The U.S. Supreme Court Implicitly Confirms That The Measure Of Cost In Predatory Pricing Antitrust Claims Is Not Necessarily Determined At The Point When The Consumer's Participation In The Transaction Comes To An End. Instead, Defendants Can Incorporate Post-Sale Rebates From The Conspiring Supplier To The Selling Dealer

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On October 5, 2015, the U.S. Supreme Court left intact the Fifth Circuit's validation of General Motor's ingenious and creative "Bump the Competition Program." The Fifth Circuit, in *Felder's Collision Parts, Inc. v All Star Advertising Agency, Inc.*, 777 F.3d 756 (5th Cir. 2015), held that, for purposes of a predatory pricing claim under the Sherman Act, 15 U.S.C. §§ 1 and 2, a predatory competitor is entitled to factor in after-sale rebates from a conspiring supplier to show that the sale was not made below its cost. In other words, cost (whether using average variable cost or some other measure of cost), is not measured at the point when the consumer's participation in the transaction comes to an end. Instead, the measure of cost can incorporate post-sale rebates (kick-backs) from a conspiring supplier.

A. The Factual Background

The automotive replacement parts after-market is unique and interesting. Felder's, a "will-fit" replacement parts dealer, is a seller of after-market collision parts located near Baton Rouge, Louisiana. Such parts are manufactured by entities other than automobile manufacturers, such as GM, but are equivalent to original equipment manufacturer ("OEM") replacement parts, and are sold by Felder's and other after-market parts sellers to collision centers and body shops for repair of damaged automobiles.

All Star, a competitor of Felder's at the dealer level, operates several automobile dealerships that sell GM-manufactured automobiles and sells OEM parts manufactured by GM to the same collision centers and body shops to which Felder's sells its "will-fit" after-market parts. Felder's and All Star compete with each other for the sale of collision replacement parts compatible with GM vehicles.

After-market collision parts make up approximately 20% of the GM automobile collision part market. After-market "will-fit" collision parts are less expensive than OEM parts and are historically sold for prices, on average, 25% to 50% lower than equivalent OEM parts. The equivalent "will-fit" after-market parts, however, are of like grade and quality as the OEM collision parts. The remaining 80% of the automobile collision part market is already subject to a monopoly by each manufacturer as to collision parts for the cars it produces and its dealer networks sell.

Funding for the purchase of collision parts by the consumer body shops is driven in large part by the insurance industry, which often pays for the repairs of automobiles following an accident. The insurance industry demands low prices and prefers "will-fit" after-market parts given their lower price structure. Faced with a decline in sales of OEM parts for which there was an after-market part available, GM and All Star began looking for a manner to increase the sale

of OEM parts. Those efforts led to GM's creation of a program it calls "Bump the Competition."

1. GM's "Bump the Competition" Program (the "Program")

In their effort to monopolize the market for such collision parts, according to Felder's amended complaint against GM and All Star, GM and All Star conspired to design and participate in a pricing program enabling All Star to "bump" any competition from the marketplace. The "Bump the Competition" Program allegedly coerced the consumer body shops to obtain OEM parts at prices significantly below comparable "will-fit" after-market parts. Those prices, however, were below All Star's average variable cost ("AVC").

Here is how the Program works: When the consumer—a body shop or collision center—requests from All Star (or any other authorized GM dealer) a particular GM part for which there is an after-market "will-fit" part alternative, and the consumer has a quote from a "will-fit" seller of the after-market part (such as Felder's), All Star sells the OEM part to the consumer at a price *33% below the price quoted by the "will-fit" after-market seller*. That discounted price to the consumer is below All Star's AVC for that part, including the cost All Star incurs to obtain the part from GM. All Star records a loss on the part at the moment of sale to the body shop or collision center. But, sometime after the consumer's portion of the transaction is completed, All Star registers a claim with GM, and GM subsequently reimburses All Star for the difference between the price paid by the consumer and the cost of the part incurred by All Star and adds an additional 14% recoupment or kick-back.

Under these circumstances, it requires no imagination to surmise from whom the body shop consumer will purchase the equivalent after-market collision parts. It most always will be the authorized GM dealer – *i.e.,* in this case, All Star.

2. Felder's Amended Complaint Against GM's Authorized Dealer (All Star)

Felder's amended complaint articulated the specific application of the "Bump the Competition" Program: An independent GM dealer (here, All Star) incurs a cost for a particular GM OEM part of $135.01. That part is normally listed for sale by All Star to a consumer for $228.83. But, the comparable "will-fit" after-market part can be sold by an entity such as Felder's to the consumer for $179.00.

Although All Star's cost of the part is $135.01, GM instructs its authorized dealer to sell the part to the consumer for $119.93, a "bottom line price" 33% below the cost of Felder's "will-fit" after-market equivalent part and *approximately $15.00 less than the cost the dealer paid GM for the part.*

After sale of the part to the consumer for $119.93, the OEM dealership then recoups from GM at a later date the difference between the sale price of $119.93 and the part cost of $135.01, plus a back-end "profit" of 14%.

Under the scheme as alleged by Felder's, All Star allegedly is able to recoup its losses in the short-term through the back-end rebate program administered by GM, and in the long-term

through the clearing of competition from the market, allowing unfettered imposition of supra-competitive prices. According to Felder's, GM and All Star likely would recoup any losses resulting from the sale of collision parts below AVC in two ways.

First, All Star sells an OEM collision part below its AVC *only when an equivalent "will-fit" after-market part is available and documented by a quote for that part.* If there is no competing price from a "will-fit" dealer of compatible after-market part, All Star will not reduce its selling price. And, when there is no longer a viable "will-fit" after-market seller upon which to base a "Bump the Competition" claim, *All Star's existing supra-competitive price will automatically win the consumer's order because there is no competition for the anticipated sale.*

Second, GM and All Star allegedly make no effort to reduce after-market parts prices from supra-competitive levels for those parts that do not have a "will-fit" dealer after-market alternative because GM and its dealers already enjoy a monopoly on those parts, thus providing no incentive to reduce prices for their customers. *Once All Star and GM successfully "bump" all of the competition, they likewise will have no incentive to reduce prices for customers on those parts that do currently have "will-fit" after-market alternatives.* This phenomenon, then, allegedly would permit GM and All Star to achieve a monopoly on all automobile collision parts for GM. For this reason, if lawful, the Program is brilliantly conceived.

B. The District Court's Dismissal Of Felder's Claims

The District Court granted the defendants Rule 12(b)(6) motion to dismiss, concluding that Felder's had not stated a predatory pricing *claim because the back-end payments to All Star by GM must be calculated into All Star's cost,* and that doing so rendered All Star's AVC below the price of the parts sold to the consumer body shops. The District Court's decision analogized the "Bump the Competition" Program to consumer rebate cases, and rejected Felder's contention that the analytical focus of below-cost pricing should be limited to the time of sale.

C. The Fifth Circuit's Affirmance of the District Court

The Fifth Circuit also framed the issue as a "rebate" issue. In doing so, the Fifth Circuit observed that *"[t]he rebate undoubtedly affects that bottom line for All Star by guaranteeing that it makes a profit on any 'Bump the Competition' sale." Id.* at 763. That, of course, suggests that Felder's itself admittedly has been injured. But, according to the Fifth Circuit, it does not mean that *competition* has been injured. *Id.* at 756.

The Fifth Circuit held that measuring All Star's AVC at the point where the consumer's participation in the transaction ended "ignores the economic realities that govern antitrust analysis." *Id.* It reached this conclusion, by recasting All Star from the role of *competitor* into the role of "consumer," and thereby enabling it to engage in a "rebate" analysis: "In purchasing the parts from GM, All Star is a *consumer*. As it does for any consumer, a rebate reduces All Star's cost of acquiring the parts." *Id.* (emphasis added).

The Fifth Circuit confirmed that its approach involved viewing All Star as a consumer rather than a competitor, by expressly analogizing Felder's claims to the case of *Stearns Airport*

Equipment Co. v. FMC Corp., 170 F.3d 518 (5th Cir. 1999). *Stearns* looked to the predatory pricing analysis under "tying" cases (which involve buy one-get one free promotions), and observed that the Fifth Circuit had held that "it would be incorrect to look at the nominal price of the 'free' product—zero—and infer predation from this fact." *Id*. at 533 n. 15. Under this consumer-driven rebate analysis, the Fifth Circuit affirmed the District Court's dismissal of Felder's claims.

D. The U.S. Supreme Court's Denial of Felder's Certiorari Petition

On October 5, 2015, in a single sentence order, the U.S. Supreme Court denied Felder's petition for a writ of certiorari.

E. What Does *Felder's Collision Parts* Mean?

A claim for attempted monopolization under the Sherman Act requires proof of (1) predatory or anticompetitive conduct; (2) specific intent to monopolize; and (3) dangerous probability of achieving monopoly power. *Spectrum Sports, Inc. v. McQuillan,* 506 U.S. 447, 456 (1993).

Federal antitrust claims which are based on a predatory pricing theory involve a three-stage process: (1) a firm sells its products in a particular market at prices below its cost; (2) this below-cost pricing drives competitors out of that market because they cannot profitably compete; and (3) once the competitors are driven out of the market, the firm can raise its prices high enough, and long enough, to recover – or "recoup" – all of its lost revenue and make a profit. *Brooke Group Ltd. V. Brown & Williamson Tobacco Corp.,* 509 U.S. 209, 222, 224 (1993). As one court explained: "Predatory prices are an investment in a future monopoly, a sacrifice of today's profits for tomorrow's." *A.A. Poultry Farms, Inc. v. Rose Acre Farms Inc.,* 881 F.2d 1396, 1401 (7th Cir. 1989).

"That below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured: It is axiomatic that the antitrust laws were passed for 'the protection of *competition*, not *competitors*.'" *Brooke Grp.,* 509 U.S. at 224 (quoting *Brown Shoe Co. v. U.S.,* 370 U.S. 294, 320 (1962)). In predatory pricing cases, this axiom has been translated into a focus not on the impact of the pricing conduct on a particular competitor, but on the coercive effect on the consumer. Under these cases, where the lower price is due to the increased efficiencies reflected in the competitor's pricing structure, then a consumer's choice to buy the competitor's good is not "coerced"; however, these courts find that consumer coercion does take place where the lower price is below the competitor's cost.

The issue then in these types of cases is how and when a Court should measure cost. Predatory pricing occurs when a defendant "sacrifice[s] present revenues for the purpose of driving [a competitor] out of the market with the hope of recouping the losses through subsequent higher prices." *Int'l Air Indus., Inc. v Am. Excelsior Co.,* 517 F.2d 714, 723 (5th Cir. 1975). And, most courts analyze predatory pricing claims as "an attempt by the defendant to preserve or extend its monopoly power under section 2 of the Sherman Act." PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 724, at 36 (3d ed. 2008).

The most unusual feature of *Felder's* is that it would seem that a successful predatory pricing scheme, as alleged in Felder's action, *should have been primarily for the benefit of GM* by driving aftermarket equivalent parts from the market. But as the Fifth Circuit pointed out:

> Felder's has never alleged that GM is selling parts below its costs, focusing instead on allegations that GM dealer All Star is selling parts at prices below its costs. The viability of Felder's claims thus turns on whether it can show that All Star is engaged in predatory pricing at the dealer level.

Felder's Collision Parts, Inc., 777 F.3d at 760 (5th Cir. 2015).

Felder's suggests that the calculation of price or cost in a predatory pricing claim also should include economic activity that occurs *after* the consumer's participation in a transaction comes to an end. Instead, according to the Fifth Circuit (quoting the District Court), "the cost and revenue associated with a particular sale should not be dissected into pieces, but rather treated as a whole, regardless of the time associated with any discount or rebate programs." *Id.* Rejecting what is described as Felder's "freeze frame" approach, the Fifth Circuit pointedly stated that "comparing price and cost as they exist only on the day of sale ignores the economic realities that govern antitrust analysis." *Id.* at 763.

The *Felder's* opinion certainly provides yet another example of the verity that predatory pricing claims are viewed with "extreme skepticism." *Stearns Airport Equipment Co., v. FMC Corp.,* 170 F.3d 518, 527-28 (5th Cir. 1999). They are "difficult if not impossible to successfully complete and thus unlikely to be attempted by rational businessmen." *Id.* at 528. Further, "mistaken inferences . . . are especially costly, because they chill the very conduct the antitrust laws are designed to protect." *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.,* 475 U.S. 574, 594 (1986). Thus, "the standard for inferring an impermissible predatory pricing scheme is high." *Taylor Publishing Co. v. Jostens, Inc.,* 216 F.3d 465, 478 (5th Cir 2000).

At bottom, however, *Felder's* represents another illustration of the ubiquitous axiom in antitrust cases that the antitrust laws were designed "*for the protection of competition, not competitors.*" *Brown Shoe Co., v. United States,* 370 U.S. 294 (1962) (Emphasis added). And, whenever an appellate court begins its written opinion with a recitation of this antitrust axiom, lawyers immediately can sense that the antitrust plaintiff in the opinion is in trouble. Consistent with this observation, the Fifth Circuit began its *Felder's* opinion as follows: "It would not be an antitrust opinion without the line that the antitrust laws were designed for 'the protection of competition, not competitors.' Though often included by rote, the axiom is particularly apt in this case." *Felder's*, 777 F.3d at 757 (quoting *Brown Shoe Co. v. United States,* 370 U.S. 294 (1962)).

Thus, in what represents understatement in the extreme, the Fifth Circuit candidly acknowledged that "*Felder's no doubt is having a tougher time selling aftermarket equivalent parts for GM vehicles in light of GM's decision*" to implement its Bump the Competition Program. *Felders* at 764 (emphasis added). More accurately stated, it might be said that GM's

Program prevents Felder's from selling *any* GM equivalent after-market parts to body shop consumers, but still it is of no moment in the antitrust context. This is so because the antitrust laws were *not* designed for the protection of Felder's alone, and as the Fifth Circuit remonstrated, "[l]ow prices benefit consumers and are usually the product of the competitive marketplace that the antitrust laws are aimed at promoting." *Id.* at 760-61.