Loyalty Discounts and the Hospitability Tradition

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The Hospitability Tradition for Unilateral Price Discounts

- "Low prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition." *Atlantic Richfield v. USA Petroleum* (S. Ct. 1990)
- "Rewarding customer loyalty promotes competition on the merits." *Virgin Atlantic v. BA* (2001)

Road Map

- Market share discounts are often client-driven
- Market share discounts have procompetitive advantages over volume discounts
- Market share discounts should presumed to be true discounts
- Foreclosure claims should require objective economic evidence that the rival could not profitably compete

Customer-Driven

- Collective action problems may drive customers to demand anticompetitive terms
- But less plausible where customers are large and sophisticated

Example: GSA City Pair Airline Contracts

- “GSA concentrates on the government's market share to make the most of the competition available. The government traveler's responsibility is to use the contract carrier. The government's delivery of market share drives the program. So, to ensure the fares stay favorable, we encourage federal travelers to use the contract carrier.”
  - http://www.gsa.gov/portal/content/103835

Advantages over Volume Discounts

- Shift risks from buyers to sellers
- Enable sellers to plan for minimum sales level even in volatile market
  - Example: 5 large buyers compete in market with volatile market shares. If each buys 80% of requirements from supplier, supplier will sell1,000 units regardless of distribution of purchases among the buyers.
- Allow smaller buyers to obtain discounts

Presumptively true discounts

- Penalty theory: monopolist raises price above monopoly level and grants discount back to monopoly level with loyalty condition.
- Problem: Monopolist exceeds monopoly profit-maximizing price, either at penalty price or monopoly price + new restriction.
- Implications:
  – True discounts should be treated with hospitability
  – If exclusionary, look for evidence of recoupment
  – Foreclosure requires profit sacrifice

Prove Foreclosure, Don't Assume It

- If a rival can profitably match a loyalty discount, it is not foreclosed.
- Hence, a minimum showing that rival cannot profitably match is required.
- Otherwise, foreclosure is a vacuous concept.
- "Condition" where consequence is change in price *is a price!*
  - 10% loyalty reward = 10% disloyalty penalty

Unstructured Rule of Reason:

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