Bundled Pricing and Antitrust

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Turning the Page on *LePage's*? Recent Developments in Bundled Pricing and Exclusive Dealing

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Bundled Pricing

- Discounts conditioned on buyer's agreement to purchase two or more products from the seller
- Pervasive in our economy
  - *Buyers expect to pay less if they purchase multiple products*
- Generally a means of price competition, with corresponding benefits to consumers

Antitrust Objections to Bundling

- Bundling can deprive equally or more efficient single-product rivals of the volume needed for economies of scale, weakening their ability to constrain the multiple-product defendant's market power
- Consumers are harmed by the potential reduction of competition in the competitive product market, and by the reinforcement of (or increase in) barriers to entry in the monopoly product market.
- Bundling has aspects of, but is different from -
  - *Predatory pricing*
  - *Tying*
  - *Exclusive dealing*
- Very few efficiencies associated with bundling
  - *Plenty of efficiencies from package sales, but conditioned discounts are not needed to realize these efficiencies*

Approaches to Bundling

- *LePage's*: Bundling by a monopolist that single-product rivals cannot match may be condemned
- Consumer welfare effects: Bundling is anticompetitive and unlawful where the effect is to raise prices or otherwise harm consumers
- Telecom-promoted: Bundling is unlawful only where the total price for all products in the bundle is below the incremental cost of all products in the bundle

Approaches to Bundling

AMC 3-part test; to be unlawful all 3 must be met:

1. After allocating all discounts and rebates attributable to the entire bundle of products to the competitive product, the defendant sold the competitive product below its incremental cost for the competitive product;
2. The defendant is likely to recoup these short-tem losses; and
3. The bundled discount or rebate program has had or is likely to have an adverse effect on competition.

PeaceHealth Case

- Plaintiff (McKenzie), with one hospital, and Defendant (PeaceHealth), with three, were the only hospitals in Lane County Oregon
- PeaceHealth offered primary, secondary, and tertiary care; McKenzie just primary and secondary
- PeaceHealth offered additional discounts to insurers of up to 35%-40% if the insurer made PeaceHealth the only preferred provider for primary, secondary, and tertiary care
- Trial court charged jury under the *LePage's* approach; it could find PeaceHealth liable if its discounts "substantially foreclose portions of the market to a competitor who does not provide an equally diverse set of services and who therefore cannot make a comparable offer."
- Judgment of $16.2 million after trebling

PeaceHealth Case

- Central issue was whether to follow *LePage's,* and court took unusual step of reaching out for amicus briefs
- Court rejected the *LePage's* standard as too vague; the loose standard of *LePage's* posed a threat to legitimate package discounts
- Court also rejected the so-called "full *Brooke Group*" approach urged by the telecoms as amici, under which the bundled pricing would be legal absent proof that the total price for all products in the bundle was below the incremental cost of all products
  - *That test renders the bundling aspect of the conduct irrelevant*
- Instead, the Court adopted the "discount attribution" test, largely in a manner consistent with the proposal of the Antitrust Modernization Commission and the writings of Professor Hovenkamp and Judge Posner

Discount Attribution Test

- Asks whether "after allocating all discounts and rebates attributable to the entire bundle of products to the competitive product, the defendant sold the competitive product below its incremental cost for the competitive product."
- In addition to satisfying this requirement, 9th Circuit agrees that a plaintiff also must show what the court called "antitrust injury," by which the court meant an actual or probable adverse effect on competition.
- Those are two of the elements of the three-part test urged by the Antitrust Modernization Commission.
  - *The AMC also included a further requirement of limited "recoupment," but, given the brief and cryptic explanation by the AMC Report, the PeaceHealth court did not understand and thus rejected that requirement.*

Discount Attribution Test

- The 9th Circuit's variant of the discount attribution test provides at least some guidance for firms in business operations and a basis for counseling
  - *Calculation of the attributed discount, at least in an approximate amount, should be straightforward in most instances, allowing businesses to price without undue fear of legal repercussions*
  - *Even if a bundled discount fails to the discount attribution safe harbor, it will not be condemned absent what the court called "antitrust injury"*
    - Better phrasing would be "harm to competition"
- Alternative rules are either unacceptably vague and overbroad (*LePage's*) or unacceptably narrow (the "full *Brooke Group*" variety of per se legality)