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Client Alert

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Supreme Court Vacates $79 Million Monopolization Verdict and Clarifies Rule Regarding Predatory Bidding

On February 20, the Supreme Court issued its opinion in *Weyerhaeuser Co. v. Ross Simmons Hardwood Lumber Co.*,[1] the first of four antitrust cases it will be deciding this term.[2] The case provides important guidance to firms in relation to their purchasing practices. It also demonstrates the Court's continued skepticism of predatory conduct claims under Section 2 of the Sherman Act and a reluctance to impose rules that might chill pro-competitive business behavior.

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The case involved allegations that the defendant overbid on key inputs in order to drive its weaker rival out of the market. The plaintiff had secured a $79 million jury verdict which the Ninth Circuit affirmed. The Supreme Court reversed. The Court noted that predatory bidding is analytically similar to predatory pricing and thus should be analyzed under the two-pronged predatory pricing test that the Court established in 1993. That test creates a high hurdle for plaintiffs and thus the decision represents a clear victory for large power buyers, giving them substantial leeway to bid aggressively for materials. The decision is also a victory for those who advocate bright line rules that businesses and their counsel can practically apply rather than the more normative concepts set forth by the Ninth Circuit.

This *Client Alert* briefly summarizes the *Weyerhaeuser* case and key take-aways.

Summary of *Weyerhaeuser*

Plaintiff Ross-Simmons operated a hardwood lumber sawmill in the Pacific Northwest. Defendant Weyerhaeuser also operated hardwood lumber sawmills in the Pacific Northwest and had amassed a large share of the purchasing market for alder, the region's primary hardwood. From 1998 to 2001, the input cost of alder sawlogs increased while the output price of hardwood lumber decreased. Caught in this squeeze, Ross-Simmons ultimately became unprofitable and went out of business in 2001. Ross-Simmons alleged that Weyerhaeuser drove it out of business by purposefully bidding up the cost for alder sawlogs to artificially high levels and buying more logs than necessary.

Ross-Simmons sued in the Oregon District Court alleging that Weyerhaeuser was engaged in monopolization and attempted monopolization in violation of Section 2 of the Sherman Act.[3] Both monopolization and attempted monopolization require a showing of anticompetitive conduct. Predatory

schemes can constitute such conduct. The quintessential predatory scheme is predatory pricing where a competitor sells its goods at prices so low that other firms are forced out of the market. Once the predator has the market to itself, it hikes prices to monopoly levels during a recoupment phase, making up for its earlier losses (and then some). In a predatory bidding scheme, the type alleged by Ross-Simmons, the predator seeks to drive its rivals out of the market not by lowering the prices of finished goods, but by bidding up the price for inputs and then once the rivals are gone, exercising its "monopsony power" (market power on the buy-side) to depress the prices it must pay suppliers during the recoupment phase.

At trial the District Court instructed the jury that Ross-Simmons could prove that Weyerhaeuser's bidding practices were anticompetitive if the jury concluded that 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." The jury returned $26 million verdict against Weyerhaeuser which was trebled to approximately $79 million.

Weyerhaeuser appealed. It argued, among other things, that the District Court's verdict ran afoul of the Supreme Court's 1993 predatory pricing decision in *Brooke Group Ltd. v. Brown & Williamson Tobacco, Corp*.[4] In *Brooke Group*, the Supreme Court held that a predatory pricing plaintiff must show (1) that the defendant had engaged in below-cost pricing in the short term and (2) that the defendant had a dangerous probability of recouping its losses in the long term.[5]

The Ninth Circuit rejected Weyerhaeuser's argument and affirmed the verdict.[6] It held that the Supreme Court's high liability standard for sell-side predatory pricing set forth in *Brooke Group* did not apply to buy-side predatory bidding. It noted that the benefit to consumers and stimulation of competition do not necessarily result from predatory bidding the way they do from predatory pricing.[7] The Ninth Circuit noted that consumers necessarily benefit during the initial phase of predatory pricing schemes when the predator lowers prices to try and drive out its rival. In a predatory bidding scheme, on the other hand, the predator can maintain or even raise the prices for its finished products while attempting to squeeze out its competitors and no consumers would benefit.[8]

The Supreme Court granted *certiorari* to decide whether the *Brooke Group* predatory pricing test should apply to claims of predatory bidding. Weyerhaeuser was supported in the Supreme Court by several amici curiae including the United States antitrust agencies which filed a brief arguing that application of the *Brooke Group* standard was preferable because it would decrease the possibility of "false positives," *i.e.* antitrust liability attaching to procompetitive behavior.

Weyerhaeuser, and several of the amici, argued that the Ninth Circuit's rule which relied on subjective notions of what price is "fair" and how much input was "necessary" was hopelessly vague and provided inadequate guidance to juries and businesses. It would, they argued, lead executives worried about antitrust liability to refrain from competing aggressively. Ross-Simmons, also supported by amici curiae, including several state Attorneys General, argued that predatory bidding, especially on the facts of the case, was quite different than predatory pricing, carrying less of a risk of "false positives," and that *Brooke Group*'s high standard of liability was not warranted.

The Supreme Court did not accept plaintiff's argument. In the opinion, authored by Justice Thomas, the Court found that predatory pricing and predatory bidding claims are analytically similar. The Court unanimously and

unambiguously held that the strict *Brooke Group* predatory pricing standard applies to predatory bidding. Specifically, it held that "a plaintiff must prove that the alleged predatory bidding led to below-cost pricing of the predator's outputs. That is, the predator's bidding on the buy side must have caused the cost of the relevant output to rise above the revenues generated in the sale of those outputs . . . A predatory-bidding plaintiff also must prove that the defendant has a dangerous probability of recouping the losses incurred in bidding up input prices through the exercise of monopsony power."

The Court repeated the frequently quoted passage from *Brooke Group* that "predatory pricing schemes are rarely tried, and even more rarely successful," and extended this view to predatory bidding. Indeed, the Court noted that predatory bidding was even *less* of a threat to consumers than predatory pricing because a predatory bidder does not necessarily rely on raising prices in the output market to recoup its losses. The Court noted that there were myriad legitimate reasons why a buyer might bid up input prices. These include a miscalculation of its input needs, a response to increased consumer demand, gaining market share in the output market, and hedging against future input price increases or shortages. The Court noted that there was nothing illicit about such bidding decisions. The Court remanded the case for further proceedings consistent with its opinion.

Take-Aways from *Weyerhaeuser*

- Businesses, even those with high market shares, have wide latitude to bid aggressively for inputs without fear of Sherman Act section 2 liability.
- The Court remains highly skeptical of predation claims.
- Truly predatory bidding behavior, marked by below-cost pricing of outputs and a dangerous probability of recouping the losses incurred in bidding up input prices through the exercise of monopsony power remains illegal.
- The Court appears unwilling to adopt rules that will potentially chill pro-competitive behavior.
- *Weyerhaeuser* marks another pro-business, pro-defendant antitrust decision from the Roberts Court.

Endnotes

[1] 549 U.S. ___ (2007) (Case No. 05-381).

[2] The others are *Bell Atlantic Corp. v. Twombly* (Case No. 05-1126), *Credit Suisse First Boston Ltd. v. Billing* (Case No. 05-1157) and *Leegin Creative Leather Products, Inc. v. PSKS, Inc.* (Case No. 06-480).

[3] 15 U.S.C. § 2.

[4] 509 U.S. 209 (1993).

[5] 509 U.S. at 222.

[6] *Confederated Tribes of Siletz Indians of Or. v. Weyerhaeuser Co.*, 411 F.3d 1030 (9th Cir. 2005).

[7] *Id.* at 1037-38.

[8] *Id.*

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