesses; (5) the similarity of the advertising used by the two parties; (6) the defendant's intent; (7) actual confusion.

Furthermore, Liggett's argument that the stipulation of validity precludes evidence that consumers were not aware of the mark is simply not the law. *See Miss World (U.K.) Ltd. v. Mrs. America Pageants*, 856 F.2d 1445, 1449 (9th Cir.1988) ("[A]n incontestable status does not alone establish a strong mark."); *Oreck Corp. v. U.S. Floor Sys., Inc.*, 803 F.2d 166, 171 (5th Cir. 1986) (incontestable status does not preclude defendant from arguing mark is weak and not infringed; "Incontestable status does not make a weak mark strong."), *cert. denied*, 481 U.S. 1069, 107 S.Ct. 2462, 95 L.Ed.2d 781 (1987); *see also Munters Corp. v. Matsui America, Inc.*, 730 F.Supp. 790, 795-96 (N.D. Ill. 1989), *aff'd* 909 F.2d 250 (7th Cir. 1990); *Cullman Ventures, Inc. v. Columbian Art Works, Inc.*, 717 F.Supp. 96, 121 (S.D.N.Y. 1989); 2 J. McCarthy, *Trademarks and Unfair Competition* § 32:44D (2d ed. 1984 & Supp. 1989).

Liggett's emphasis on B&W's questions to witnesses and arguments about Liggett's Conway Milliken study is also misplaced. The court explained on numerous occasions during the trial that Liggett's extensive testimony and evidence concerning the promotion of its quality seal opened the door to cross-examination and evidence of the effectiveness of that promotion. The court then allowed Liggett to present additional evidence about what the study was designed to determine, how it was conducted, and the significance of the results. Furthermore, Liggett's counsel had ample opportunity in closing arguments to counter any arguments by B&W's counsel concerning the significance of the Conway Milliken Report.[46]

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[46] Liggett also contends that B&W improperly took advantage of the court's pre-trial rulings which prevented Liggett from calling consumers who had confused B&W's black and gold lion closure seal, a seal which was not the basis of Liggett's claim in this case, with the Liggett quality seal trademark. Liggett further contends that it was tricked or prevented from calling Saul Lefkowitz, a former chairman of the United States Trademark Trial and Appeal Board, who would have testified that registration of the quality seal was proper, a fact B&W conceded. Other proposed testimony by Mr. Lefkowitz sought to instruct the jury on the law, a matter within the province of court. The court is satisfied that its initial position concerning these witnesses was correct.

Liggett's other arguments concerning the use of prejudicial, inadmissible and improper evidence are based almost exclusively on B&W's closing argument. However, Liggett failed to object during closing argument to most of the statements which it now claims were so prejudicial as to warrant a new trial. The Fourth Circuit has emphasized that "[i]t is the universal rule that during closing argument counsel 'cannot as a rule remain silent, interpose no objections, and after a verdict has been returned seized for the first time on the point that the comments to the jury were improper and prejudicial.'" *Dennis v. General Elec. Corp.* 762 F.2d 365, 366-67 (4th Cir.1985) (quoting *United States v. Elmore*, 423 F.2d 775, 781 [5th Cir.] *cert. denied*, 400 U.S. 825, 91 S.Ct. 49, 27 L.Ed.2d 54 [1970], and *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 239, 60 S.Ct. 811, 851-52, 84 L.Ed. 1129 [1940]). Liggett had every opportunity in its rebuttal argument to clarify any arguments which it believed were misleading on the part of B&W. The alleged improprieties in B&W's closing argument do not involve any exceptional circumstances which would impair "the public reputation and integrity of the judicial proceeding." *Dennis*, 762 F.2d at 367; *see also Socony-Vacuum Oil*, 310 U.S. at 239, 60 S.Ct. at 851-52.

For the foregoing reasons, Liggett's motion for a new trial on the trademark and unfair competition claims will be denied.

An order and judgment in accordance with this memorandum opinion shall be entered contemporaneously herewith.

ORDER and JUDGMENT

For the reasons set forth in a memorandum opinion filed contemporaneously herewith,

IT IS ORDERED AND ADJUDGED that Defendant's motion for judgment notwithstanding the verdict pursuant to Rule 50(b), Federal Rules for Civil Procedure, be, and the same hereby is, GRANTED, and that the jury verdict and judgment in favor of the Plaintiff be, and the same hereby is, SET ASIDE, and judgment entered for the Defendant; and

IT IS FURTHER ORDERED that Defendant's alternative motion for a new trial pursuant to Rule 59, Federal Rules of Civil Procedure, be, and the same hereby is, DENIED; AND

IT IS FURTHER ORDERED that Plaintiff's motion for a new trial pursuant to Rule 59, Federal Rules of Civil Procedure, be, and the same hereby is, DENIED.

STATUTORY PROVISIONS INVOLVED
UNITED STATES CODE
TITLE 15

15 U.S.C. § 2; (Sherman Act §2)

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $10,000,000 if a corporation, or, if any other person, $350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

15 U.S.C. §§ 13 (a); (Robinson-Patman Act § 2(a))

It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, of to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them: Provided, That nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered: Provided, however, That the Federal Trade Commission may, after due investigation and hearing to all interested parties, fix and establish quantity limits, and revise the same as it finds necessary, as to particular commodities or class of commodities, where it finds that available purchasers in greater quantities are so few as to render differentials on account thereof unjustly discriminatory or promotive of monopoly in any line of commerce; and the foregoing shall then not be construed to permit differentials bases on differences in quantities greater than those so fixed and established: And provided further, That nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade: And provided further, That nothing herein contained shall prevent price changes from time to time where in response to changing conditions affecting the market for or the marketability of the goods concerned, such as but not limited to actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned.