The Supreme Court Considers the Applicability of the "Price-Squeeze" Theory of Illegal Monopolization

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Yesterday, the United States Supreme Court heard oral arguments in Pacific Bell Telephone Co. v. linkLine Communications, Inc., No. 07-512, in which the Court may decide whether plaintiffs can state a valid claim under Section 2 of the Sherman Act by alleging "price-squeezing." Plaintiffs allege a Section 2 claim against an alleged regional telephone monopoly, which is required by federal statute to allow its competitors access to its services so its competitors can also offer competing services. Just four years ago, in Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, LLP, the Supreme Court rejected a plaintiff's similar claim that a regional monopoly's failure to provide interconnection services to its rivals was a "refusal to deal" violative of the antitrust laws not withstanding the statutory requirement to do so. 540 U.S. 398 (2004).

BACKGROUND

Plaintiffs—internet service providers ("ISPs") that sell digital subscriber line ("DSL") internet access to retail customers—purchased DSL at wholesale prices from Defendant SBC, and competed in the retail market with DSL services provided by SBC itself. Although it was required to provide wholesale DSL to Plaintiffs in a "just and reasonable" manner under the 1934 Telecommunications Act, SBC allegedly created a price squeeze by charging ISPs a high wholesale price relative to the price at which Defendant provided retail services, thus squeezing the margins with which Plaintiffs can sell DSL services. Plaintiffs allege that the price squeeze amounted to an unlawful monopolization violative of Section 2 of the Sherman Act. Defendant moved to dismiss the complaint, arguing that Plaintiffs failed to allege the elements of predatory pricing under Brooke Group Ltd. v. Brown & Williamson Tobacco Corp. necessary to support a price squeeze claim. 509 U.S. 209 (1993). Under the Brooke Group standard, Plaintiffs must allege that Defendant's pricing to the consumer is below an appropriate measure of its cost, and that Defendant has a dangerous probability of recouping the income lost by pricing below cost once it drives competitors out through its predatory low prices. The district court did not resolve this issue because, it found, the amended complaint would satisfy those requirements. Thus, the court refused to dismiss the amended complaint for failure to state a claim, but granted Defendant's motion to certify the court's order for interlocutory appeal.

The Court of Appeals for the Ninth Circuit affirmed in a divided opinion, holding that Plaintiffs stated a valid price squeezing claim. According to the court, a price squeeze occurs when a vertically integrated company sets its wholesale prices or rates at so high a level that its competitors (which purchase from it at wholesale) cannot compete with it in the retail market. The court reasoned that although SBC's wholesale activity was regulated, "there is no comparable regulatory attention paid to the retail DSL market. Any restrictions on pricing at the retail level derive primarily from the antitrust laws." The court also noted that price squeezing claims had been recognized by federal appellate courts, and had been considered good law for over six decades under Alcoa, a case decided by the Second Circuit while sitting as the Supreme Court by designation. United States v. Aluminum Co. of Am. (Alcoa), 148 F.2d 416 (2d. Cir. 1945). In Alcoa, Judge Learned Hand concluded that an aluminum monopolist acted unlawfully when it charged more than a "fair

price" for upstream aluminum products, then priced downstream aluminum products so low that competitors were unable to earn a "living profit."

Judge Gould dissented, stating that "the Supreme Court's decision in [Trinko] in essence takes the issues of wholesale pricing out of the case, and thus transforms what is left of any claim of 'price squeeze.'" What then remained was essentially a predatory pricing claim in the retail market, and thus Judge Gould would have required Plaintiffs to allege, consistent with the Brooke Group standard, "market power, below cost sales [by Defendant in the retail market], and probable potential for recoupment in the retail market." According to Judge Gould, Plaintiffs had not adequately alleged those factors, and thus their claim should have been dismissed without prejudice.

The Supreme Court granted certiorari to resolve the issue. Of note, the Ninth Circuit's decision created a Circuit split by conflicting with decisions from the D.C. Circuit and Eleventh Circuits, both of which have held that price squeeze claims can survive only by pleading facts sufficient to state a claim under the Brooke Group standard.

INTENSE AMICI INTEREST AND CONFLICT AMONG REGULATORS

Various amici curiae have filed briefs before the Court, including the Department of Justice, which argued that the Plaintiffs would have to meet the Brooke Group standard to state a claim. The Federal Trade Commission, however, issued a public statement declining to join the DOJ amicus brief, with the commissioners stating that they "disagree with the DOJ's analysis" and that "the holding of the Ninth Circuit is unquestionably correct."

In their briefing before the Supreme Court, Plaintiffs reversed their original argument that a price squeeze claim could survive without alleging the Brooke Group elements. Plaintiffs asked the Court to vacate the Ninth Circuit's decision because it was incomplete. Notably, Plaintiffs did not state that the Ninth Circuit had wrongly decided the issues; rather, the Ninth Circuit responded to a very narrow question regarding whether price squeeze claims had been completely subsumed by Trinko. Plaintiffs argued that the lower courts correctly held that price squeeze claims survived, but that the issue of whether Brooke Group applied had yet to be decided below, and was not properly before the Supreme Court.

Shortly after Plaintiffs filed their brief, amici curiae including the American Antitrust Institute ("AAI"), filed amicus briefs arguing among other things that, because Plaintiffs had abandoned their price squeeze claim, the case was moot and should be dismissed without further consideration. The Solicitor General and AAI filed motions for leave to participate in the argument as amici curiae, and the Court granted both motions.

SUMMARY OF THE ARGUMENT

Before the Supreme Court yesterday, Petitioner SBC argued that the Court should reverse the Ninth Circuit and hold that SBC had no duty under the antitrust laws to provide DSL at prices that allowed Plaintiffs a margin of profit. SBC claimed that it sold wholesale DSL services to its retail competitors only because federal statutes required it to do so, and thus it had no "antitrust duty" to deal with competitors on specific terms.

Chief Justice Roberts started by asking whether the case was properly before the Court, and Justice Ginsburg noted that Plaintiffs had requested that the Ninth Circuit decision be vacated. SBC responded by stating that amici curiae, including AAI, were capable of defending the Ninth Circuit decision, and argued that if the Court failed to reverse the decision below, nothing prevented Plaintiffs or future litigants from relying upon the Ninth Circuit's prior decision.

Justice Breyer observed that a monopolist could use upstream monopoly power to destroy competitors in downstream markets that otherwise could have expanded vertically and eventually challenged the upstream monopoly. SBC responded that forcing an upstream monopolist to share its legitimately earned monopoly profits with downstream competitors would disincentivize investment and innovation.

The United States argued that the Court should overturn the Ninth Circuit and hold that a plaintiff must meet the Brooke Group standard to allege a valid claim for price squeezing. Justice Souter asked why the Court should issue a new antitrust rule if a regulatory body such as the Federal Communications Commission could appropriately resolve the issues in the case. "[I]f . . . the FCC can act, isn't that a good reason for us not to be developing new antitrust doctrine . . . ?" The Government responded that no new doctrine was needed because current antitrust law already barred the claim.

Justice Kennedy challenged Plaintiffs' change of position, noting their brief before the Court was the first time that Plaintiffs agreed with the arguments in Judge Gould's dissent. Justice Kennedy noted that Plaintiffs had argued for the positions taken by the district court and court of appeals before, and suggested that Plaintiffs' change of position was prejudicial to SBC. Chief Justice Roberts questioned the idea that Plaintiffs' change of position should affect the Court's decision: "[T]he reason you think we should vacate is not because the Ninth Circuit didn't decide the question, but because you are willing not to press it?" Plaintiffs responded that the Ninth Circuit had not decided the question, and that they could assert a valid claim on remand under the Brooke Group standard.

Appearing in support of Petitioner as amicus curiae, AAI argued that the Court should vacate the Ninth Circuit decision and remand the case. According to AAI, the validity of past price squeeze cases was not properly before the Court, and thus the Court need not address whether those cases should be overruled. If the Court addressed the merits, however, AAI contended that the Court should uphold price squeezing as a theory of liability under traditional antirust doctrine, still valid after Trinko.

Justice Scalia challenged the idea that antitrust laws should properly apply to the facts in this case. As in Trinko, regulators here could exercise their power and prescribe prices for the upstream monopolist to set. AAI responded that here, the regulations challenged were less restrictive than in Trinko, and that in fact regulators had anticipated that antitrust law would apply.

In its brief rebuttal, SBC argued that clear rules—such as the Brooke Group standard—were essential for businesses and that lack of clarity of the rules discourages competitors from engaging in cut-throat competition, which is the ultimate objective of the antitrust laws.

IMPLICATIONS

In linkLine, the Court is set to clarify the extent to which antitrust laws apply to pricing related unilateral conduct by an alleged monopolist after Trinko. Clarification would be welcome to alleviate widespread confusion over the proper standard, as demonstrated by the present Circuit split between Ninth Circuit and the D.C. and Eleventh Circuits. The decision will follow on the heels of a line of recent opinions limiting the reach of the antitrust laws, including Weyerhaeuser v. Ross Simmons Hardwood Co., 549 U.S. 312 (2007) (limiting claims of predatory pricing), Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007) (setting a more restrictive pleading standard), Credit Suisse Securities LLC v. Billing, 127 S.Ct. 2383 (2007) (concluding that securities laws grant implied immunity from antitrust laws in some securities cases), and Leegin Creative Leather Products v. PSKS, Inc., 127 S.Ct. 2705 (2007) (overturning long-standing precedent barring vertical minimum price fixing). The Court's decision also may have implications on the proper analysis for predatory pricing, and answer some question unanswered by the Trinko and Weyerhaeuser decisions.

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