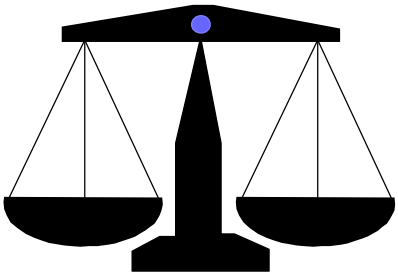

General Counsel Corner

By Peter H. Gunst, Esquire

New Developments in Below-Cost Pricing Law

In the past few years, below-cost pricing laws have become increasingly popular as a defense against the deep discount and "loss leader" strategies employed by many hypermarket and unbranded competitors.

These statutes, enacted in many states, generally contain some criterion for establishing what constitutes a below-cost price, and typically create a judicial inference that any price below the statutory norm either is intended or has the effect of restraining competition or injuring a direct competitor.

Unless the price-cutter can rebut the inference (which is not easy to do) or demonstrate that it was merely meeting competition in the market, it may be held liable for damages or be subject to an injunction prohibiting further misconduct.

As lawsuits under these statutes become more common, courts are being presented with interesting issues concerning their impact and interpretation. Decisions issued by the South Carolina Supreme Court late last October and by the Wisconsin Court of Appeals last November are worth noting.

In *R. L. Jordan Oil v. Boardman Petroleum*, competing convenience store operators had engaged in a price war. One sold branded Citgo gasoline, the other was unbranded.

A pattern developed: the unbranded operator would reduce its prices to establish the traditional two-cent differential between branded and unbranded product. The branded operator would then reduce its prices to match the unbranded, and thereby wipe out the historic differential. And so prices would spiral downward, until both marketers were selling below cost.

The branded operator — which actually reached below-cost pricing levels first because it paid more for product than its unbranded competitor — sued its rival for below-cost selling in violation of §39-5-325(A) of the South Carolina Unfair Trade Practices Act.

The unbranded operator defended by asserting a meeting competition defense, arguing that it had done nothing more than preserve the historic differential between branded and unbranded gasoline long recognized throughout the market.

The South Carolina Supreme Court rejected the defense. It emphasized that the state below-cost sales law had to be read literally, and that it only provided for the reduction of prices to meet "existing competition." That meant merely meeting a competitor's price, and not reducing prices to a still lower level.

No reason existed to provide any further relief to an unbranded marketer, the South Carolina Supreme Court concluded. Because unbranded competitors normally possess the advantage of paying less for petroleum products than do their branded rivals, they normally are able to establish legally lower prices than their competitors.

It is only when a branded competitor meets the unbranded marketer's lowest legal price that the unbranded marketer cannot legally respond with a further price reduction.

In that situation, the statute provides no defense. As the South Carolina Supreme Court concluded, "[t]here is no support for the argument the legislature intended to protect independent gasoline retailers over retailers selling national brands."

In *Gross v. Woodman's Food Market,* a branded convenience store operator obtained summary judgment against his unbranded competitor, which had sold gasoline and diesel fuel at below-cost prices, as calculated under §100.30 of Wisconsin's Unfair Sales Act. The branded operator was awarded statutory damages of $2,000 per day for each of the 295 days on which the unbranded marketer sold any product below the statutory standard, for total damages of $590,000.

The unbranded marketer appealed, arguing among other things that it was merely meeting competition and that its low diesel fuel prices could not conceivably have adversely impacted its branded competitor.

The unbranded marketer lost on appeal. Its meeting competition defense with respect to its pricing of gasoline failed because it had only documented when it matched low competitive prices with respect to regular gasoline.

That showing, according to the Wisconsin Court of Appeals, did not explain "why the price for mid-grade gasoline was set below the statutory minimum price." The court emphasized that "the exception must be established for each grade of fuel [the defendant] sells."

With respect to its pricing of diesel fuel, the unbranded marketer argued that its market presence was so slight that it could not conceivably have impacted the plaintiff's competitive sales.

The unbranded marketer emphasized that most of its diesel fuel was used to supply its own vehicles; that it did not advertise diesel fuel; that its diesel fuel price could not be seen from the road; and that the location of its diesel pump was so inconvenient that a semi-truck could not use it unless it first dropped its trailer at another location.

Still the defense failed. Although the branded operator could not show that he had actually lost sales as a result of his competitor's below-cost diesel fuel sales, he had averred without contradiction that he had been forced to take the defendant's below-cost pricing of diesel fuel into account in making his own pricing decisions, with the result that he had been injured through the overall decline in his own profit margin.

The Wisconsin court agreed, finding the evidence sufficient to support the conclusion that the plaintiff had been "injured by losing profits from setting his prices, including diesel, lower to compete with [the defendant's] prices."

The court's holding seems extreme. If the unbranded marketer's diesel fuel sales were as inconsequential as they appeared to be, how could the plaintiff have *reasonably* reduced his prices in response to what appeared to be a non-existent competitive threat? One would think that the issue of the reasonableness of the plaintiff's pricing

decisions should have been left to the jury, and should not have been decided on summary judgment.

In any event, these decisions show that below-cost pricing statutes are being utilized and rigorously enforced.

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