GCR NEWS
GLOBAL COMPETITION REVIEW

Wright: FTC should view loyalty discounts as exclusion

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4 June 2013


Joshua Wright

The US Federal Trade Commission should consistently view loyalty discounts between suppliers and retailers as a kind of exclusive dealing and not as predatory pricing, which requires a more problematic test to prove, FTC commissioner Joshua Wright said.

Loyalty discounts are among the most common methods of competition between suppliers in industries from airlines to health care, Wright said. The antitrust agencies have long been concerned by the potential competitive pitfalls of such agreements, in which a supplier of a product agrees to give a significant discount to a retailer as long as the retailer satisfies certain thresholds of sales of that product.

Agencies are concerned, he said, that a monopolist might use the discounts to protect its market position by stifling its rivals' access to retailers – raising rivals' costs and ultimately harming consumers. Wright said that such deals should be viewed as a form of exclusive dealing, in which the supplier requires a retailer or distributor to stock and sell a significant – but less than 100 per cent – share of its product.

Speaking at the annual Bates White antitrust conference yesterday, Wright spoke at length about his views of loyalty discounts – how they should be analysed, and, moreover, how courts and antitrust enforcers should view the potential for such discounts to help or harm competition.

In his view, anti-competitive examples of loyalty discounts are tantamount to exclusion – by pressuring downstream sellers of a product to shut out the rivals of a supplier with significant market power – but do not necessarily involve predatory pricing, or the price-cost test that proving it requires.

"The key economic point is that the antitrust concerns potentially arising from loyalty discounts involve anti-competitive exclusion rather than predatory pricing," Wright said, adding that such discounts are best understood when viewed through the lens of modern antitrust literature about raising a rival's costs.

According to that literature, he says, for an agency to find that a loyalty discount violated the antitrust laws generally requires "strict assumptions concerning the existence of significant economies of scale, barriers to entry, and the absence of pro-competitive efficiencies".

However, loyalty discounts often include those pro-competitive efficiencies, he said, including minimising the possibility that a distributor could use one supplier's deep investments to promote a rival supplier's products, as well as intensifying competition between suppliers to win access to distributors' customers.

While some commentators say the law should evaluate the competitive benefits or harm of such discounts the same way it evaluates other discount-based claims – by requiring proof of below-cost pricing – any antitrust concerns about loyalty discounts are actually concerns about exclusion, and "as a result, the legal framework developed to evaluate exclusive dealing claims ought to be used to evaluate claims relating to loyalty discounts," Wright says.

The question remains as to how the FTC looks as such deals, he says, but recent cases suggest that the FTC "appears more likely to adopt an exclusion framework than a price predation framework in its analysis of loyalty discounts".

However, he says, two cases – the FTC's case against McCormick in 2000 and its investigation of Church & Dwight – suggest practitioners should be cautious in believing the FTC will apply an exclusionary approach to loyalty discounts generally.

In response to questions after his speech, Wright stressed that he did not necessarily support a legal theory that loyalty discounts are likely to violate the antitrust laws. And while there is empirical data showing that exclusion does happen in loyalty discounts, it does not appear to happen often.

First published on the *Global Competition Review* website, 4 June 2013
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