View metadata, citation and similar papers at core.ac.uk
brought to you by CORE
provided by Biblioteca Digital Jurídica do Superior Tribunal de Justiça

Prêmio IBRAC-TIM 2016 – 2.º Colocado Categoria Pós-Graduação

THE APPROACH OF ANTITRUST LAW TOWARD EXCESSIVE PRICING: A MATTER OF POLICY OR FAIRNESS?

Aplicação da lei concorrencial com relação a preços excessivos: uma questão de política antitruste ou equidade?

Ricardo Villela Mafra Alves da Silva

Abstract: This essay analyzes the approach of antitrust law toward excessive pricing, inquiring whether antitrust law should be enforced against excessive pricing as a matter of policy and/or fairness. Upon examination of basic concepts of price theory to explain why price matters, and brief review of literature regarding criteria to define excessive pricing, this essay concludes that excessive pricing should not be subject to prosecution as a matter of policy, but abusive pricing should be subject to prosecution as a matter of fairness, provided that the firm has significant market power and faces an inelastic demand curve.

Key words: antitrust policy; excessive pricing; abusive pricing; price theory; fairness.

Resumo: Este trabalho analisa a aplicação da lei concorrencial com relação a preços excessivos, questionando se a lei concorrencial deve ser aplicada contra preços excessivos por questões de política pública e/ou equidade. Mediante estudo de conceitos básicos de teoria do preço para explicar por que preços importam e breve revisão de doutrina sobre critérios para definir preços excessivos, conclui-se que preços excessivos não devem ser objeto de preocupação por questões de política pública, enquanto que preços abusivos devem ser objeto de preocupação por questões de equidade, contanto que o agente tenha poder de mercado significativo e encare demanda inelástica.

Palavras-chave: política antitruste; preço excessivo; preço abusivo; teoria do preço; equidade.

Introduction

In every jurisdiction that has passed antitrust laws, authorities have struggled, at some point, with the following question: should the antitrust laws be enforced against excessive pricing?

As noted by Frederick Abbott, such question denotes a paradox in antitrust policy, to the extent that many experts agree that one of the main objectives of antitrust law is, precisely, "to protect consumers against the charging of excessive prices"[1].

The treatment of excessive pricing remains, to this date, one of the most challenging issues of antitrust enforcement. On the one hand, there are numerous policy questions that must be addressed. How to determine when a price is excessive? Should there be a differentiation between excessive and abusive price? If a price is deemed excessive, can the antitrust authority determine what the fair price should be? If so, are there instruments or methods that enforcers may use to set forth the fair price?

One the other hand, there are fairness arguments in favor of enforcement against excessive pricing, especially when the product in question is deemed essential (*e.g.*, medicine). Should antitrust allow dominant firms to exploit consumers by charging excessive pricing? Is it fair to leave consumers unassisted when they are unable to acquire essential goods due to excessive pricing?

Enforcers have generally refrained from applying antitrust law directly against excessive pricing[2], "even though it is the incipient threat of future 'excessive' prices that motivates enforcement action against exclusionary behavior and cartels"[3].

In Brazil, the issue was addressed by Carlos Ragazzo, who argues that antitrust should fight the causes of the excessive pricing, and not the excessive pricing itself[4].

---

[1] ABBOTT, Frederick M. Excessive pharmaceutical prices and competition law: doctrinal development to protect public health. Available at <http://ssrn.com/abstract=2719095>. Accessed on August 27, 2016. p. 2.

[2] ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT. Excessive prices. Available at <http://www.oecd.org/competition/abuse/49604207.pdf>. Accessed on August 27, 2016. p. 2.

[3] Ibid. p. 2.

[4] RAGAZZO, Carlos Emmanuel Joppert. Preço abusivo, eficácia jurídica e análise econômica: afinal, onde está a cabeça de bacalhau? Revista do IBRAC, v. 18, p. 21-43,

Notwithstanding, the issue will inevitably reemerge from time to time, and it is reasonable to assume that, sooner or later, the Administrative Council for Economic Defese ("Cade") will be required to take a firm stance regarding the treatment of excessive pricing. For example, the excessive pricing debate returned to the spotlight when, in the end of 2015, when the price of the drug Daraprim, used for treating life-threatening infection, rose from US$13,50 to US$750,00, following the acquisition of the drug's intellectual property by a firm[5].

The matter at hand is not an easy one, so this brief essay does not have the intention of providing all the answers for the daunting problem. Therefore, we will limit our subject to the following questions: (i) whether antitrust authorities should fight excessive pricing as a matter of policy; and (ii) whether antitrust authorities should fight excessive pricing as a matter of fairness.

The first section of this essay will address the importance of price in a capitalist economy and how price variations affect welfare. A few basic concepts developed by price theory, that are useful for the issues discussed herein, will be explained.

The second section will provide a brief overview two of the main problems faced by antitrust authorities when dealing with excessive pricing: where exactly to draw the line between fair and excessive prices and what are the implications of such issue.

The third section will set forth a proposal to deal with excessive pricing. The proposal will be based on the idea that should be a differentiation between excessive pricing and abusive pricing. Thus, we will argue that excessive pricing should not be prosecuted by antitrust authorities as a matter of policy, whereas abusive pricing should be fought by antitrust authorities as

---

2011. Frederick M. Abbott criticizes such solutions, denominated by him as the "fixing the market" alternative. "There is a fundamental problem with the 'fixing the market' approach when addressing products protected by legislatively authorized market exclusivity mechanisms such as patents and regulatory marketing exclusivity. That is, mechanical aspects of the market are not broken in the conventional antitrust sense. Rather, the market has been designed without adequate control mechanisms or 'limiters' that act to constrain exploitive behavior. Political institutions, such as legislatures, that might step in are constrained by political economy (e.g., lobbying), and do not respond as they should" (ABBOTT, Frederick M. Excessive pharmaceutical… p. 2).

[5] POLLACK, Andrew. Drug goes from $13.50 a tablet to $750, overnight. The New York Times, New York, 20 Sept. 2015. Available at <http://www.nytimes.com/2015/09/21/business/a-huge-overnight-increase-in-a-drugs-price-raises-protests.html?_r=0>. Accessed on August 27, 2016.

a matter of fairness. Accordingly, a few possibilities will be discussed about how to define abusive pricing.

1. Why does price matter?

Price is one of the most important (if not the most important) variable in a healthy capitalist market. Its main function is to show both to consumers and producers how much quantity of a certain good or service is desired[6]. Thus, price allows market participants to allocate scarce resources in the most efficient manner.

From a social perspective, price has an additional meaning: it limits access to products. Expensive products are accessible to a small percentage of society, while cheap products are accessible to a larger group of people.

The difference between how price is understood from a social and economic point of view leads to situations where high prices may be deemed unfair from a social perspective, but not from an economic perspective.

But economics does not forgo the social impact of high prices altogether. It deals with the social issue arising from high prices by showing that a loss of welfare occurs whenever prices go up. In this context, it is said that a deadweight loss occurs whenever firms restrict output and extract rents from consumers.

As explained by Posner, the deadweight loss is the loss suffered by society as a result of a price increase, which is not offset by the rent transferred to the firm by consumers[7].

---

[6] For the sake of simplicity, "product" will be used hereinafter to mean both goods and services.

[7] POSNER, Richard. The social costs of monopoly and regulation. The Journal of Political Economy, Chicago, vol. 83, pp. 807-828, 1975. pp. 807-809.

Figure 1 - Deadweight loss representation[8]

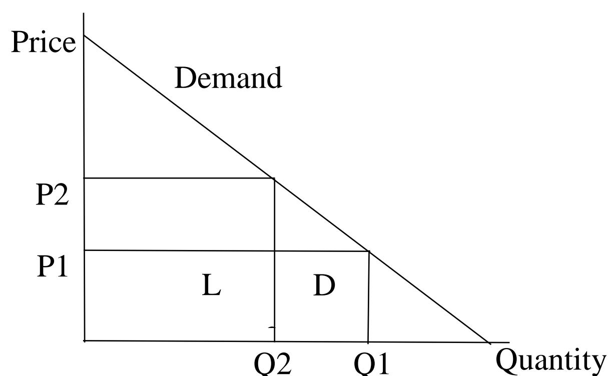

Figure 1 shows the graphic representation of the deadweight loss generated by a price raising from P1 to P2, and a consequent restriction of output from Q1 to Q2. The area comprising L and D represents the loss yielded by the price raise. The square area marked as L is equivalent to the transfer of rent from consumers to the firm; in other words, it represents a loss of wealth by consumers, which is offset by a gain of wealth by the firm[9]. The triangle D, by its turn, represents the loss of wealth that is not rent transferred from consumers to the firm. In other words, area D is equivalent to the loss of wealth of non-consumers of the product in question, that now will be unable (or unwilling) to acquire it. It is a loss shared by all society and is not offset by a gain of wealth by the firm, which is why it is generally denominated as a deadweight[10].

---

[8] See original in Ibid. p. 808.

[9] It must be said that such offsetting is not deemed neutral from a welfare perspective by antitrust enforcers in most jurisdiction, since it is purely a transfer of rent. Williamson has proposed a more detailed tradeoff model specifying which type of welfare gains might be taken into account to offset a loss generated by a price raise. See WILLIAMSON, Oliver E. Economies as an antitrust defense: The Welfare Tradeoffs. The American Economic Review, Pittsburgh, Vol. 58, pp. 18-36, 1966; WILLIAMSON, Oliver E. Economies as an antitrust defense revisited. The University of Pennsylvania Law Review, Philadelphia, Vol. 125, pp. 699-736, 1977.

[10] The explanation of the deadweight loss graphical representation is derived from basic principles of price theory and it has been set forth by many economists. Notwithstanding, many of these assumptions and more sophisticated models based on such assumptions may be found in POSNER, Richard. The social costs of monopoly and regulation. The Journal of Political Economy, Chicago, vol. 83, pp. 807-828, 1975.

The deadweight loss, therefore, is the closest economic representation of the main social issue generated by high prices: it excludes a certain number of people from the market. In theory, the larger the triangle D, the higher the number of people who are kept from consuming the product in question.

The exclusion of consumers from market and loss of welfare are the reason why one of the main concerns of antitrust is keeping prices at the lowest levels possible[11] (together with increasing product quality and innovation).

Price theory can also demonstrate how valuable a product is not only by pointing out its demand curve, but also by showing how rigidly demand reacts to a price raise. The degree to which demand reacts to changes in price is called elasticity. If, as a result of a price increase, there is a proportionately small decrease in demand, it is said that the demand curve is inelastic. If, however, there is a proportionately large decrease in demand in response to a price increase, the demand is deemed elastic.

An inelastic demand occurs when the product in question does not have close substitutes and it is somehow essential to consumers. Medicines, for example, will probably have an inelastic demand if they are essential and have no close substitutes. In those cases, the consumer is "locked" to the product, and even substantial increases in price might not be sufficient to lower demand[12].

---

[11] The lowest level that a firm can set its price, according to price theory, is where demand curve intersects with the firm's marginal cost curve. Below that point, firms would be offering their products at a loss, which would not be a rational economic behavior. However, this would only occur in perfectly competitive markets, which is rarely the case. This is why we state that antitrust seeks to keep prices as low as possible under given market circumstances, which is not to say that the lowest level possible cannot be substantially above the firm's marginal cost. Even though this affirmation may be unsettling to some antitrust scholars and practitioners, we believe that stating the opposite would be clearly wrong (e.g., "keeping prices at the lowest levels possible is not among the main concerns of antitrust policy"). In that context, there are arguments in favor of choosing consumer surplus (which is a result of low prices) as a priority of antitrust policy. See, for example, Russell Pittman argument in favor of consumer's surplus as the main antitrust standard in the analysis of mergers. PITTMAN, Russell. Consumer Surplus as the Appropriate Standard for Antitrust Enforcement. Available at <http://ssrn.com/abstract=996643>. Accessed on September 15, 2016. pp. 12-13.

[12] "As a monopolist or as a potential cartelist, you would like to be facing a demand curve that is inelastic above the competitive price. That means that it will be really profitable to raise prices to the monopoly level because the industry will not lose many sales but will get higher prices for what is sold". See GRADY, Mark F. Cases and materials on antitrust. Los Angeles [s.n.], 2016. 1074 p. p. 18.

The implications of low elasticity are not ignored by antitrust authorities. The Horizontal Merger Guidelines of the U.S. Federal Trade Commission and Department of Justice, for example, determines that restriction of output is more likely to occur as a result of a merger if: (i) the resulting firm has relatively high market share; (ii) the output of the firm already committed to price levels prior to the price increase is relatively low; (iii) the margin of the suppressed output is relatively low; (iv) response of rivals to the restriction of output is not significant; and (v) the market elasticity of demand is low[13].

Low elasticity of demand, therefore, is a strong indication that the product is somehow essential to consumers[14] and there are no viable options (*i.e.*, close substitutes) available in case of a price increase.

Therefore, it might be said – especially from a social, if not economical, perspective – that price increases are more harmful in case of products with inelastic demand. People who need the product will be forced to transfer a bigger share of their wealth to the dominant firm, otherwise they will not be able to acquire the quantity that they need.

If the demand is elastic, price increases would have little effect on welfare (even though there would still be a deadweight loss), since consumers would simply be able to switch to a substitute product or stop consuming the product altogether.

In summary, price matters not only because of its economic role of allocating scarce resources efficiently, but also because it dictates how many people will be able to have access to products.

The questions that arise, therefore, are: (i) if price matters, and dominant firms may raise their prices and exclude several consumers from the market, should antitrust do something about it? (ii) if the answer is positive, where should antitrust authorities draw the line between cases where they must intervene and cases where they should leave it to the market to correct the issue?

2. The difficult task of defining excessive pricing

The determination of fair price has been a subject of study for many economists. Evans and Padilla identify three main criteria used by economists

[13] FEDERAL TRADE COMMISSION; DEPARTMENT OF JUSTICE. Horizontal Merger Guidelines. Available at <https://www.ftc.gov/>. Accessed on September 16, 2016. p. 23.

[14] If a product does not have close substitutes, but is not essential, consumers would simply stop buying it in case of a price increase, which would lead to an elastic demand.

to analyze the fairness of prices: production cost, competitive pricing and profit margin[15].

The production-cost approach was used by Marxist economists and classical economists to determine fair price. Accordingly, the fair price of a product would be "equal to the value of labor involved in its production"[16]. It might be said that this approach has been completely disregarded by modern antitrust policy.

Neo-classical economists, as well as the ordo-liberal school of economic thought, argue that the main drive of fair price is competition. In this sense, fair price "would result from the free interaction of demand and supply in a competitive market"[17].

Evans and Padilla point to a number of practical issues that would arise from this approach. According to the authors, while in competitive and static markets the competitive price would be given by the incremental cost of production (in other words, the point at which marginal cost approaches and/or intersect demand), establishing competitive price in dynamic and concentrated markets would be substantially more complex[18]. In dynamic industries, the price is not established according to marginal cost, but rather on consumers' "willingness to pay as to cover fixed costs in the least output restricting way"[19]. In oligopolistic markets, for example, price will be set forth above marginal cost (and, depending on the level of output restriction, substantially above it).

In addition to production cost and competitive pricing, Evans and Padilla state that some economists have relied on the idea of profit benchmarking to determine fair price. Under this method, price would be deemed abusive if profits are "higher than [firms] could expect to earn in an otherwise identical competitive market", in which case the return on capital of the firm would be "greater than its weighted average cost of capital"[20].

The authors raise several issues to this approach, such as the existence of strategies based on the maximization of the profits earned on a group of products rather than a single product, manufacturing carried out across multiple company's divisions and countries, and the absence of relevant variables in the

---

[15] PADILLA, Jorge; EVANS, David S. Excessive Prices: Using Economics to Define Administrable Legal Rules. Available at <http://ssrn.com/abstract=620402>. Accessed on September 11, 2016. pp. 5-8.

[16] Ibid. p. 5.

[17] Ibid. p. 5.

[18] Ibid. p. 6.

[19] Ibid. p. 6.

[20] Ibid. p. 6.

accounting of business profits, such as past research and development expenditures and costs associated with risk[21].

Another problem of using profit benchmarking to determine whether or not price is excessive is that some firms may have high profits even though they are charging competitive prices. Suppose that firm A has a R$10,00 average production cost per unit and all other firms have a R$20,00 average production cost per unit, but they all charge R$25,00 for their product. Should firm A's price be deemed excessive because its profit margin is higher than its competitor's? If the answer is yes, then antitrust policy would be punishing firm A for being more efficient than its rivals.

As a result, if profits should be used as benchmark for defining excessive pricing, antitrust enforcers would have to engage in the complicated task of determining the nature of the rent transferred to the firm.

Economists often classify rents transferred to firms as Ricardian (scarcity rents), Schumpterian (entrepreneurial rents) or Porterian (monopoly rents)[22].

Ricardian rents are those derived from scarcity of goods. A firm may charge high prices not because it is abusing its market power, but simply because it does not have enough inputs to increase its output[23]. Even if the firm had stockpiled the scarce input in anticipation of its shortage, in which case the firm would in theory be able expand production even if temporarily, it might be that raising output would be inefficient, as price would not properly reflect the scarcity of the good in question. Accordingly, in the hypothetical context of an innovative firm with high profit margin, Sidak and Teece explain that such firm "may have both a high market share and be highly profitable, but this profit in no way implies that it is exercising socially undesirable restraint over its output", since it would be "simply collecting sufficient Ricardian rents to recover its initial investment and offer encouragement to other innovators and entrepreneurs"[24].

The Schumpterian or entrepreneurial rents occur when a firm develops a new technology or method that provides it with a competitive edge over its competitors, allowing the firm to charge a higher price to consumers or

---

[21] Ibid. pp. 6-7.

[22] SIDAK, J. Gregory; TEECE, David J. Comments of J. Gregory Sidak and David J. Teece before the Federal Trade Commission & U.S. Department of Justice on the Horizontal Merger Guidelines Review Project. Available at < http://ssrn.com/abstract=1504706>. Access on September 14, 2016. p. 11.

[23] Ibid. p. 11.

[24] Ibid. p. 13.

to offer the same price as before, but with higher profit margin due to lower costs. There is no question as to the desirability of firms collecting Schumpterian rents, as it creates incentives for innovation and technological progress[25].

Lastly, monopoly rents are those collected by firms exercising their market power. Those rents might be the result of anticompetitive conducts and are the main concern of antitrust policy[26]. However, monopoly rents may also be collected by firms that have monopolized their markets through superior efficiency, and it is doubtful that antitrust policy should intervene in such circumstances. After all, collecting monopoly profits is the single biggest incentive for firms to be efficient and innovative.

It seems, therefore, that any criteria picked by antitrust authorities to draw the line between fair and excessive pricing is bound to raise several practical issues. While economics does not offer a reliable test to identify excessive pricing, Courts have also struggled with the subject.

In Brazil, Cade has never punished firms for excessive pricing, even though many complaints have been filed and analyzed by the authority[27].

Evans and Padilla report a couple of cases in which European authorities have condemned excessive pricing as a standalone infringement[28]. In Case CA98/2/2001, the Office of Fair Trading ("OFT") concluded that Napp Pharmaceuticals Holdings Ltd had established excessive prices for some of its products. According to Evans and Padilla, the OFT reached such conclusion based on a "preponderance-of-evidence" approach, through which the authority took into consideration costs, price and profitability benchmarks[29].

The European Commission, by its turn, punished United Brands for excessive pricing in Case 27/76 (herein after "United Brands"). According to Evans and Padilla, the Commission adopted a two-step test; "First, the test requires comparing actual costs and prices. Second, the test requires

---

[25] Ibid. p. 14.

[26] "The type of rent that ought to be the target of antitrust concern stems from the naked exercise of market power by a firm. These circumstances might arise because of exclusionary conduct lacking efficiency justifications" (Ibid. p. 15).

[27] RAGAZZO, Carlos Emmanuel Joppert. A eficácia jurídica da norma de preço abusivo. Available at <http://works.bepress.com/carlos_ragazzo/16/>. Accessed on September 14, 2016. p. 189.

[28] PADILLA, Jorge; EVANS, David S. Excessive Prices: Using Economics… pp. 8-15.

[29] Ibid. pp. 16-17.

determining whether a price is excessive in itself or by comparison to competitor's products"[30].

Both methods (preponderance of evidence and the United Brands' two-step test) have their shortcomings and might be problematic in practice for the reasons explained above with respect to using benchmarking approaches. As a result, there is a chance that "supra-competitive prices will be blessed in some instances, while competitive prices will be condemned in others"[31].

Although Evans and Padilla argue that, from the perspective of an efficient antitrust policy, excessive pricing should be *per se* legal[32], they go on to suggest a test capable of detecting excessive pricing in a more rational manner, which is comprised of three cumulative conditions: (i) the firm must have a monopoly that is the result of past investments or innovation and is protected by insurmountable legal barriers to entry; (ii) the price set forth by the firm widely exceeds its average total cost; and (iii) the high price might impair the emergence of new products in adjacent markets[33].

A few aspects of such test must be addressed. Given the fact that the first condition proposed by the test requires the existence of insurmountable legal barriers to entry, it is implied that the law should only fight excessive pricing when the law itself was part of the problem. If the legal barriers are related to intellectual property protection, the question of whether antitrust should intervene to lower down the innovator's price is a complicated one, and it might be that intellectual property laws would be a better mechanism to solve the problem (for example, through compulsory licensing, which is possible remedy under Brazilian law). If, however, the legal barriers were created by other laws or regulations, then competition advocacy might arguably be a better alternative than antitrust intervention to lower the legal barriers.

The third condition imposes on the plaintiff the burden of demonstrating, in a counterfactual scenario, that new products would emerge in an adjacent market if the price of the product in question was lower. This condition would make a claim brought under the proposed test resemble a market foreclosure case rather than an excessive pricing one (*e.g.*, "I cannot develop my product A because the price of input B is too high, and the producer

[30] Ibid. p. 15.

[31] Ibid. p. 22.

[32] "The advantage of specifying a common *per se* legal standard for all excessive pricing cases is that it greatly simplifies the application of the law, providing firms with a more certain legal environment and allowing competition authorities to focus on other more grievous offences" (Ibid. p. 29).

[33] Ibid. p. 29.

of input B is a monopolist shielded from competition by insurmountable legal barriers"). Accordingly, additional questions would arise: can antitrust authorities punish a firm for supposedly foreclosing a market that does not exist (and might not come to existence even if the prices are lower)? What happens if price is lowered, but no new product emerges? If the adjacent market already exists and the party bringing the claim is a competitor of the defendant in such market, should the test be applied differently[34]?

Akman and Garrod propose a different test to define excessive pricing, using the United Brands method as the starting point[35]. According to the authors, in United Brands, the European Commission established that price would be deemed excessive if (i) the price-cost margin is excessive, and (ii) the price is unfair in itself or in comparison with that of similar products[36]. The authors argue that such test may not be a good guidance to firms, which may lead to uncertainty and, consequently, loss of welfare[37].

Therefore, they propose a different test, comprised of three steps[38]. In the first step, the antitrust authority would compare the price in question with that of a given reference transaction, looking for any discrepancies between both. If a significant price difference is found, the authority would apply the second step, to determine if the firm has obtained gains in expense of consumers. If the answer is positive, then a third and last step would follow, in which the antitrust authority would inquire whether the transfer of rent at the expense of consumers is the result of changes in the market (supply and demand) or simply the result of lack of competition. If the reason for the excessive price is lack of competition, then the antitrust authority should intervene[39].

---

[34] The possibility of market foreclosure was the essence of Commissioner Paulo Furquim's test proposed in the judgment of process no. 08012.005181/2006-37. See RAGAZZO, Carlos Emmanuel Joppert. A eficácia jurídica… pp. 190-191.

[35] AKMAN, Pinar; GARROD, Luke. When are excessive prices unfair? Available at <http://ssrn.com/abstract=1578181>. Accessed on September 14, 2016.

[36] Ibid. p. 2.

[37] Ibid. pp. 4-5.

[38] For a detailed description of such test, see Ibid. pp. 10-13.

[39] The authors also mention "competition issues" as grounds for intervention under the third step, although it is not clear if the expression should be understood as synonym of "lack of competition". The difference is relevant, as lack of competition might not be the result of competition issues (from an antitrust perspective). In this sense: "[a]lthough the principle of dual entitlement deems prices unfair with respect to exogenous fluctuations in supply and demand, in our procedure prices should only be found unfair if they are unfair due to competition issues. Consequently, an abuse should

The underlying principle of the Akman-Garrod test seems to be that firms should not be allowed to (excessively) extract rents from consumers due to lack of competition. Even though such principle seems right and fair at first glance, one might argue that lack of competition may be the result of superior efficiency by the monopolist firm and, as stated before, it is doubtful that a policy forbidding efficient firms to charge monopoly prices is beneficial in the long run. That is probably the reason why the authors argue, in their conclusion, that antitrust policy should focus on the causes of the lack of competition rather than its effects (excessive price)[40].

Carlos Ragazzo, by his turn, propose that excessive pricing prosecution should be forgone altogether[41]. Aside from the several policy reasons for not pursuing prosecution of such practices, already addressed above, the author argues that under the new Brazilian antitrust statute (Law no. 12,529/2011), excessive pricing was excluded from the non-exhaustive list of anticompetitive practices subject to prosecution contained in article 36, § 3. Ragazzo recognizes, however, that the practice can still be prosecuted in Brazil under the catch-all provision set forth in article 36.

3. Addressing excessive pricing: a proposal

As addressed above, defining general rules to guide antitrust authorities with respect to legal treatment of excessive pricing is difficult, if not impossible (or at least inadvisable).

Notwithstanding, there are conducts, as demonstrated by the Daraprim price increase, that are facially unreasonable and arguably should not be allowed by antitrust law as a matter of fairness. Those are situations where the price is not only excessive, but is also abusive.

Accordingly, even though we agree with arguments that, as a matter of policy, prosecuting excessive pricing is simply not effective, we nevertheless think that antitrust authorities should intervene if: (i) the price is so high as to be considered not only excessive, but abusive; and (ii) the demand for the product in question is inelastic.

Antitrust doctrine has often relied upon concepts that are somehow vague and subjective, such as reasonableness and abusiveness, but nevertheless

only be found if the firm gains sufficiently at the expense of customers due to a lack of competition" (Ibid. p. 13).

[40] Ibid. p. 19.

[41] RAGAZZO, Carlos Emmanuel Joppert. A eficácia jurídica… p. 208.

can be applied with an acceptable degree of certainty and predictability by Courts and administrative tribunals.

In the United States of America, for example, the idea of reasonableness has been used since the early years of the Sherman Act to interpret the overreaching language contained in the Section 1 of said statute. Since the dissenting opinion issued by Justice White in Standard Oil[42], U.S. Courts have developed the rule of reason to determine which types of restrains of trade are forbidden under Section 1 of the Sherman Act.

The rule was further specified and detailed through case law, with the development of concepts such as naked restrains and ancillary restrains[43]. Such concepts have been used as aids to determine when the rule of reason should be applied and how flexible its application should be (*e.g.* full rule of reason or truncated rule of reason[44]).

In addition, the idea of abusiveness is not new to Brazilian law. According to article 187 of Law no. 10.406/2002 (Civil Code), abuse of right occurs whenever a person manifestly exceeds the limits of a right, taking into consideration the social or economic purpose of the right in question, as well as standards of good faith and good costumes. Specifically, the concept of abusiveness has been used by Cade in sham litigation cases.

In the administrative process no. 08012.004484/2005-51, Commissioner Cesar Mattos used the concept of abusive exercise of a right to define the requirements for the characterization of sham litigation. According to the Commissioner, "the abuse of a right arises from the irregular use of such right, with a different purpose than that originally recognized for the right in question" and, consequently, the Law, as a tool of moral valuation, "oriented to ensure order, safety and social peace, is violated by the abusive exercise of a right"[45].

The abuse of right is inherently flexible and, consequently, it would be difficult to formulate a definition that could be applied broadly. Also, its characterization depends heavily on the facts of the case. However, it seems to

---

[42] Standard Oil Co. of New Jersey v. United States, 221 U.S. 1 (1911).

[43] The creation of these concepts is generally attributed to Justice Taft's opinion in Addyston Pipe & Steel Co. v. United States 175 U.S. 211 (1899).

[44] See, for example, NCAA v. Board of Regents of the University of Oklahoma, 468 U.S. 85 (1984); FTC v. Indiana Federation of Dentists, 476 U.S. 447 (1986); and PolyGram Holding, Inc. v. FTC, 416 F.3d 29. (D.C. Cir. 2005).

[45] Page 9 of concurring opinion issued by Commissioner Cesar Mattos in the administrative process no. 08012.004484/2005-51.

be generally accepted that the prohibition of the abuse of right establishes a standard of good-faith behavior.

In this sense, Brazil's Superior Court has decided that the holder of a subjective right may not exercise it in such a manner that "deviates from the theological sense (purpose or social function) of the norm that supports it (exceeding the limits of reasonableness)"[46].

The right to charge whatever price a firm wish was not granted by the Law so as to allow exploitation of consumers by charging abusively high prices. Therefore, it is hereby argued that antitrust should intervene if: (i) the price increase performed by a firm may be deemed abusive, and not merely excessive; (ii) the firm has significant market power, so as to make unlikely that the expansion of output by a competitor would neutralize, at least partially, the harmful effects of the abusive price; and (ii) the demand of the product in question is inelastic, so as to prevent consumers from switching to close substitutes or stopping to consumer the product altogether.

Since the abuse of right is a matter of standard of behavior, the abusive price should be determined in accordance with past practices of the dominant firm. It might be said that firms are allowed (and even expected) to charge high prices as a reward for their efforts for being more efficient than their competitors. Such practice is in accordance with the social and economic purposes of free enterprise, as well as with good faith and good costumes. There is not, however, a general permission for firms to exploit consumers, especially if such consumers have no viable alternatives so as to avoid or mitigate such exploitation.

In that sense, substantial increases in price in a short period of time that cannot be supported by any economic reason, or substantial price increases that can only be explained by concentration of market power, might be deemed abusive if demand is inelastic and therefore there is no possibility for the market to correct itself.

We recognize that it is difficult, if not impracticable, to provide an accurate quantitative criterion for the characterization of abusiveness in a price increase. Any number proposed herein would be arbitrary. Notwithstanding, we believe that antitrust should not close its eyes completely to abusive pricing when the market is not capable of correcting the problem without intervention (*i.e.*, when demand is inelastic).

With respect to other excessive pricing situations (such as, for example, several non-substantial price increases throughout a prolonged period

[46] Superior Court of Justice, REsp 1143216 / RS, J. Luiz Fux, judged on March 24, 2010.

of time or maintenance of high prices for an extended period), we agree with Ragazzo that other laws – such as the intellectual property laws, consumer protection laws and sectoral regulation – may be more effective than antitrust in proving remedy[47].

Thus, as a matter of policy, antitrust authorities should not spend significant resources in prosecuting excessive pricing, since there seems to be no test capable of drawing a clear line between reasonable and excessive prices. As a matter of fairness, however, we believe antitrust enforcers should take action if a certain price increase is facially unreasonable and abusive, provided that the demand curve facing the firm is inelastic[48].

Conclusion

This essay has addressed the problem of excessive pricing, with the purpose of determining if antitrust should be enforced against such practice as a matter of policy and/or as a matter of fairness.

After a brief explanation about why price matters in a capitalist economy and how to draw a line between reasonable and excessive price, we concluded that: (i) price matters because it allows the market to allocate scarce resources efficiently and, from a social perspective, it limits the number of people who have access to a certain product; and (ii) scholars and policymakers have not been able to formulate a reliable test to detecting excessive pricing and, as a result, many scholars suggest that antitrust law should forgo excessive pricing prosecution altogether.

Notwithstanding those findings, however, we concluded that there might be situations where prices are not only excessive, but are also abusive. In those situations, if the firm has substantial market power and faces an inelastic demand curve, antitrust law should address the problem.

Therefore, we conclude that, even though antitrust should not be enforced against excessive pricing as a matter of policy, it should be enforced

[47] RAGAZZO, Carlos Emmanuel Joppert. A eficácia jurídica… pp. 203-205.

[48] As explained by Mark Grady, "[t]he demands facing individual firms are more elastic than the demands facing entire industries". See GRADY, Mark F. Cases and materials… p. 18. Stated backwards, this means that the demand curve facing an industry will be less elastic than those facing an individual firm, which means that the demand curve of the industry might be inelastic, whereas the firm may face an elastic demand curve. Therefore, we are only concerned with situations where the firm, individually, faces an inelastic demand curve.

against abusive (and not only excessive) pricing, if the demand curve faced by the firm in question is inelastic and the firm has substantial market power.

References

ABBOTT, Frederick M. *Excessive pharmaceutical prices and competition law: doctrinal development to protect public health*. Available at <http://ssrn.com/abstract=2719095>. Accessed on August 27, 2016.

AKMAN, Pinar; GARROD, Luke. *When are excessive prices unfair?* Available at <http://ssrn.com/abstract=1578181>. Accessed on September 14, 2016.

FEDERAL TRADE COMMISSION; DEPARTMENT OF JUSTICE. *Horizontal Merger Guidelines*. Available at <https://www.ftc.gov/>. Accessed on September 16, 2016.

GRADY, Mark F. *Cases and materials on antitrust*. Los Angeles [s.n.], 2016. 1074 p.

ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT. *Excessive prices*. Available at <http://www.oecd.org/competition/abuse/49604207.pdf>. Accessed on August 27, 2016.

PADILLA, Jorge; EVANS, David S. *Excessive Prices: Using Economics to Define Administrable Legal Rules*. Available at <http://ssrn.com/abstract=620402>. Accessed on September 11, 2016.

POLLACK, Andrew. Drug goes from $13.50 a tablet to $750, overnight. The New York Times, New York, 20 Sept. 2015. Available at <http://www.nytimes.com/2015/09/21/business/a-huge-overnight-increase-in-a-drugs-price-raises-protests.html?_r=0>. Accessed on August 27, 2016.

PITTMAN, Russell. *Consumer Surplus as the Appropriate Standard for Antitrust Enforcement*. Available at <http://ssrn.com/abstract=996643>. Accessed on September 15, 2016.

POSNER, Richard. The social costs of monopoly and regulation. *The Journal of Political Economy*, Chicago, vol. 83, pp. 807-828, 1975. pp. 807-809.

RAGAZZO, Carlos Emmanuel Joppert. *A eficácia jurídica da norma de preço abusivo*. Available at <http://works.bepress.com/carlos_ragazzo/16/>. Accessed on September 14, 2016.

___________. Preço abusivo, eficácia jurídica e análise econômica: afinal, onde está a cabeça de bacalhau? *Revista do IBRAC*, v. 18, p. 21-43, 2011.

SIDAK, J. Gregory; TEECE, David J. *Comments of J. Gregory Sidak and David J. Teece before the Federal Trade Commission & U.S. Department of Justice on the Horizontal Merger Guidelines Review Project*. Available at < http://ssrn.com/abstract=1504706>. Access on September 14, 2016.

WILLIAMSON, Oliver E. Economies as an antitrust defense: The Welfare Tradeoffs. *The American Economic Review*, Pittsburgh, Vol. 58, pp. 18-36, 1966

___________. Economies as an antitrust defense revisited. *The University of Pennsylvania Law Review*, Philadelphia, Vol. 125, pp. 699-736, 1977.