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"A DEFENDANT'S PARADISE": FAILINGS OF THE *BROOKE GROUP* TEST IN THE AIRLINE AND E-COMMERCE INDUSTRIES

KAITLYN THORSON*

ABSTRACT

The airline and e-commerce industries have notable and important parallels, particularly when viewed the antitrust context. Both industries are controlled by large, powerful companies operating across several markets guarded by substantial barriers to entry, which presents the opportunity for such companies to use predatory pricing to threaten—or extinguish—new and existing competition. Predatory pricing, which is prohibited by the Robinson-Patman Act and § 2 of the Sherman Act, can take different forms, but it has been defined generally as pricing goods or services below a relevant measure of cost with the dangerous probability of recouping foregone profits in the primary market.

This definition of the offense and the *Brooke Group* test derived from it have allowed companies to avoid antitrust scrutiny despite their use of predatory pricing tactics as an anticompetitive tool. Specifically, the *Brooke Group* analysis fails to properly identify cases of predatory pricing because it avoids chilling competition at the expense of allowing actual anticompetitive conduct to continue unrestrained. Since 1993, when the seminal case *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.* was decided, predatory pricing cases have been doomed from the moment the suits are filed: a vast majority of the cases are dismissed on summary judgment, and the cases that do survive motions for summary judgment are uniformly decided in favor of the defendant.

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The *Brooke Group* test largely is not equipped to detect the very conduct it was created to address. As demonstrated by the test's application in the airline and e-commerce industries, the below-cost requirement should be adjusted to allow for incremental-cost analysis where appropriate. Additionally, the recoupment prong of the test should be altered to allow plaintiffs to show that companies that incur losses in the primary market are recouping them in different markets or product lines. This change should properly balance the competing concerns of chilling legitimate, pro-competitive business practices and protecting the competitive process.

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I. INTRODUCTION

AT FIRST BLUSH, it may seem farfetched to suggest that the airline and e-commerce industries have notable and important parallels, but this truth is uniquely evident in the context of antitrust lawsuits. Importantly, both industries are primarily controlled by large, powerful companies operating across several different markets guarded by substantial barriers to entry, which presents the opportunity for such companies to use their market power to threaten—or extinguish—new and existing competition.[1] These companies have used predatory pricing, among

[1] *See* David M. Magness, Comment, *Getting Past Summary Judgment in Predatory Pricing Cases After American Airlines: Will Post-Chicago Analysis Ever Prevail?*, 5 HOUS. BUS. & TAX L.J. 424, 428, 430 (2005); Lina M. Khan, *Amazon's Antitrust Paradox*,

other strategies, to maintain their market position by driving out competition.[2] Predatory pricing, which is prohibited by the Robinson-Patman Act and the Sherman Antitrust Act, can take different forms, but it has been defined generally as pricing goods or services below the relevant measure of cost with the dangerous probability of recouping foregone profits in the primary market.[3]

This definition of the offense and the *Brooke Group* test derived from it are major reasons why companies have been able to avoid antitrust scrutiny despite years-long use of predatory pricing tactics as an anticompetitive tool. Specifically, the rule's rigid below-cost and recoupment prongs serve as a substantial barrier to plaintiffs seeking to prove that companies are, in fact, engaged in violations of United States antitrust laws.[4] Since 1993, when the seminal case *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*[5] was decided, predatory pricing cases have been doomed from the moment the suits are filed. Numerous cases have been dismissed on summary judgment, and many of the cases that do survive motions for summary judgment have been decided in favor of the defendant.[6] Astoundingly, not a single predatory pricing case has succeeded on the merits since the *Brooke Group* decision was handed down.[7]

The current antitrust framework, as articulated in *Brooke Group*, "fails to capture the architecture of market power in the twenty-first-century marketplace."[8] It repeatedly has proven to

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126 YALE L.J. 710, 716 (2017) ("It is as if Bezos charted [Amazon's] growth by first drawing a map of antitrust laws, and then devising routes to smoothly bypass them . . . . Amazon has marched toward monopoly by singing the tune of contemporary antitrust.").

[2] *See* William N. Evans & Ioannis N. Kessides, *Localized Market Power in the U.S. Airline Industry*, 75 REV. ECON. & STAT. 66, 66 (1993); Khan, *supra* note 1, at 716.

[3] *See* Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222–23 (1993).

[4] Magness, *supra* note 1, at 428–32.

[5] *Brooke Grp.*, 509 U.S. 209.

[6] C. Scott Hemphill & Philip J. Weiser, *Beyond* Brooke Group*: Bringing Reality to the Law of Predatory Pricing*, 127 YALE L.J. 2048, 2049, 2062–63 (2018) ("While it is true that no predatory pricing case . . . has been litigated to a final judgment for plaintiffs, this is not too revealing, as very few antitrust cases reach a final judgment. Numerous predatory pricing cases have survived summary judgment, while others have survived dismissal. It is likely that still other cases have settled favorably without ever leaving a notable opinion.") (footnotes omitted).

[7] *See* Patrick Bolton, Joseph F. Brodley & Michael H. Riordan, *Predatory Pricing: Strategic Theory and Legal Policy*, 88 GEO L.J. 2239, 2258–59 (2000); Magness, *supra* note 1, at 431.

[8] Khan, *supra* note 1, at 716.

be an unworkable standard in detecting and obviating predatory pricing schemes, particularly when the defendant company operates across several complex and interrelated markets.[9] Airline industry cases provide a clear example of this shortcoming and demonstrate the changes needed to curtail anticompetitive conduct effectively.[10] These cases also show that failure to implement necessary changes will likely allow antitrust violations to continue unfettered in industries with similarly complex markets, such as the e-commerce industry.[11] Furthermore, allowing these violations to continue creates poor incentives for businesses and thwarts the goals of antitrust law as a whole. In short, the overly restrictive *Brooke Group* test, with its focus on marginal cost, has created "a defendant's paradise" that rewards rather than curbs anticompetitive behavior.[12]

This Comment will begin with background on antitrust law generally and the influences that have shaped it and background on predatory pricing as a violation of § 2 of the Sherman Act. It will then explore predatory pricing in the airline industry to illustrate the exceptional difficulties imposed by the *Brooke Group* test. Next, it will compare the airline and e-commerce industries to demonstrate that suits brought against the e-commerce giants are very likely to suffer from the same fatal flaws as those brought against major airlines under current law. Finally, this Comment will propose an alternative test that will allow for proper—and necessary—enforcement of the antitrust laws.

II. THE DEVELOPMENT OF ANTITRUST LAW

The goals of early antitrust law were somewhat nebulous and ill-defined at the outset;[13] however, many scholars note that the aim of these laws centered around breaking up the trusts and cartels that threatened principles of free trade and economic liberty.[14] These trusts, powerful entities created by acquiring

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[9] *See* Bolton et al., *supra* note 7, at 2258–59; Magness, *supra* note 1, at 431, 435.

[10] *See* Hemphill & Weiser, *supra* note 6, at 2065.

[11] *See* Khan, *supra* note 1, at 717.

[12] Oliver E. Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284, 305 (1977).

[13] *See* ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 7 (1978).

[14] *See* James May, *Antitrust in the Formative Era: Political and Economic Theory in Constitutional and Antitrust Analysis*, 50 OHIO ST. L.J. 257, 288–98 (1989), *as reprinted in* C. PAUL ROGERS III & WILLIAM R. ANDERSEN, ANTITRUST LAW: POLICY AND PRACTICE 7, 7–12 (5th ed. 2020); *see also* Joshua D. Wright & Douglas H.

multiple businesses in a given industry, were formed to amass broad control of a product or service's distribution and production.[15] Similarly, producers and sellers formed cartels to control the production or price of a product.[16] The business practices of these entities were strategically adopted to establish control of market prices and the relevant market itself, which demonstrated the danger of consolidating too much power into a single entity in a given market.[17] The infamous Standard Oil Company is a classic example. Standard Oil controlled ten percent of the oil-refining industry in the U.S. when it was incorporated in 1870, but by the early 1900s, it had increased its control of the industry to approximately ninety percent.[18] Standard Oil effectuated this exponential increase in control by acquiring fourteen companies outright and majority interests in twenty-six others, all of which were then controlled through the Standard Oil Trust's board of trustees.[19] Standard Oil used its vast accumulation of market power to set supracompetitive prices in the markets it monopolized while using profits from those markets to undercut competitors' prices in remaining markets, thereby driving those competitors out of business.[20]

In response to the growing power of trusts and cartels like Standard Oil, Congress sought to protect "long-established ideals of economic opportunity, security of property, freedom of exchange, and political liberty" by regulating the formation and operation of these entities.[21] In other words, the bedrock of early antitrust law was premised on the protection of "basic economic rights and political freedom" from the trusts' growing concentration of wealth rather than economic efficiency or consumer welfare.[22] During the Sherman Act congressional debates, Senator Sherman explained that among the problems plaguing

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Ginsburg, *The Goals of Antitrust: Welfare Trumps Choice*, 81 FORDHAM L. REV. 2405, 2406 (2013).

15 *Monopolies and Trusts*, ENCYCLOPEDIA.COM, https://www.encyclopedia.com/history/encyclopedias-almanacs-transcripts-and-maps/monopolies-and-trusts [https://perma.cc/C9XF-QVYY].

16 *Cartel*, BLACK'S LAW DICTIONARY (11th ed. 2019).

17 *See* May, *supra* note 14, at 9–11.

18 Barak Orbach & Grace Campbell Rebling, *The Antitrust Curse of Bigness*, 85 S. CAL. L. REV. 605, 609–10 (2012); *see* Standard Oil Co. of New Jersey v. United States, 221 U.S. 1, 32–33 (1911).

19 Orbach & Rebling, *supra* note 18, at 610–11.

20 Khan, *supra* note 1, at 723; *Standard Oil*, 221 U.S. at 42–43.

21 May, *supra* note 14, at 7.

22 *Id.* at 8.

the "popular mind" at the time, none was more pressing than "the inequality of condition, of wealth, and opportunity that has grown within a single generation out of the concentration of capital into vast combinations to control production and trade and to break down competition."[23] He opined that, without congressional action to address the problem, "there will soon be a trust for every production and a master to fix the price for every necessity of life."[24] The Supreme Court later echoed this sentiment in the *Standard Oil* case, noting that the Sherman Act was intended to address "the widespread impression that [the trusts'] power had been and would be exerted to oppress individuals and injure the public generally."[25]

Conversely, Congress was also concerned with the Sherman Act's potential for chilling legitimate competition,[26] which is a theme that continues to influence antitrust jurisprudence today.[27] It was against this backdrop that the term "monopoly" was defined as encompassing "situations of market dominance achieved through private or governmental activity that artificially impeded free competition."[28] Early advocates of restricting anticompetitive behavior recognized that not all successful business ventures were established by utilizing anticompetitive measures and, thus, that these businesses would not be proper targets of antitrust law.[29] The view was that "a man who merely by superior skill and intelligence . . . got the whole business because nobody could do it as well as he could was not a monopolist," rather, a monopoly "involved something like the use of means which made it impossible for other persons to engage in fair competition."[30] However, these considerations were sidelined by the "big is necessarily bad" approach that permeated the debates and early interpretations of the antitrust law.[31]

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[23] 21 CONG. REC. 2460 (1890) (statement of Sen. John Sherman).

[24] *Id.*

[25] *Standard Oil*, 221 U.S. at 50.

[26] *Id.* at 90.

[27] *See* Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 223–24 (1993); United States v. AMR Corp., 335 F.3d 1109, 1116 (10th Cir. 2003).

[28] May, *supra* note 14, at 10.

[29] *Id.*

[30] 21 CONG. REC. 3152 (1890) (statement of Sen. George Hoar).

[31] ROGERS & ANDERSEN, *supra* note 14, at 29; *cf.* H.R. REP. NO. 63-627, at 19 (1914) ("The concentration of wealth, money, and property in the United States under the control and in the hands of a few individuals or great corporations has grown to such an enormous extent that unless checked it will ultimately threaten the perpetuity of our institutions."). *See generally* LOUIS D. BRANDEIS, *Shall We*

The courts began interpreting the Sherman Act provisions and their proper scope in light of these early theories and sentiments, which was no small task due to the Act's broad language and lack of clearly defined terms.[32] In *United States v. Trans-Missouri Freight Ass'n*, the Supreme Court first interpreted § 1 of the Sherman Act, which prohibits "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade."[33] The Court adopted an expansive view of Section 1, holding that the provision's key phrase "contract in restraint of trade" encompassed not only *unreasonable* restraints of trade but rather "*all* contracts . . . and no exception or limitation can be added without placing in the [A]ct that which has been omitted by [C]ongress."[34] Just one year later, the Court clarified that the effect of the *Trans-Missouri* decision was not to "render illegal most business contracts or combinations . . . because . . . they all restrain trade in some remote and indirect degree," and emphasized that such an interpretation would be "to make a most violent assumption, and one not called for or justified by the decision mentioned, or by any other decision of this court."[35]

In the landmark case *Standard Oil Co. of New Jersey v. United States*,[36] the Supreme Court began laying the groundwork for future interpretations of § 2 of the Sherman Act. Section 2 prohibits the monopolization of "any part of the trade or commerce among the several States, or with foreign nations."[37] The *Standard Oil* Court opined that Section 2 extended the reach of Section 1 to "a[ny] attempt[ ] to reach the end prohibited by the [first] section" and held that the proper determining factor in distinguishing illegal restraints of trade from valid restraints "is the rule of reason guided by the established law and by the plain

Abandon the Policy of Competition?, *in* THE CURSE OF BIGNESS: MISCELLANEOUS PAPERS OF LOUIS D. BRANDEIS 104, 114–15 (Osmond K. Fraenkel ed., 1934).

32 ROGERS & ANDERSEN, *supra* note 14, at 13 (citing WILLIAM LETWIN, LAW AND ECONOMIC POLICY IN AMERICA: THE EVOLUTION OF THE SHERMAN ANTITRUST ACT 95–99 (1965)) (noting that Congress intentionally gave deference to the courts in interpreting the Sherman Act).

33 166 U.S. 290, 312 (1897).

34 *Id.* at 328 (emphasis added).

35 United States v. Joint-Traffic Ass'n, 171 U.S. 505, 568 (1898); *see also* Anderson v. United States, 171 U.S. 604, 616 (1898) (adopting a test for illegal restraints of trade to determine whether the anticompetitive effect of the restraint was direct or "indirect and incidental"); ROGERS & ANDERSEN, *supra* note 14, at 18.

36 221 U.S. 1 (1911).

37 Sherman Antitrust Act, ch. 647, § 2, 26 Stat. 209 (current version at 15 U.S.C. § 2).

duty to enforce the prohibitions of the act and thus the public policy which its restrictions were obviously enacted to subserve."[38] The Court also emphasized the importance of "the individual right to contract, when not unduly or improperly exercised" as the most efficient check on the exercise of monopoly power.[39] Despite this recognition, the Court later continued to interpret the Sherman Act's prohibitions "so broadly that a wide range of conduct sufficed to create liability for dominant firms."[40] The expansive liability created by these overly broad interpretations, among other factors, subsequently prompted an overcorrection in the law as the Court sought to narrow the Sherman Act's reach and avoid unnecessarily punishing competitive conduct.

Competing economic theories and analyses developed by "Harvard School" and "Chicago School" scholars also heavily influenced the modern contours of antitrust policy and the practical applications of the law.[41] The Harvard School, which included scholars such as Philip Areeda, Donald Turner, and Carl Kaysen, stressed the importance of industrial organization and market structures, such as market concentration and entry barriers, as significant factors in preserving competitive markets.[42] In contrast, the Chicago School, including scholars Richard Posner and Robert Bork, emphasized consumer welfare, measured in terms of allocative and productive efficiency and viewed through the lens of price theory, as the proper goal of the antitrust laws.[43] Additionally, these scholars viewed the market structures at the center of the Harvard School's analysis as the result of firm performance rather than the cause, meaning that a given firm's dominance is more likely the result of efficient business practices rather than anticompetitive behavior

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[38] *Standard Oil*, 221 U.S. at 61–62.

[39] *Id.* at 62.

[40] William E. Kovacic, *The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Conduct: The Chicago/Harvard Double Helix*, 2007 COLUM. BUS. L. REV. 1, 17 (2007). *See generally* United States v. Aluminum Co. of Am., 148 F.2d 416 (2nd Cir. 1945); Am. Tobacco Co. v. United States, 328 U.S. 781 (1946).

[41] Kovacic, *supra* note 40, at 14–15.

[42] William G. Shepherd, *Economic Analysis to Guide Antitrust Enforcement: Prospects for Section 2*, 35 N.Y. L. SCH. L. REV. 917, 919–20 (1990); ROGERS & ANDERSEN, *supra* note 14, at 27. *See generally* CARL KAYSEN & DONALD F. TURNER, ANTITRUST POLICY: AN ECONOMIC AND LEGAL ANALYSIS (1959).

[43] ROGERS & ANDERSEN, *supra* note 14, at 27–29; Khan, *supra* note 1, at 722, 730. *See generally* BORK, *supra* note 13.

under this theory.[44] The Chicago School, in particular, had a profound influence on the development of the law during the 1960s and 1970s, as evidenced by the Court's adoption of the School's theories in pinpointing violations of the antitrust laws.[45]

III. SHERMAN ACT SECTION 2, PREDATORY PRICING, AND THE CREATION OF A "DEFENDANT'S PARADISE"

Predatory pricing is addressed both in the Robinson-Patman Act and § 2 of the Sherman Act.[46] Section 2 of the Sherman Act generally prohibits establishing, attempting to establish, or maintaining a monopoly in any part of interstate trade or commerce.[47] A successful Section 2 claim requires proof of "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of superior product, business acumen, or historic accident."[48] Specifically, the plaintiff must show that the defendant has engaged in predatory or anticompetitive conduct with the specific intent to monopolize the relevant market and a dangerous probability of achieving monopoly power.[49] In contrast, the Robinson-Patman Act's prohibitions focus on price discrimination to lessen competition substantially or create a monopoly.[50]

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[44] Shepherd, *supra* note 42, at 922–23.

[45] *See* Kovacic, *supra* note 40, at 21–26; Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U. PA. L. REV. 925, 932 (1979); *see also* Reiter v. Sonotone Corp., 442 U.S. 330, 343 (1979) (quoting BORK, *supra* note 13, at 66) (referring to the Sherman Act as a "consumer welfare prescription"); Khan, *supra* note 1, at 720–21, 721 n.39.

[46] *See* Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222 (1993).

[47] "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony . . . ." Sherman Antitrust Act, ch. 647, § 2, 26 Stat. 209 (current version at 15 U.S.C. § 2).

[48] United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

[49] *See* Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458–59 (1993).

[50] Robinson-Patman Act, 15 U.S.C. § 13(a). Price discrimination refers to "[t]he practice of offering identical or similar goods to different buyers at different prices when the costs of producing the goods are the same." *Price Discrimination*, BLACK'S LAW DICTIONARY (11th ed. 2019).

While these laws differ in some respects,[51] an important distinction between the two is that the Robinson-Patman Act only applies to commodities, not services.[52] Otherwise, certain kinds of price discrimination under the Robinson-Patman Act and violations of Section 2 generally are analyzed in the same way because "the essence of the claim under either statute is the same: A business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market."[53] With that in mind, this Comment will further analyze the various influences that have shaped Section 2 predatory pricing law over the decades.

The influence of the Harvard and Chicago Schools' competing economic theories played a pivotal role not only in the development of antitrust policy in general but also in the development of predatory pricing law.[54] From the outset, the Harvard School exerted considerable influence on courts' early attempts to distill a distinction between competitive and anticompetitive pricing.[55] As a result, "[t]he pre-1975 legal standard for predatory pricing hinged on two factors—unfair use of pricing power against new entrants or smaller firms, and protection of long run market competitiveness viewed primarily in terms of market structure."[56] Thus, the courts were focused on structural competitiveness as the goal of the Sherman Act while paying little or no attention to economic efficiency concerns.[57]

The emphasis on structural competition boiled down to two elements of the predatory pricing offense: evidence of market power in the relevant market and intent to use predatory pricing as a way to increase or maintain market power.[58] Market power, sometimes referred to as monopoly power, is defined as

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51 *Brooke Grp.*, 509 U.S. at 222 (explaining that Sherman Act Section 2 claims must meet the standard of "a dangerous probability of actual monopolization," whereas the standard under the Robinson-Patman Act requires only "'a reasonable possibility' of substantial injury to competition").

52 Robinson-Patman Act, 15 U.S.C. § 13(a).

53 *Brooke Grp.*, 509 U.S. at 222.

54 *See* Nicola Giocoli, *Games Judges Don't Play: Predatory Pricing and Strategic Reasoning in U.S. Antitrust*, 21 SUP. CT. ECON. REV. 271, 280–81 (2013).

55 *Id.* at 279–80.

56 *Id.* at 274 (citing Joseph F. Brodley & George A. Hay, *Predatory Pricing: Competing Economic Theories and the Evolution of Legal Standards*, 66 CORNELL L. REV. 738, 755–56 (1981)).

57 *Id.* (citing Brodley & Hay, *supra* note 56, at 755–56).

58 *Id.*; *see* United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

"the power to control prices or exclude competition."[59] Such market power can usually be inferred from a firm's dominant market share once the court defines the relevant market.[60] Economic considerations, such as efficiency and the relationship between price and cost, were not considered in evaluating predatory pricing complaints at the time; instead, the Court adopted a per se rule of illegality (if both of the above elements were met) that resulted in shaky and broadly drawn inferences of predatory behavior.[61] The Court defended its broad use of the per se rule by asserting that alternative, more fact-intensive approaches would "leave courts free to ramble through the wilds of economic theory."[62] Notably, the Court's reluctance to explore relevant economic theory resulted in the precise chilling effect on pro-competitive behavior that had been cautioned against for decades, as well as the law's later overcorrection to very narrow predatory pricing liability.[63]

Specifically, the Court's strict approach resulted in defendants losing predatory pricing cases roughly seventy-five percent of the time.[64] This phenomenon was met with scholarly criticism on all sides of the aisle, including Donald F. Turner and Phillip Areeda's highly influential article advocating for a new, more workable rule.[65] Areeda and Turner argued that there were two main defects in predatory pricing theory: (1) failure to clearly define what constitutes the offense; and (2) exaggerated fears that monopolists will engage in predatory pricing in the first place.[66] Ultimately, they aimed to fix these issues by proposing that courts use marginal cost as the benchmark for the "below-cost" pricing element.[67] "Marginal cost is the increment to total cost that results from producing an additional increment of out-

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59 *Grinnell*, 384 U.S. at 571 (quoting United States v. E.I. du Pont De Nemours & Co., 351 U.S. 377, 391 (1956)).

60 *Id.*

61 Giocoli, *supra* note 54, at 274–75.

62 United States v. Topco Assocs., 405 U.S. 596, 609 n.10 (1972).

63 *See id.* at 609–10; Giocoli, *supra* note 54, at 275 ("[T]he ghost of killing 'good' competition has haunted the whole history of anti-[predatory pricing] enforcement and has been the underlying argument in all of its critiques.").

64 Giocoli, *supra* note 54, at 280–81 (citing R.H. Koller II, *The Myth of Predatory Pricing: An Empirical Study*, 4 ANTITRUST L. & ECON. REV. 105, 110 (1971) (finding that 95 out of 123 federal predatory pricing cases were decided against the defendant)).

65 *See generally* Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975).

66 *Id.* at 697–98.

67 *Id.* at 702–03.

put" and is used because firms consider "incremental effects on revenues and costs" when making a profit-maximizing decision such as a price cut.[68] Thus, Areeda and Turner "concluded that marginal-cost pricing is the economically sound division between acceptable, competitive behavior and 'below-cost' predation."[69] They argued that there should be no prohibition on pricing at or above "reasonably anticipated" marginal cost because this practice leads to the proper allocation of resources and is consistent with competition on the merits.[70] However, they asserted that "the presumption of illegality for prices below both marginal and average cost should be conclusive," as neither of the aforementioned benefits arises when prices are set below marginal cost.[71]

Areeda and Turner's test ultimately replaced marginal cost with average variable cost marginal cost can be particularly difficult to define in practice and average variable cost is a close approximation that a court can more practically determine.[72] The final rule recommended that prices at or above reasonably anticipated average variable cost be "conclusively presumed lawful," while prices below reasonably anticipated average variable cost should be "conclusively presumed unlawful."[73] The Areeda-Turner test "conquered [U.S. courts] as completely as the Holy Inquisition conquered Spain."[74] Courts were eager to apply the user-friendly test to complex predatory pricing cases—most likely as a means to avoid "rambl[ing] through the wilds of economic theory"[75]—and defendants' luck began to change as a result.[76] In conjunction with that change, judicial avoidance of economic considerations had the effect not of stifling legitimate

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[68] *Id.* at 700–02 (emphasis omitted).

[69] *Id.* at 716.

[70] *Id.* at 712, 715 ("[T]o establish predatory pricing, it should be necessary to show that a monopolist has priced both below immediate marginal cost and below the marginal cost at the output which he reasonably anticipated he would attain within a reasonable period of time.").

[71] *Id.* at 713.

[72] *Id.* at 716–17, 732–33. "[A]verage variable cost is the sum of all variable costs divided by output." *Id.* at 700; *see* Giocoli, *supra* note 54, at 280.

[73] Areeda & Turner, *supra* note 65, at 733.

[74] Giocoli, *supra* note 54, at 280 (alteration in original) (citing JOHN MAYNARD KEYNES, THE GENERAL THEORY OF EMPLOYMENT, INTEREST AND MONEY 32 (1936)).

[75] United States v. Topco Assocs., 405 U.S. 596, 610 (1972).

[76] Giocoli, *supra* note 54, at 280–81 (citing Bolton et al., *supra* note 7, at 2253–54) (noting that plaintiffs lost every predatory pricing case brought between 1975 and 1980).

competition but stifling legitimate claims of anticompetitive behavior.[77]

It is for this reason that the rule was widely criticized as an over-simplification of a complex issue.[78] Scholars argued that, in practice, the Areeda-Turner test "holds dominant firm pricing per se legal,"[79] effectively making it impossible for plaintiffs to establish the elements of a predatory pricing claim.[80] Areeda and Turner were also criticized for the rule's failure to address the strategic considerations that might cause a firm to engage in predatory pricing.[81] For instance, one critique pointed out that the pair's allocative efficiency theory does not distinguish between continuous marginal cost pricing and temporary price cuts adopted for strategic purposes.[82] This is problematic for a few reasons. Marginal costs can be a poor indicator of both total and unit costs in the first place,[83] meaning that the rule designed to detect below-cost pricing may not accurately capture a firm's actual costs in some cases. Further, strategic, short-term marginal cost pricing carries negligible immediate benefits and long-run resource misallocations, which refutes Areeda and Turner's theory that "[t]he firm maximizes profit when price . . . is equal to marginal cost . . . ."[84] To illustrate, if a company temporarily cuts prices as a competitive strategy, but its customers mistakenly believe the price reduction is permanent, they may change their consumption practices and incur extra costs, resulting in negligible social benefits not captured by the rule.[85] Therefore, the rule is not properly equipped to capture the intertemporal and strategic considerations that must be considered in the predatory pricing analysis.[86]

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77 *See* Williamson, *supra* note 12, at 305 (calling the shift in predatory pricing theory "a defendant's paradise").

78 *See* F. M. Scherer, *Predatory Pricing and the Sherman Act: A Comment*, 89 HARV. L. REV. 868, 883, 890 (1976) (arguing that courts must conduct an examination of the facts of a particular case, along with intent and market structure, in determining whether a defendant is engaged in predatory pricing); Giocoli, *supra* note 54, at 282.

79 Giocoli, *supra* note 54, at 284 (quoting Brodley & Hay, *supra* note 56, at 793).

80 *See id.*

81 *See* Williamson, *supra* note 12, at 289; Giocoli, *supra* note 54, at 286.

82 Giocoli, *supra* note 54, at 289–90.

83 *Id.* at 290.

84 Areeda and Turner, *supra* note 65, at 702.

85 *See* Giocoli, *supra* note 54, at 285–86, 290–91.

86 *Id.* at 286.

Oliver Williamson, whose work exposed the rule's lack of strategic and intertemporal components, also emphasized that long-held beliefs about predatory pricing—especially the belief that the practice is irrational and unlikely to occur except in the rarest of circumstances[87]—simply did not ring true in application.[88] The crux of Williamson's argument rested on the theory that when strategic and intertemporal considerations are given the proper weight, various circumstances exist under which predatory pricing might prove to be a profitable—and rational—business decision.[89] As Richard Posner acknowledged, "[e]liminate strategic considerations, and it becomes impossible to construct a rational motivation for predatory pricing [and] . . . to ignore strategic considerations is not satisfactory."[90] Thus, a test that ignores these considerations does not allow courts adequate discretion to conduct the fact-intensive inquiry necessary to distinguish an anticompetitive pricing strategy from a pro-competitive one.[91]

Other scholars agreed that strategic considerations are crucial to the predatory pricing analysis,[92] which resulted in some courts utilizing an "Augmented Areeda-Turner Rule" approach.[93] Under the augmented rule, prices above average total cost were considered lawful, prices below average variable cost were considered unlawful, and prices between average total cost and average variable cost were presumptively lawful, subject to rebuttal evidence of predatory intent and market structure.[94] Plaintiffs in augmented-rule jurisdictions succeeded on predatory pricing claims roughly seventeen percent of the time.[95] However, the majority of federal courts largely ignored the ever-

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87 *See* BORK, *supra* note 13, at 155. *See generally* John S. McGee, *Predatory Price Cutting: The* Standard Oil (N.J.) *Case*, 1 J.L. & ECON. 137 (1958) (using empirical evidence to argue that Standard Oil was not engaged in predatory pricing practices and that a rational business would never find a price war to be a profitable strategy). McGee's empirical findings have been widely called into question. *See, e.g.*, Elizabeth Granitz & Benjamin Klein, *Monopolization by "Raising Rivals' Costs": The* Standard Oil *Case*, 39 J.L. & ECON. 1, 23 (1996).

88 Williamson, *supra* note 12, at 286–87; *see* Giocoli, *supra* note 54, at 287.

89 Williamson, *supra* note 12, at 285, 287.

90 Posner, *supra* note 45, at 939.

91 *See* Williamson, *supra* note 12, at 287–92; Giocoli, *supra* note 54, at 287.

92 Giocoli, *supra* note 54, at 288–90.

93 Bolton et al., *supra* note 7, at 2253.

94 Giocoli, *supra* note 54, at 291.

95 *Id.* (citing Bolton et al., *supra* note 7, at 2254).

increasing scholarship advocating for such an approach.[96] Similarly overlooking developments in economic theory, the Supreme Court would soon tip the balance back in favor of predatory pricing defendants.[97]

This shift began in the *Matsushita* case, where the Court embraced the importance of the price–cost relationship in the predatory pricing framework for the first time.[98] In doing so, the Court also adopted a strict evidentiary standard for these claims. In addition to showing that the defendant set its prices below its costs (i.e., that the defendant was intentionally incurring short-term losses), the plaintiffs would also need to demonstrate that the defendant would subsequently wield enough power in the relevant market to recoup those losses and gain additional profits through long-term supracompetitive pricing.[99] Although the Court had finally incorporated relevant economic concepts into its analysis, its opinion explicitly adhered to the outdated argument that predatory pricing schemes are inherently irrational, and thus "are rarely tried, and even more rarely successful," despite a growing consensus to the contrary.[100]

Matsushita set the stage for the Court's holding in *Brooke Group*, which put the proverbial nail in the coffin for plaintiffs alleging predatory pricing violations. The *Brooke Group* Court again reaffirmed that the plaintiffs must demonstrate that the prices at issue are below the defendant's costs, usually determined by some variation of the Areeda-Turner test (i.e., by comparing the allegedly predatory prices to the firm's average variable costs).[101] Interestingly, the Court declined to define the appropriate cost measure in this context because the parties had agreed to use average variable cost.[102] Thus, although the Court signaled approval of the Areeda-Turner test, it did not mandate

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96 *See generally* Chris Sagers, *"Rarely Tried, and . . . Rarely Successful": Theoretically Impossible Price Predation Among the Airlines*, 74 J. AIR L. & COM. 919 (2009).

97 *See generally id.*; Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 588–92 (1986); Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222–229 (1993).

98 *Matsushita*, 475 U.S. at 588–92.

99 *Id.*

100 *Id.* at 589 (citing BORK, *supra* note 13, at 149–55; Areeda & Turner, *supra* note 65, at 699; Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263, 268 (1981)); Sagers, *supra* note 96, at 920; Williamson, *supra* note 12, at 287–93; Posner, *supra* note 45, at 939. *See generally* Paul L. Joskow & Alvin K. Klevorick, *A Framework for Analyzing Predatory Pricing Policy*, 89 YALE L.J. 213 (1979); Brodley & Hay, *supra* note 56.

101 *Brooke Grp.*, 509 U.S. at 222. *See generally* Areeda & Turner, *supra* note 65.

102 *See Brooke Grp.*, 509 U.S. at 222 n.1.

its use.[103] The Court also rejected the theory that predatory pricing could be demonstrated by showing that a firm's prices were above its costs but below its competitor's costs or the general price levels in the market.[104] In doing so, the Court announced a general rule that above-cost pricing reflects either "the lower cost structure of the alleged predator, and so represents competition on the merits or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price cutting."[105] Of course, it may be true that above-cost pricing of this sort reflects an edge gained through efficiency and lawful competition; however, the Court's blanket rule assumes that all predatory pricing schemes take the form of an explicit below-cost price cut.[106] Williamson demonstrated that a firm could achieve the same desired end using different means.[107] For example, by building up excess capacity in anticipation of a new entrant to the market and then flooding the market's supply upon entry, a company could lower the market price enough to push the new competitor out of the market entirely.[108] The Court's fear of chilling legitimate business practices thus created a carve-out in the below-cost requirement that insulates defendants from liability.

In addition, the Supreme Court held that the plaintiffs must prove that the defendant had a dangerous probability of recouping its investment in the below-cost pricing scheme through supracompetitive profits in the relevant market.[109] The recoupment prong further breaks down into separate requirements. First, the pricing scheme must be capable of actually achieving the intended goal.[110] This analysis "requires an understanding of the extent and duration of the alleged predation, the relative financial strength of the predator and its intended victim, and their respective incentives and will."[111] Next, the plaintiffs must show that the below-cost pricing "would likely injure competi-

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[103] *See id.* at 224 (providing the Areeda and Turner's proposed below-cost rule in dicta).

[104] *Id.* at 223; *see also* Atlantic Richfield Co v. USA Petroleum Co., 495 U.S. 328, 340 (1990).

[105] *Brooke Grp.*, 509 U.S. at 223.

[106] *See id.* at 223–24.

[107] Williamson, *supra* note 12, at 335.

[108] *Id.*

[109] *Brooke Grp.*, 509 U.S. at 224; Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 588–89 (1986).

[110] *Brooke Grp.*, 509 U.S. at 225.

[111] *Id.*; *see* Areeda & Turner, *supra* note 65, at 710.

tion in the relevant market."[112] However, "[e]vidence of below-cost pricing is not alone sufficient to permit an inference of probable recoupment and injury to competition."[113] Instead, evidence of likely competitive harm "requires an estimate of the cost of the alleged predation and a close analysis of both the scheme alleged by the plaintiff and the structure and conditions of the relevant market."[114]

The Court's reasoning assumes that only successful predation schemes can be harmful, while unsuccessful schemes simply result in lower prices for consumers.[115] This analysis is flawed, or at least incomplete, for a few reasons. First, the Court's "selective evaluation of the academic literature" led it to formulate a rule that relies on controversial theories and inadequate empirical support.[116] The Court also failed to consider that failed predatory pricing schemes can still be harmful; for example, these schemes have distortive effects in the market.[117] It also did not address how it reached the conclusion that false positives in this context would chill pro-competitive pricing decisions. Importantly, experts have found that this theory does not hold water when the predation seeks primarily to exclude competitors rather than to recoup excess profits from the price cut.[118] Finally, the below-cost and recoupment tests operate in isolation rather than working in conjunction to identify violations.[119] The *Brooke Group* test as a whole would be better equipped to detect predatory pricing if evidence of recoupment informed the below-cost analysis and vice versa.[120]

The Court itself also recognized the difficulty of establishing these elements.[121] However, it emphasized that predatory pricing is a rare practice that closely mimics the lowering of prices to stimulate competition rather than injure it; therefore, drawing mistaken inferences "chill[s] the very conduct the antitrust laws are designed to protect" and justifies such a high bar to recov-

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112 *Brooke Grp.*, 509 U.S. at 225.

113 *Id.* at 226.

114 *Id.*

115 Hemphill & Weiser, *supra* note 6, at 2054.

116 *Id.* at 2053.

117 *Id.* at 2054.

118 *Id.* (citing Louis Kaplow, *Recoupment, Market Power, and Predatory Pricing*, 82 ANTITRUST L.J. 167 (2018)).

119 *See id.* at 2055.

120 *Id.* at 2055–56.

121 Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 226 (1993).

ery.[122] The Court further stated that "[i]t would be ironic indeed if the standards for predatory pricing liability were so low that antitrust suits themselves became a tool for keeping prices high."[123] The Court certainly is not wrong on this point. But its insistence on avoiding false positives at the expense of effectively barring legitimate claims produces an equally ironic result: the standards for liability are now so high that antitrust law has become a tool for protecting anticompetitive conduct.

Proponents of the *Brooke Group* test echo the Court's justifications and argue that using a more complex test would further complicate antitrust cases that, by nature, are already extremely fact-intensive and costly, both in terms of money and time.[124] Therefore, a reliable test requiring a relatively simple application allows courts to avoid "the evil committed by earlier decisions," namely, punishing pro-competitive behavior through the use of a vague and overbroad standard.[125] Again, these are certainly valid points. However, the application of the *Brooke Group* test gives broad protection to defendants where empirical evidence shows actual use of anticompetitive tactics.[126] This application unacceptably protects monopolists, harms consumers, and thwarts the goals of antitrust law as a whole. Indeed, the Sherman Act was enacted to *protect* the competitive process from anticompetitive business practices[127]—the transformation of predatory pricing law into a liability shield for businesses seeking to *destroy* competition strongly suggests that the Court's interpretations have missed the forest for the trees.

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122 *Id.*

123 *Id.* at 226–27.

124 *See* Giocoli, *supra* note 54, at 282 (discussing academia's embracement of a "meaningful and workable" test).

125 *Id.* at 283 (quoting Herbert Hovenkamp, *The Areeda-Turner Treatise in Antitrust Analysis*, 41 ANTITRUST BULL. 815, 835 (1996)); *see* Hemphill & Weiser, *supra* note 6, at 2052–53.

126 *See* James A. Brander & Anming Zhang, *Market Conduct in the Airline Industry: An Empirical Investigation*, 21 RAND J. ECON. 567, 580 (1990); Sagers, *supra* note 96, at 923–26.

127 Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993) ("The purpose of the [Sherman] Act is not to protect businesses from the working of the market; it is to protect the public from the failure of the market. The law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself.").

IV. PREDATORY PRICING IN THE AIRLINE INDUSTRY

A. Structure and Characteristics of the Airline Industry

Predatory pricing allegations in the airline industry provide a particularly illustrative case study of the failings of the *Brooke Group* test.[128] In the era following airline deregulation, fervent allegations of predatory pricing have been raised by competitors[129] and investigated by the U.S. government.[130] Some studies have even found evidence of predation among the airlines.[131] Despite this evidence, plaintiffs have been unable to prove predatory pricing violations since the adoption of the *Brooke Group* test.[132] Violations are nearly "impossible to prove without direct, smoking-gun evidence" in this context, in part because of the role of deregulation in shaping the industry's structure and characteristics.[133]

The early airline industry developed substantially under the Hoover Administration's policy of industry self-regulation.[134] At this time, the industry was also financially dependent upon federal subsidies.[135] Walter Folger Brown, then-Postmaster General, "used a broad statutory discretion to award federal mail contracts—on which the industry was then dependent for its very life—and used that discretion to force the existing major carriers to divide the country's available passenger traffic among

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128 Sagers, *supra* note 96, at 924–25 (citing *Aviation Competition Hearing: Before the Subcomm. on Aviation of the S. Comm. on Com., Sci., & Transp.*, 105th Cong. 1067 (1998) (statement of Alfred Kahn); Stephan P. Brady & William A. Cunningham, *Exploring Predatory Pricing in the Airline Industry*, Transp. J., Fall 2011, at 5). *See generally* Hemphill & Weiser, *supra* note 6.

129 Sagers, *supra* note 96, at 944 (citing *In re* Air Passenger Comput. Rsrvs. Sys. Antitrust Litig., 694 F. Supp. 1443, 1475–76 (C.D. Cal. 1988)); *see* Cont'l Airlines, Inc. v. Am. Airlines, Inc., 824 F. Supp. 689, 692–93 (S.D. Tex. 1993).

130 *See* United States v. AMR Corp., 140 F. Supp. 2d 1141, 1144 (D. Kan. 2001); Sagers, *supra* note 96, at 924 (citing Office of the Secretary, Dept. of Transp., Enforcement Policy Regarding Unfair Exclusionary Conduct in the Air Transportation Industry: Findings and Conclusions on the Economic, Policy, and Legal Issues (2001); Office of the Secretary, Dept. of Transp., Statement of the Enforcement Policy Regarding Unfair Exclusionary Conduct (1998)).

131 Sagers, *supra* note 96, at 938; Thomas Gale Moore, *U.S. Airline Deregulation: Its Effects on Passengers, Capital, and Labor*, 29 J.L. & Econ. 1, 1–2 (1986)).

132 *See* Hemphill & Weiser, *supra* note 6, at 2049, 2064–68 (discussing that the result varies from case to case); Sagers, *supra* note 96, at 922, 927.

133 Sagers, *supra* note 96, at 927, 936–44; *see* Peggy J. Hoyt, Comment, *Developing Antitrust Policy on the Internet: Lessons from the Airline Industry*, 28 Transp. L.J. 315, 315 (2001).

134 Sagers, *supra* note 96, at 936.

135 *Id.* at 936–37.

themselves."[136] These divisions were agreed to in secret, which prompted a backlash that spurred the creation of the Civil Aeronautics Board (CAB) and decreased federal subsidies to the airlines.[137] The CAB support kept airlines operating at profitable levels despite the dip in federal subsidies, and airlines came to depend on the Board's assistance to stay afloat.[138] The CAB was phased out of existence during deregulation in the late 1970s, and a new era of intense competition came about as a response to the sudden lack of federal aid that the industry had been dependent upon since its inception.[139]

During the early years of deregulation, which was undertaken to increase competition and make airline services cheaper for consumers, the industry was flooded with new entrants and aggressive competition.[140] This period was also punctuated by strategic reorganizations and acquisitions of smaller, new entrants and competitors.[141] Even major airlines, like PanAm, TWA, Eastern, and Braniff, either failed or were acquired by the surviving carriers during this time.[142] Thus, the industry's hallmark—aggressive competition—began to take hold as airlines struggled to survive in a deregulated industry.[143] However, this competition also resulted in significant cost savings for consumers and spurred the transition to the industry's hub-and-spoke structure, which remains in place today.[144] In this structure, high-traffic airports are the "hubs" where planes arrive frequently and where passengers can change planes if their flight have multiple legs.[145] The structure allows airlines to offer more frequent departure flights and increase load factors.[146] However, it also allows major airlines to exert considerable influence over the

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136 *Id.* at 936.

137 *Id.* at 937.

138 *Id.*

139 *Id.* at 937–39; Fred L. Smith, Jr. & Braden Cox, *Airline Deregulation*, LIBR. ECON. & LIBERTY, https://www.econlib.org/library/Enc/AirlineDeregulation.html [https://perma.cc/HGU9-7MYJ].

140 Sagers, *supra* note 96, at 937; *see* Hoyt, *supra* note 133, at 319–20.

141 Sagers, *supra* note 96, at 937.

142 *Id.* at 937, n.81.

143 *Id.* at 937; *see generally* Hoyt, *supra* note 133.

144 Sagers, *supra* note 96, at 938 (citing Steven A. Morrison & Clifford Winston, *Intercity Transportation Route Structures Under Deregulation: Some Assessments Motivated by the Airline Experience*, 75 AM. ECON. REV. (PAPERS & PROC.) 57, 59 (1985)).

145 *Passenger Terminal Layout and Design: Passenger Requirements*, https://www.britannica.com/technology/airport/Passenger-terminal-layout-and-design [https://perma.cc/SKT3-P4UD].

146 *Id.*

operation of hubs where they hold monopolies—often to the detriment of low-cost carriers.[147]

In the 1990s, there was a fresh wave of new entrants into the industry, primarily due to both Southwest Airlines' success as a low-cost carrier and a renewed spike in acquisition activity as the airlines navigated the end of a short period of record profitability.[148] Most new entrants failed or were acquired, sparking allegations of predation toward smaller competitors and low-cost carriers.[149] Since that time, most airline carriers have struggled to operate at profitable levels and have continued using aggressive tactics to try to counteract less-than-stellar financial performance.[150]

The structure of the deregulated airline industry and its related market characteristics—along with the substantial obstacles posed by the *Brooke Group* test[151]—have allowed major airlines to engage in predatory behavior as a means of limiting the competitive threat posed by low-cost carriers.[152] In this context, predation typically takes the form of a major airline responding to low-cost carrier entry by dropping prices and increasing capacity on the routes it monopolizes.[153] The low-cost carrier is then forced to leave the market, and the major airline is free to resume normal pricing and capacity, having displaced the other discouraged, low-cost carriers from entering the market.[154]

For starters, the industry's hub-and-spoke structure facilitates the major carriers' maintenance of market power in part because specific city-pair routes are "highly insulated from geographic competition."[155] This, in turn, creates substantial barriers to entry for small competitors seeking to establish hubs

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147 *See* Hemphill & Weiser, *supra* note 6, at 2049.

148 Sagers, *supra* note 96, at 939.

149 *Id.* at 941.

150 *See id.* at 939–40.

151 *See supra* notes 124–26 and accompanying text (providing background for the *Brooke Group* test).

152 *See* Hemphill & Weiser, *supra* note 6, at 2049.

153 *Id.*; Michael E. Levine, *Airline Competition in Deregulated Markets: Theory, Firm Strategy, and Public Policy*, 4 YALE J. ON REG. 393, 417 (1987).

154 Hemphill & Weiser, *supra* note 6, at 2049.

155 Sagers, *supra* note 96, at 948; *see* Russell A. Klingaman, *Predatory Pricing and Other Exclusionary Conduct in the Airline Industry: Is Antitrust Law the Solution?*, 4 DEPAUL BUS. L.J. 281, 282 (1992) (stating that the top five carriers transported sixty-nine percent of all passengers in 1978 and seventy-three percent of all passengers by 1990).

in markets already controlled by major airlines.[156] This structure also plays a role in the major airlines' vertical integration of regional carriers to supply additional traffic to hub networks and "to forestall the growth of would-be entrants."[157]

Other substantial barriers to entry include limited airport facilities and capacity, significant information costs, and high-fixed costs associated with industry entry and airline operation.[158] Constrained airport capacity poses an issue for new entrants because limited access to airport facilities effectively prevents them from entering the market in the first place.[159] Capacity issues are caused in part by government ownership of most commercial airports, as well as from lower consumer fares and increased air traffic prompted by deregulation.[160] However, anticompetitive behavior also perpetuates the problem. Specifically, major airlines have pressured airport operators to avoid "support[ing] needed expansion and . . . develop[ing] market-based means for apportioning facilities in a pro-competitive fashion."[161]

Branding and customer loyalty are leading drivers of high information costs because they are crucial to an airline's profitability.[162] Consumers are often ill-equipped to purchase tickets based on service quality because purchases are made before the consumer even sets foot on the plane.[163] As a result, purchases depend on "consumer confidence in reliability and safety," meaning that airlines must spend considerable resources cultivating brand recognition and customer loyalty to be profitable.[164]

High-fixed costs of operation also pose significant difficulties for new entrants and motivate the incumbent airlines to compete aggressively to maintain market power and profitability. Notably, large and small airlines alike are plagued by huge fixed costs and inefficient capital structures, due in part to the costs of

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156 Sagers, *supra* note 96, at 941; *see* Klingaman, *supra* note 155, at 288.

157 Sagers, *supra* note 96, at 944–45.

158 *Id.* at 943–44 (citing Levine, *supra* note 153, at 396); *see generally* Hoyt, *supra* note 133, at 329–43.

159 Sagers, *supra* note 96, at 943–44.

160 *Id.* at 943.

161 *Id.*

162 *Id.* at 944, 947 (citing Levine, *supra* note 153, at 426–27).

163 *Id.* at 943–44.

164 *Id.*

union contracts[165] and the fact that the cost of operating a flight is primarily fixed, regardless of whether the flight in question takes off with a full cabin or not.[166] In fact, "the only major carriers [that were] not in bankruptcy" at the end of 2005 "were American, Continental, and Southwest."[167] Thus, the dire financial straits common in the industry incentivize airlines to skirt the law to survive.

Finally, aggressive pricing tactics that shaped the industry after deregulation continue to impact the industry today. The advent of this phenomenon can be traced in part to the use of computer reservation systems (CRS) beginning in the 1970s.[168] Before these systems were made publicly accessible via the internet, CRS usage was limited to the airlines that owned them and the travel agencies that used them to book flights for customers.[169] A handful of the largest domestic carriers owned all CRS, and agencies typically used only one system, leaving smaller carriers at a significant disadvantage.[170] For example, during the 1980s, seventy percent of agencies used the systems owned by United and American, and fifty-seven percent of all tickets were sold using CRS.[171] Inevitably, the larger carriers abused CRS as an anticompetitive tool, and they "have not denied that their motive was to ensure that all passengers pay as close as possible to their maximum willingness to pay."[172]

Together, these factors make the airline industry a monopolist's dream. Empirical evidence shows that the structural components discussed facilitate predatory conduct and the maintenance of market power, as demonstrated by the "significant market share dominance" enjoyed by major airlines "on at least some routes in their hubs."[173] Other significant markers of market power include higher fares at concentrated hub airports,

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165 *Id.* at 939–40; *cf.* Delta Air Lines, Inc., Annual Report 7 (Form 10-K) (Mar. 27, 2006) (stating that several large airlines filed for bankruptcy in 2005, in part to reduce the costs of collective bargaining).

166 Sagers, *supra* note 96, at 942.

167 Paul Stephen Dempsey, *The Financial Performance of the Airline Industry Post-Deregulation*, 45 HOUS. L. REV. 421, 428 (2008); *see* Delta Air Lines, Inc., *supra* note 165, at 5 (noting that United, US Airways, and ATA Airways, among others, filed for Chapter 11 bankruptcy to reduce operating costs).

168 Aimee Minick, *Computer Reservations Systems, Airlines, and the Internet*, 65 J. AIR L. & COM. 891, 892 (2000); *see generally* Hoyt, *supra* note 133, at 329–43.

169 Levine, *supra* note 153, at 415; Minick, *supra* note 168, at 892.

170 Levine, *supra* note 153, at 415.

171 *Id.*

172 Sagers, *supra* note 96, at 942.

173 *Id.* at 945.

"oligopolistic pricing where two or more majors dominate a particular route," and price signaling between major airlines.[174] Entry barriers posed by the industry's hub-and-spoke structure also support the maintenance of market power.[175] Southwest Airlines, for example, is one of only a few low-cost carriers that have been able to effectively compete with the majors for market share at the hubs they dominate.[176] Specific city-pair routes "are also highly insulated from geographic competition . . . so airlines are well situated to practice zone pricing to limit predatory losses."[177] Furthermore, because airlines typically compete with each other in multiple markets, "[d]eveloping a reputation for predation in one market might discourage entry in others, thereby protecting excess profits in several markets with predatory losses in only one."[178] Last but certainly not least, airlines are not subject to the price discrimination restrictions in the Robinson-Patman Act because the Act applies only to sales of commodities—not services.[179] This leaves § 2 of the Sherman Act as the primary check on airline predation, which has been demonstrably problematic since the introduction of the *Brooke Group* test.

Empirical evidence shows not only that airline markets are susceptible to predatory pricing but that it takes place with regularity.[180] In fact, "[i]t is widely accepted that [low-cost carrier] entry in some airline markets draws swift and drastic incumbent price reactions, and the observed patterns of those reactions suggest predatory motives."[181] Evidence of predation is especially observable "if price-cost comparisons are made on incremental basis," because of the way airlines record this data.[182] Incremental basis tests compare the incremental increase in revenue generated by predatory increases in output to the incre-

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174 *Id.* at 945–46 (citing Severin Borenstein, *Hubs and High Fares: Dominance and Market Power in the U.S. Airline Industry*, 20 RAND J. ECON. 344, 344 (1989); Margaret A. Peteraf & Randal Reed, *Pricing and Performance in Monopoly Airline Markets*, 37 J.L. & ECON. 193, 206, 208 (1994)).

175 *See* Dempsey, *supra* note 150, at 457; Sagers, *supra* note 96, at 940.

176 *See* Dempsey, *supra* note 150, at 428; Sagers, *supra* note 96, at 939.

177 Sagers, *supra* note 96, at 948 (citing Brander & Zhang, *supra* note 126, at 571, 580).

178 *Id.*

179 Robinson-Patman Act, 15 U.S.C. § 13(a); *see* Sagers, *supra* note 96, at 942 n.104 (explaining that courts broadly hold that transportation is not a commodity).

180 *See* Brander & Zhang, *supra* note 126, at 580–82.

181 Sagers, *supra* note 96, at 948.

182 *Id.*

mental increase in costs generated only by that additional output.[183] This kind of comparison is useful in detecting predatory pricing because "[i]t will frequently be the case that capacity responses to entry that are below-cost on this incremental basis will appear to be above-cost if the comparison is made on the basis of the predator's total output in the market."[184] Two renowned economists, Joseph Stiglitz and Kenneth Elzinga, used this comparison to offer expert testimony in Section 2 cases brought against major airlines.[185] Even though this testimony showed that the prices in question were "either below cost in an absolute sense or represented a seriously anticompetitive profit sacrifice," neither court adopted the proposed tests.[186]

B. Failings of the *Brooke Group* Test in Airline Predatory Pricing Suits

Given the availability of empirical evidence showing predatory pricing in the airline industry, many have marveled at the difficulty of proving the violation in court. The root of this problem lies in the application of the *Brooke Group* test and the judiciary's unwillingness to part with the idea that predatory pricing is "rarely tried, and even more rarely successful."[187]

Several airline predatory pricing cases demonstrate the need to re-think the *Brooke Group* test. One such case is *Spirit Airlines, Inc. v. Northwest Airlines, Inc.*,[188] in which Spirit brought suit against Northwest for using anticompetitive methods to keep Spirit out of Northwest's hub in Detroit.[189] Specifically, Spirit alleged that "Northwest targeted certain of the routes on which it and Spirit competed and substantially increased capacity and began pricing below Northwest's average variable cost or its average total cost."[190] Northwest's predatory conduct included

> denying Spirit access to unused gates controlled by Northwest and/or charging Spirit unreasonable and discriminatory prices

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183 *Id.* at 948 n.134.

184 *Id.* at 948–49 n.134.

185 *Id.* at 949 & n.135.

186 *Id.* at 949; *see* United States v. AMR Corp., 335 F.3d 1109, 1116–17, 1120 (10th Cir. 2003) (rejecting all four tests proposed by the government's experts and affirming summary judgment for the defendant); Spirit Airlines, Inc. v. Nw. Airlines, Inc., 431 F.3d 917, 938 (6th Cir. 2005) (using the modified Areeda-Turner rule).

187 Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986).

188 431 F.3d 917.

189 *Id.* at 921.

190 *Id.* at 924 (emphasis omitted).

> to use those gates . . . [and] threatening to eliminate . . . discounts, promotions or other benefits to companies in the greater Detroit metropolitan area if those companies designated a carrier other than Northwest for service to or from Detroit.[191]

Spirit's entry into the Detroit–Boston market increased the route's capacity and lowered its ticket price, thereby decreasing Northwest's associated revenues.[192] Because of this, Northwest responded by "matching Spirit's $49 one-way fare, and increas[ing] capacity on the city pair."[193] The result of this scheme, coupled with a similar scheme in the Detroit–Philadelphia market, "produced the result Northwest intended when, by that start of the fourth quarter of 1996, Spirit was forced to abandon service in both city pairs."[194]

This case is notable as the only airline predatory pricing case where the plaintiffs have succeeded in any meaningful way.[195] However, this success was short-lived. The Sixth Circuit Court of Appeals reversed summary judgment for the defendant, but the parties settled out of court before the court reached the case's merits.[196] The court relied heavily on Spirit's expert testimony in reversing summary judgment, although the court did not expressly adopt the measure they proposed.[197]

Specifically, these experts advanced the use of the Elzinga-Mills test, which "describes the predator's view of below-cost pricing as 'an investment strategy'" and looks to "the profit the firm would earn if the target remained in the market" as the proper benchmark for calculating "the predator's reasonably expected gains and losses."[198] The test then breaks down into three discrete analyses, the first of which was "to compare Northwest's average fares during the months when Spirit operated its flights on the [Detroit–Boston] route to the average fares that would have prevailed on the route, but for Northwest's alleged

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191 *Id.* (emphasis omitted).

192 *Id.* at 923–24.

193 *Id.* at 924–25 (emphasis omitted).

194 *Id.* at 925 (emphasis omitted).

195 Sagers, *supra* note 96, at 953.

196 *Id.*

197 *See Spirit Airlines*, 431 F.3d at 937–46, 949–53.

198 *Id.* at 929–30; Sagers, *supra* note 96, at 955 n.167 (noting that Elzinga & Mills' work was suggested as one possible measure of recoupment that drove the reasoning in *Brooke Group*); *see* Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 226 (1993).

predation" to measure the predator's financial sacrifice.[199] The next step "compares the average fares Northwest would expect to charge, during the months immediately after Spirit exited the market, to the average fares that otherwise would have prevailed in the market" to determine the return Northwest would reap by driving Spirit out of the market.[200] Finally, the test "compare[s] the anticipated monthly sacrifice during predation with the anticipated monthly return during recoupment to understand whether predatory pricing plausibly would have been a profitable option for Northwest to exercise."[201] Using this test, Spirit's expert opined that "Northwest had successfully recouped its lost revenue within months after Spirit's departure from these routes."[202] The court agreed that even if the jury found that Northwest's prices were set above its average variable cost, "the jury must also consider the market structure . . . to determine if Northwest's deep price discounts in response to Spirit's entry and the accompanying expansion of its capacity on these routes injured competition by causing Spirit's departure from this market and allowing Northwest to recoup its losses."[203]

The court also highlighted a key issue with the *Brooke Group* test: the Areeda-Turner rule that many courts have baked into the test "is an artifact of the cost structure in the airline industry compared to conventional manufacturing plants envisioned by Areeda and Turner."[204] In other words, the test was not designed to detect predatory pricing in industries that cannot account for costs using a traditional structure. The below-cost element provides an example of the burden this imposes on plaintiffs. Airlines traditionally keep their books in a way that "facilitate[s] management decision models based on fully allocated costs," which means that plaintiffs will find it difficult, if not impossible, to distinguish fixed costs from variable costs.[205] Unless plaintiffs can do so in order to allocate an airline's costs to certain routes, the *Brooke Group* test has foreclosed claims for lack of sufficient evidence of predation.[206] However, *Spirit* dem-

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[199] *Spirit Airlines*, 431 F.3d at 929–30.
[200] *Id.* at 930.
[201] *Id.* (alteration in original).
[202] *Id.*
[203] *Id.* at 953.
[204] *Id.* at 952.
[205] Sagers, *supra* note 96, at 954; *see* Michael L. Denger & John A. Herfort, *Predatory Pricing Claims After* Brooke Group, 62 ANTITRUST L.J. 541, 548–51 (1994).
[206] Sagers, *supra* note 96, at 954.

onstrates that if courts allowed plaintiffs to prove predatory pricing based on incremental costs and associated gains, the *Brooke Group* test would capture much more of the predatory conduct occurring in the airline industry.

Another notable case demonstrating these difficulties is *United States v. AMR Corp.*, where the Department of Justice alleged that American Airlines used predatory practices to maintain a monopoly of its Dallas–Fort Worth hub.[207] The Justice Department's experts offered "an exceedingly careful, multi-part test" to show that "American's flights on the challenged routes were unprofitable" overall, and that the "costs of the incremental capacity added to combat [low-cost carrier] fares—American added substantial capacity at very low fares—outweighed the incremental revenue of that added capacity."[208] On appeal, the Tenth Circuit Court of Appeals "rejected this approach wholesale, holding that an airline plaintiff must show that flights as a whole are unprofitable."[209]

The Tenth Circuit's approach sharply contrasts with the Sixth Circuit's willingness to explore relevant market characteristics to identify predatory pricing not captured by strict interpretations of the *Brooke Group* test. The court's failure to recognize that showing "flights as a whole are unprofitable" is fundamentally incompatible with the kind of data available to plaintiffs and serves as a perfect example of the willingness to sacrifice adequate enforcement in favor of judicial economy.[210] In cases involving interrelated markets and non-traditional cost structures, courts should instead use a dynamic approach to ensure that predatory pricing schemes and anticompetitive conduct are not beyond the reproach of the antitrust laws.[211]

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207 140 F. Supp. 2d 1141, 1144 (D. Kan. 2001).

208 Sagers, *supra* note 96, at 955; *see* 140 F. Supp. 2d at 1173–74.

209 Sagers, *supra* note 96, at 955; *see* United States v. AMR Corp., 335 F.3d 1109, 1117–20 (10th Cir. 2003), *aff'g* 140 F. Supp. 2d 1141.

210 Sagers, *supra* note 96, at 955. *Compare AMR Corp.*, 335 F.3d at 1117–20, *with* Spirit Airlines, Inc. v. Nw. Airlines, Inc., 431 F.3d 917, 929–30 (6th Cir. 2005).

211 *See supra* notes 197–204, 207–209 and accompanying text; Sagers, *supra* note 96, at 955 (stating that an incremental-basis test "could properly segregate the costs because in an airline predation scheme, added capacity will be entirely or mostly in the lowest fare category.").

V. IMPLICATIONS OF AIRLINE PREDATORY PRICING JURISPRUDENCE ON THE E-COMMERCE INDUSTRY

The issues raised by *Brooke Group*'s failings in the airline industry also carry significant implications for industries with similar markets—including the e-commerce industry. The two industries share similarities in structure and market complexity that demonstrate the need to revisit the *Brooke Group* test to effectively police anticompetitive behavior. In particular, the ability of e-commerce giants, such as Amazon and Google, to engage in predatory pricing in one market and recoup those losses by exercising monopoly power in another closely mirrors the ability of airline carriers to do so in different flight markets.[212]

With the advent of a more hands-on regulation of the e-commerce giants, signified by the filing of numerous antitrust lawsuits against these companies,[213] the courts must take a more flexible approach to predatory pricing analysis. Specifically, the traditional *Brooke Group* test should be utilized on an incremental-cost basis in oligopolistic industries where individual monopolists dominate certain markets.[214]

Aggressive price competition is not normally an issue in oligopolistic industries characterized by high concentration and domination by a few firms.[215] In this context, price cuts on one company's products force the other market participants to follow suit, thereby reducing the overall market price in the industry but keeping each firm's market share at the same level.[216] This price interdependence, therefore, leads to less price competition.[217] However, this is not the case in oligopolistic industries where individual firms hold monopolies in certain markets protected by high entry barriers.[218] This kind of market struc-

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212 *See generally* Hoyt, *supra* note 133.

213 *See* STAFF OF SUBCOMM. ON ANTITRUST, COM. & ADMIN. LAW OF THE COMM. ON THE JUDICIARY, 116TH CONG., REP. ON INVESTIGATION OF COMPETITION IN DIGITAL MARKETS 6–7 (Comm. Print 2020); Rebecca Klar, *Amazon Hit with Antitrust Lawsuit Alleging E-Book Price Fixing*, THE HILL (Jan. 14, 2021, 8:56 PM), https://thehill.com/policy/technology/534364-amazon-hit-with-class-action-lawsuit-alleging-e-book-price-fixing [https://perma.cc/4MJ9-AMCK].

214 *See* Hemphill & Weiser, *supra* note 6, at 2065.

215 *See* ROGERS & ANDERSEN, *supra* note 14, at 340.

216 *Id.*

217 *Id.*

218 *See* Hemphill & Weiser, *supra* note 6, at 2065; Khan, *supra* note 1, at 745 (arguing that focusing on "competitive process and market structure" is the proper lens for analyzing competition because "the best guardian of competition

ture, which characterizes both the airline and e-commerce industries, does not fit well with *Brooke Group*'s rigid analysis and provides additional justification for amending the rule.

Several alternative approaches to the predatory pricing test have been advanced by legal and economic scholars alike,[219] but the incremental-cost tests advanced by the plaintiffs' experts in *Spirit* and *AMR Corp.*[220] appear best-suited to address the unique nature of the e-commerce and airline industries. These tests allow plaintiffs to present evidence tailored to these industries' cost and market structures, thus capturing airline and e-commerce firms' ability to selectively set predatory prices in one market while recouping those profits in a separate market.

Amazon, well-known for its success despite posting losses year after year, provides an example.[221] When the company first rolled out its Amazon Prime membership program, estimates show that Amazon was losing roughly $11 per customer per year—resulting in an estimated loss of $1 billion to $2 billion annually.[222] However, studies of the Amazon Prime program show that Prime members, who make up 47% of American consumers, "increase their purchases from Amazon by about 150%" after purchasing a membership.[223] Businesses like Target and Walmart have been unable to match these numbers,[224] which signifies that Amazon's market dominance has been spurred, at least in part, by purposely incurring losses.[225]

A more flagrant example of predatory pricing not captured by the current analytical framework is Amazon's initial "loss leading" policy in the e-book market.[226] When Amazon decided to

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is a competitive process, and whether a market is competitive is inextricably linked to . . . how that market is structured").

219 *See generally* Tom Campbell & Nirit Sandman, *A New Test for Predation: Targeting*, 52 UCLA L. Rev. 365 (2004); Richard O. Zerbe, Jr. & Donald S. Cooper, *An Empirical and Theoretical Comparison of Alternative Predation Rules*, 61 Tex. L. Rev. 655 (1982).

220 *See supra* notes 197–204, 207–209 and accompanying text.

221 Khan, *supra* note 1, at 747.

222 *Id.* at 751.

223 *Id.* at 751–52.

224 *Id.* at 752.

225 *Id.* at 753 (noting that "Amazon's dominance stems in part from its first-mover advantage as a pioneer of large-scale online commerce" but asserting that its success is due to "deeply cutting prices and investing heavily in growing its operations—both at the expense of profits" in important ways).

226 *Id.* at 756–57, 757 n.240 (first citing United States v. Apple, Inc., 952 F. Supp. 2d 638, 649–50 (S.D.N.Y. 2013); then citing George Packer, *Cheap Words*, New Yorker (Feb. 17, 2014), http://www.newyorker.com/magazine/2014/02/

enter the industry to promote its new Kindle product, it priced its e-books at $9.99.[227] This price was significantly lower than the wholesale cost incurred to purchase these books and the prices set by competitors in the e-book industry.[228] Unsurprisingly, Amazon quickly captured ninety percent of the market.[229] Several large publishers then partnered with Apple to combat Amazon's pricing strategy, resulting in the Department of Justice (DOJ) filing suit against Apple.[230] Shockingly, when confronted with arguments that it was punishing the wrong companies, the DOJ stated that there was no evidence to show that Amazon had engaged in predatory pricing.[231] Notably, the DOJ viewed the e-book business line to be profitable as a whole and did not take into account that Amazon could easily recoup its lost profits in one of several other business lines it operates.[232]

The analysis that led to the DOJ's conclusion suffers from the same flaws evident throughout predatory pricing cases in the airline industry. Specifically, the *Brooke Group* analysis fails to properly identify actual instances of predatory pricing because it avoids chilling competition at the expense of allowing actual anticompetitive conduct to continue unfettered.[233] In light of the ever-growing nature of the e-commerce industry and the empirical evidence showing that predation is going undetected, it is no longer sufficient to accept these false negatives.[234] The *Brooke Group* test itself—or its application in oligopolistic industries where monopolists control specific markets—must be changed. Allowing companies to continue engaging in predatory pricing

17/cheap-words [http://perma.cc/42AN-Y6UT]; and then citing Jeffrey A. Trachtenberg, *E-Book Sales Fall After New Amazon Contracts*, WALL ST. J. (Sept. 3, 2015), https://www.wsj.com/articles/e-book-sales-weaken-amid-higher-prices-1441307826 [https://perma.cc/TLE8-VGY6]).

227 *Id.* at 757.

228 *Id.*

229 *Id.* (citing *Apple*, 952 F. Supp. 2d at 649).

230 *Id.* at 758 (citing *Apple*, 952 F. Supp. 2d at 658–61, 681).

231 *Id.* (citing Response of Plaintiff United States to Public Comments on the Proposed Final Judgment at 21, *Apple*, 952 F. Supp. 2d 638 (No. 12-CV-2826)).

232 *Id.* at 759.

233 Hemphill & Weiser, *supra* note 6, at 2052 ("The Court's approach accepts some false negatives—anticompetitive above-cost price cuts—in order to avoid the chilling effect of false positives. Such a lenient rule, however, can be costly.").

234 Congress has also taken note of this issue and has recommended that changes be made to predatory pricing law, among other things. *See* STAFF OF SUBCOMM. ON ANTITRUST, COM. & ADMIN. LAW OF THE COMM. ON THE JUDICIARY, 116TH CONG., REP. ON INVESTIGATION OF COMPETITION IN DIGITAL MARKETS 19–21 (Comm. Print 2020) (identifying a broad set of reforms for further examination by the Members of the Subcomittee to consider given the digital economy).

without appropriate enforcement of the antitrust laws creates poor incentives for large, powerful companies and thwarts the goals of antitrust law as a whole.

VI. CONCLUSION

The *Brooke Group* test has proven to be an unworkable standard not equipped to detect the very conduct it was created to address. As demonstrated by the test's application in the airline and e-commerce industries, the below-cost requirement should be adjusted to allow for incremental-cost analysis where appropriate. Additionally, the recoupment prong of the test should be altered to enable plaintiffs to show that companies that incur losses in the primary market are recouping the losses in different markets or product lines. This change would adequately balance the competing concerns of chilling legitimate, pro-competitive business practices and protecting the competitive process.