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DOJ and FTC Hold Joint Workshop to Explore Conditional Pricing Practices

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On June 23, 2014, the Federal Trade Commission and the Department of Justice hosted a day-long joint workshop, consisting of panels of economists and lawyers, to explore conditional pricing practices. Although conditional pricing practices can take a variety of forms, the primary practices explored at the workshop were single-product discounts (*e.g.*, loyalty or market share discounts) and multiproduct discounts (*e.g.*, bundled pricing).

The central question for discussion was what economic and legal test or framework should be applied to evaluate conditional pricing practices. The discussion revolved around the two analyses that traditionally have been employed to evaluate such practices. One analysis analogizes discounting to predatory price-cutting and borrows from the predatory pricing paradigm some version of the price-cost test. The reasoning is that as long as the net effective price is above some appropriate measure of cost, then the pricing practice likely reflects beneficial competition and should be deemed a "safe harbor." The other analysis focuses on whether the pricing practice raises the costs of rival firms or forecloses rival firms' ability to compete effectively. This analysis applies a traditional rule of reason framework, weighing anticompetitive effects against procompetitive efficiencies, as is often the case when examining exclusive dealing arrangements.

There appeared to be a consensus at the workshop that the ideal test or framework would be able to identify anticompetitive harm with the fewest number of false positives or false negatives in a manner that is relatively easy to administer by courts and businesses. However, there was no consensus on which test or framework comes closest to that ideal.

Nonetheless, a majority of panelists concluded that a price-cost test is not the best mechanism for assessing the legality of conditional pricing practices. One criticism was that using a price-cost test yields too many false negatives; that is, anticompetitive effects through raising rivals' costs or foreclosing rivals from the market can occur even when price is above cost. Another criticism was that the test is not as easy to administer as once thought. These panelists largely endorsed a traditional rule of reason analysis that would be more adept at considering the diversity of conditional pricing practices and their effects. Even so, many expressed a desire for some alternative safe harbors or presumptions to aid in counseling and administration.

The price-cost test, however, was not without its defenders. Proponents of some form of price-cost test argued that it protects against frivolous lawsuits, prevents the chilling of pro-competitive price-cutting, and allows for equally efficient rival firms to make sales. And both proponents and critics recognized that the judiciary has shown a preference for a price-cost test for bundled pricing and single-product discounts where price is the predominant mechanism of alleged exclusion (see *Cascade Health Solutions v. PeaceHealth* and *Eisai v. Sanofi-Aventis*).

Notwithstanding the debate over the appropriate test, there was wide agreement that unless a firm has a "dominant" market position, unilateral (as opposed to collusive) conditional pricing practices are unlikely to present a concern. Therefore, market share could serve as a potential screen for any analysis of conditional pricing practices.

Given the views expressed at the workshop and the still-evolving U.S. case law, one can expect the agencies will, as many courts have done, assess any conduct before them against both types of analyses before choosing the analysis that is most consistent with consumer welfare in that situation. For businesses and their counsel, the safest course would be to perform the same assessment until there is greater clarity in the law or from the agencies.

Putting a spotlight on these issues could mean that the agencies are keeping a watchful eye out for enforcement efforts regarding such practices, but only time will tell. For example, the DOJ has not brought a conditional pricing case since its 2011 consent with United Regional Health Care System of Wichita Falls, Texas, where the DOJ used the price-cost test to analyze contracts with insurers that led them to pay higher prices if they also contracted with a competing hospital. Even so, one can expect challenges to continue to come primarily from competitors of firms implementing conditional pricing strategies.

The agencies will be accepting public comments through August 22, 2014.[1] With so many open questions and the lack of empirical economic studies of conditional pricing practices, the agencies will welcome any and all contributions to the debate.

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1 http://www.ftc.gov/news-events/events-calendar/2014/06/conditional-pricing-practices-economic-analysis-legal-policy.

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