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SUPREME COURT EQUATES BUYER-SIDE "PREDATORY" BUYING WITH SELLER-SIDE PREDATORY PRICING

On February 20, 2007, the Supreme Court issued a unanimous opinion in *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., Inc*.[1] In reversing the jury verdict for the plaintiff and holding that alleged predatory buying is subject to the same principles as alleged predatory pricing, as articulated in *Brooke Group v. Brown & Williamson Tobacco Corp.*,[2] the Court removed significant uncertainty as to when competing for inputs crosses the line from aggressive competition to potentially illegal predation under the Sherman Act. *Weyerhaeuser*, however, does not relax the more rigorous tests for illegality that may apply to concerted conduct by buyers. Accordingly, although the Supreme Court has given firms significantly greater freedom to compete for scarce inputs, caution is still appropriate when forming buying groups designed to achieve the same objective.

Background

Logs, the most significant cost of a sawmill, are often purchased through an open bidding market. Sawmill operators purchase logs as inputs and sell hardwood. Petitioner Weyerhaeuser, a hardwood lumber sawmill operator, enjoyed a 65 percent share of the upstream alder log market but held only 3 percent of the downstream hardwood market (other types of wood can be used to make hardwood). Nonetheless, according to rival Respondent Ross-Simmons, Weyerhaeuser bid up the price of alder logs to the point at which Ross-Simmons could not profitably sell hardwood, ultimately causing Ross-Simmons' sawmill to shut down.

In an ensuing action, Ross-Simmons charged that Weyerhaeuser's use of its monopsony power (that is, a buyer-side monopoly power) to drive Ross-Simmons out of business violated Section 2 of the Sherman Act. Ross-Simmons asserted that, under Learned Hand's famous opinion in *Alcoa*,[3] buying at more than a "fair price" in order to obtain market power in an input market was unlawful. By contrast, Weyerhaeuser asserted that its conduct must be analyzed under *Brooke Group*'s test for predatory pricing, which requires a price "below cost" and a "dangerous probability of recouping" the predator's below-cost "investment."[4]

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1 No. 05-381 (Feb. 20, 2007) ("Slip Op.").

2 509 U.S. 209 (1993).

3 In *U.S. v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945) ("*Alcoa*"), the court held it unlawful for a monopolist to charge more than a "fair price" for a primary product while simultaneously charging too little for a secondary product as a result of which second-level competitors could not "make a living profit." *Id*. at 437-38.

4 *Brooke Group*, 509 U.S. at 222-24.

The District Court, agreeing with Ross-Simmons, charged the jury that Weyerhaeuser's conduct could be unlawful if Weyerhaeuser "purchased more logs than it needed, or paid a higher price for logs than necessary, in order to prevent [Ross-Simmons] from obtaining the logs they needed at a fair price."[5] The jury returned a $79-million verdict, including treble damages, against Weyerhaeuser. The Court of Appeals affirmed.[6] Granting certiorari, the Supreme Court, in a unanimous opinion by Justice Thomas, disagreed, and held that *Brooke Group* governs predatory-buying schemes. Because Ross-Simmons conceded that it could not meet the *Brooke Group* test, the Court vacated the Ninth Circuit's judgment and remanded the case for further proceedings.[7]

The Supreme Court's Predatory Buying Analysis

The *Weyerhaeuser* Court grounded its analysis on the insight that predatory-buying schemes are "analytically similar" to predatory-pricing schemes.[8] The *Brooke Group* rule, requiring proof of below-cost pricing and recoupment, rests on the premises that predatory-pricing schemes often fail; that below-cost pricing often benefits consumers; and that the risk of costly "false positives" — the "chill[ing of] legitimate price cutting" by improperly condemning competitively benign activity — is significant.[9] A more relaxed legal test risks "depriving consumers of the benefits of lower prices."[10] Predatory buying, the Court reasoned, is similar because "both claims" require that the predator "suffer losses today on the chance that it will reap anticompetitive profits in the future."[11] Moreover, just as low prices can benefit consumers, aggressive bidding for inputs, too, can produce consumer benefits during the alleged "predatory" period.[12] Indeed, the Court reasoned, alleged predatory buying poses *fewer* competitive risks than predatory pricing, because obtaining upstream monopsony power does not invariably threaten downstream market power that is necessary to cause consumer harm.[13]

The Court accordingly reasoned that *Brooke Group*'s principles apply to predatory-buying schemes. Nonetheless, the Court recognized that *Brooke Group*'s "below-cost" prong required an adjustment when applied to predatory buying. Specifically, as applied to predatory buying, the test remains whether price is below cost in the output market, but the relevant costs include increased costs from higher input prices.[14] Thus, as the Court explained, raising price upstream is potentially predatory if it "cause[s] the cost of the relevant output to rise above the revenues generated in the sale of those outputs."[15]

Although the Court focused on the output market in applying *Brooke Group*'s below-cost prong, the Court did not address whether the recoupment prong must include some effect in the output market or, as some have suggested, could focus solely on harm in the input market. Ross-Simmons' theory focused on potential harm in

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5 Slip Op. at 3-4.

6 *Confederated Tribes of Siletz Indians of Or. and Ross-Simmons Hardwood Lumber Co. v. Weyerhaeuser Co.*, 411 F.3d 1030, 1035 (9th Cir. 2005).

7 Slip Op. at 13.

8 *Id.* at 8.

9 *Id.* at 5-6, 7.

10 *Id.* at 6 (citing *Brooke Group*, 509 U.S. at 224).

11 *Id.* at 10.

12 *Id.* at 11.

13 *Id.*

14 *Id.* at 12.

15 *Id.* (citing *Brooke Group*, 509 U.S. at 223).

the upstream alder log market; but because Ross-Simmons conceded that it could not meet the *Brooke Group* test, the Court did not address whether downstream harm was required. Nonetheless, the Court's emphasis that "[s]imilar legal standards should apply to claims of monopolization and to claims of monopsonization"[16] strongly suggests that some form of consumer harm (*i.e.*, some effect in the output market) may ultimately be required for illegality. This is a key issue that the lower courts likely will address in subsequent cases.

Implications

Weyerhaeuser gives firms greater freedom to compete aggressively for inputs. Provided that prices in the output market remain above cost, Section 2 claims challenging input prices as illegally high should fail. Although the Court technically reserved whether a different legal test might apply when the plaintiff's theory is that the defendant employed higher input prices as a strategy to impede rivals in the *output* market,[17] the Court's logic strongly suggests that the same legal test should govern both "upstream" and "downstream" predatory buying claims.

Nonetheless, *Weyerhaeuser* only concerns unilateral conduct challenged under Section 2 of the Sherman Act. The Court did not alter the rules that apply to *concerted* buyer-side activity by rivals. Such activity, which remains subject to Sherman Act Section 1's Rule of Reason, is subject to potentially more stringent antitrust scrutiny. Thus, before engaging in joint bidding, forming buyer co-ops, or jointly negotiating royalty rights, careful attention to the potential antitrust issues remains essential.

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16 *Id.* at 9; *see also id.* at 12 (acknowledging the "general theoretical similarities of monopoly and monopsony").

17 *Id.* at 8 n.2.

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