PRICE AND PREJUDICE: THE CASE AGAINST CONSUMER EQUALITY IN THE INFORMATION AGE

by
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Due to technological advances and changes in markets for consumer goods and services, the ability of firms to engage in various forms of price discrimination has increased greatly in recent years. At the same time, consumer awareness and resentment of these practices—which go under names such as dynamic, differential, and personalized pricing—also has risen. Despite consumer antipathy, most forms of price discrimination are not unlawful when applied to end-use purchasers of consumer goods or services. This Article aims to demonstrate why the current state of affairs might reflect good public policy. To do so, it surveys the economic concept of price discrimination and explains why firms are motivated to price discriminate, what methods they use to do so, and the impediments firms face in their efforts to engage in price discrimination. The Article then analyzes the current legal regulation of price discrimination, including the Robinson-Patman Act, and explains why the law typically does not prohibit merchants from engaging in differential pricing for end-use consumers. After reviewing the economic and legal concepts of price discrimination, this Article uses traditional economic analysis to explain why a rigidly enforced principle of equal treatment, while superficially appealing to consumers, would forbid potentially beneficial price discrimination practices. The Article concludes by suggesting (without endorsing) other legal norms that can be used to guide consumer pricing law including minimizing normatively undesirable wealth distribution, maximizing overall consumer welfare, protecting privacy rights, and eradicating invidious forms of discrimination. This will demonstrate that a vigorous anti-equality stance is neither inimical to consumer rights nor incompatible with progressive critiques of laissez faire approaches to contract law.

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I. INTRODUCTION

A serious conflict is emerging between consumers and retailers due to the dramatic expansion of dynamic, differential and personalized pricing. These practices are all forms of what economists term price discrimination—charging different prices to different consumers for the same good or service based upon their willingness to pay.[1] Unequal pricing practices are extraordinarily unpopular with consumers, but due to technological advances and changes in markets for consumer goods and services, the ability of firms to engage in various forms of price discrimination has expanded at a rapid pace in recent years.[2] At the same time, consumer awareness and resentment of these practices has grown steadily.[3] The Annenberg Public Policy Center at the University of Pennsylvania recently issued a report that demonstrates the depth of public distaste with the unequal treatment caused by price discrimination.[4] En route to concluding that consumers "overwhelmingly object to . . . all forms of price discrimination as ethically wrong,"[5] the Annenberg Report reported the following interesting poll findings:

> 76% agree that "it would bother me to learn that other people pay less than I do for the same products."

[1] *See infra* Part II.A–C (discussing the concept of economic price discrimination); Part II.A (discussing the concept of legal price discrimination).

[2] *See infra* Part II.D.

[3] *See infra* Part IV.A (discussing consumer reactions to price discrimination).

[4] JOSEPH TUROW ET AL., OPEN TO EXPLOITATION: AMERICAN SHOPPERS ONLINE AND OFFLINE (2005), http://www.annenbergpublicpolicycenter.org/04_info_society/Turow_APPC_Report_WEB_FINAL.pdf [hereinafter ANNENBERG REPORT].

[5] *Id*. at 4.

> 64% agree that "it would bother me to learn that other people get better discount coupons than I do for the same products."
>
> 66% disagree that "it's OK with me if the supermarket I shop at keeps detailed records of my buying behavior."
>
> 87% disagree that "it's OK if an online store I use charges people different prices for the same products during the same hour."
>
> 72% disagree that "if a store I shop at frequently charges me lower prices than it charges other people because it wants to keep me as a customer more than it wants to keep them, that's OK."[6]

Despite the consumer resentment reflected in the Annenberg Report, most forms of price discrimination in consumer goods and services are not unlawful when applied to end-use purchasers of consumer goods or services.[7] Understanding why this state of affairs might reflect good public policy requires a basic understanding of the economics of price discrimination, as well as an appreciation of the current state of the law on differential pricing practices. By using traditional economic analysis, this Article aims to demonstrate that a rigidly enforced principle of equal treatment, while superficially appealing to consumers, would forbid potentially beneficial price discrimination practices. As such, this Article argues that norms such as protecting privacy interests and forbidding invidious forms of racial and gender discrimination are better suited to the task of informing consumer-pricing regulation than the notion of consumer equality.

The Article proceeds as follows: Part II surveys the economic concept of price discrimination. This Part explains why firms are motivated to price discriminate, what methods they use to do so, and the impediments firms face in the price discrimination process. Part III surveys the current legal regulation of price discrimination and explains why current federal law typically does not prohibit merchants from engaging in differential pricing for end-use consumers. Part IV argues that principles of consumer equality, though superficially appealing, should not drive consumer-pricing law. This Part asserts that a widely enforced equality principle could harm consumers by eliminating forms of price discrimination that might be potentially beneficial. At the same time, Part IV endeavors to show that a vigorous anti-equality stance is neither inimical to consumer rights nor incompatible with progressive critiques of laissez faire approaches to contract law, including those based upon privacy, welfare maximization, and anti-discrimination norms.

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6 *Id*.

7 *See infra* Part III.A–B (addressing legality of price discrimination).

II. AN INTRODUCTION TO ECONOMIC PRICE DISCRIMINATION

A. Economic Price Discrimination Defined

The term price discrimination[8] has both economic[9] and legal meanings. This subsection will address only the economic meaning.[10] At the most basic level, price discrimination is the sale of the same commodity or service to different buyers at different prices based upon their willingness to pay, absent a justification based upon cost.[11] In more precise economic terms, "price discrimination is present when two or more similar goods are sold at prices that are in different ratios to marginal costs."[12]

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8 On occasion, one sees terms in the literature such as differential or dynamic pricing instead of price discrimination. For our purposes here, we can consider all of these terms to be synonymous. *See* Peter J. Hammer, *Differential Pricing of Essential AIDS Drugs: Markets, Politics and Public Health*, 5 J. INT'L ECON. L. 883 n.1 (2002) (equating differential pricing with price discrimination); Robert M. Weiss & Ajay K. Mehrotra, *Online Dynamic Pricing: Efficiency, Equity and the Future of E-Commerce*, 6 VA. J.L. & TECH. 11, ¶ 1 (2001), http://www.vjolt.net/vol6/issue2/v6i2-a11-Weiss.html ("[D]ynamic pricing allows online companies to adjust the prices of identical goods to correspond to a customer's willingness to pay.").

9 For a sampling of the economics literature on price discrimination, *see* Lars A. Stole, *Price Discrimination and Imperfect Competition* (Univ. of Chi., GSB, 2003), *available at* http://gsblas.uchicago.edu/papers/hio-distrib.pdf; JEAN TIROLE, THE THEORY OF INDUSTRIAL ORGANIZATION 133–52 (1988); Louis Phlips, *Price Discrimination*, *in* 3 THE NEW PALGRAVE: A DICTIONARY OF ECONOMICS 952, 952–54 (John Eatwell et al. eds., 1987) [hereinafter Phlips, *Price Discrimination*]; LOUIS PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION (1983) [hereinafter PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION]; DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 290–308 (4th ed. 2005).

10 *See infra* Part III.A for a brief overview of the law of price discrimination.

11 *See* Michael J. Meurer, *Price Discrimination, Personal Use and Piracy: Copyright Protection of Digital Works*, 45 BUFF. L. REV. 845, 869 (1997) ("Price discrimination means that consumers of an identical product are charged different prices by the same seller, or that consumers of similar products made by the same seller are charged a price differential unrelated to cost."); *see also* Marcel Kahan & Ehud Kamar, *Price Discrimination in the Market for Corporate Law*, 86 CORNELL L. REV. 1205, 1215 (2001):

> Price discrimination occurs when a producer charges a higher price to consumers with a higher willingness to pay and a lower price to consumers with a lower willingness to pay. . . . What distinguishes price discrimination from regular price differences between products in competitive markets is that price discrimination is the sale of products by the same producer at prices that are in different ratios to marginal costs of production.

12 Hal R. Varian, *Price Discrimination*, *in* 1 HANDBOOK OF INDUSTRIAL ORGANIZATION 597, 598 (Richard Schmalensee & Robert D. Willig eds., 1989) (citing GEORGE STIGLER, THE THEORY OF PRICE (4th ed. 1987)). Marginal cost can be defined as "the *increment*, or addition, to cost that results from producing one more unit of output." CARLTON & PERLOFF, *supra* note 9, at 30; *see also* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 8 (6th ed. 2003) ("Marginal cost is the change in total costs brought about by a one-unit change in output; in other words, it is the cost that would be avoided by producing one unit less.").

Examples of price discrimination abound in our society:[13] many entertainment venues, such as movie theaters, provide discounts to senior citizens and children[14] (thus charging more to adult non-seniors); airlines charge different amounts for similar seats on the same flight;[15] publishers charge higher amounts to institutional subscribers, such as university libraries, than they charge individual buyers;[16] and car dealers sell the same car to different buyers at different prices.[17] In these and many other cases, the same good or service is being sold to different consumers at different prices based upon their willingness to pay ("WTP"), not the seller's cost.

By definition, then, price differences based solely upon cost differentials do not constitute economic price discrimination. For example, after individual negotiation, a car dealer might sell exactly the same model of a car with the same features to two different consumers at two different prices. This clearly satisfies the definition of economic price discrimination. In contrast, the price of a Honda Accord with a four-cylinder engine might not be the same as a

[13] *See* Glen O. Robinson, *Personal Property Servitudes*, 71 U. CHI. L. REV. 1449, 1505–506 (2004) ("Price discrimination is an accepted feature of modern markets, as anyone knows if she has bought an airline ticket, used a special discount card at the grocery store, or negotiated a price for a new car."); Varian, *supra* note 12, at 598 ("Price discrimination is one of the most prevalent forms of marketing practices.").

[14] *See* Mark Klock, *Unconscionability and Price Discrimination*, 69 TENN. L. REV. 317, 331 (2002) ("Senior citizens and college students, who are often less willing or able to pay as much for goods and services, commonly receive discriminatory discounts."); Michael J. Meurer, *Copyright Law and Price Discrimination*, 23 CARDOZO L. REV. 55, 70 (2001) ("Senior citizen and student discounts are common for musical, theatrical, and movie performances.").

[15] *See* Kevin Outterson, *Pharmaceutical Arbitrage: Balancing Access and Innovation in International Prescription Drug Markets*, 5 YALE J. HEALTH POL'Y L. & ETHICS 193, 204 n.44 (2005) ("On almost every flight, passengers will have paid many different prices for the same service. The market has been segmented into multiple buyer groups, including business travelers, vacation travelers, frequent flyers, and last minute purchasers.").

[16] *See In re* Brand Name Prescription Drugs Antitrust Litig., 186 F.3d 781, 787 (7th Cir. 1999) (Posner, J.) ("[P]ublishers of scholarly journals commonly charge a much higher price to libraries than to individuals even though the cost of making and selling the journal is identical to both classes of purchaser."); Klock, *supra* note 14, at 331 ("Publishers commonly charge university libraries many times more than what they charge individuals for subscriptions to journals.").

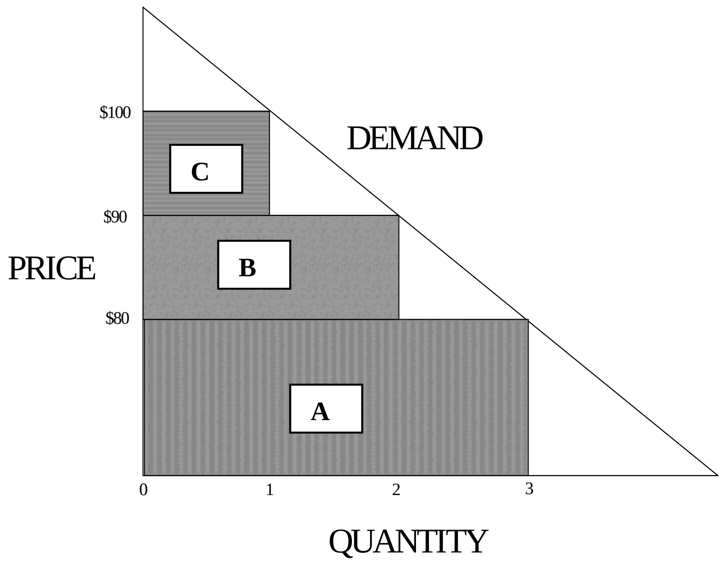
[17] *See* Fiona Scott Morton et al., *Consumer Information and Discrimination: Does the Internet Affect the Pricing of New Cars to Women and Minorities?*, 1 QUANTITATIVE MARKETING & ECON. 65, 69 (2003) ("Car prices are individually negotiated, so there is opportunity for significant price discrimination in the market. The same car sells for different prices because supply and demand shift over time and consumers differ in characteristics."). Although car sales are the quintessential example of a market where negotiation, haggling and dickering are prevalent, there are some car dealers and carmakers that offer fixed prices. *See* Ian Ayres, *Further Evidence of Discrimination in New Car Negotiations and Estimates of its Cause*, 94 MICH. L. REV. 109, 142 (1995). ("[T]he retail car market has seen a dramatic shift away from haggling. More than 10% of new car dealers currently sell all of their cars at nonnegotiable prices, and more than 70% of dealers sell at least one of their models without dickering."); *but see id*. at 143 (noting that "[t]he presence of no-haggle dealers has provoked an 'emotional response' from the other dealers, and the growth rate of no-haggle sales has begun to taper").

"fully loaded" Honda Accord with a V6 engine and leather seats. Selling these two vehicles at different prices is not price discrimination if the higher costs of producing the fully loaded V6 Accord account for the car's higher price. Nevertheless, the concept of price discrimination can be expanded further to situations where the goods being sold are not identical, but where the difference in the cost of producing the items does not account for the pricing difference. For example, paperback and hardcover versions of the same book are not identical commodities, so we might expect that they would be priced differently. But a form of price discrimination may be at work if the difference in prices between a paperback and a hardcover version of the same book is not explained fully by the difference in the costs of producing these different versions.[18]

Producers usually prefer price discrimination to uniform pricing. Understanding why this is so requires a comprehension of consumer surplus. A basic example will illustrate this concept. Imagine that we have a marketplace comprised of a single seller, Sam, and three consumers Adam, Betty and Charles. Assume that Sam's reservation price, the lowest price that he will accept for a particular good, is $80, and Adam, Betty and Charles have reservation prices of $80, $90 and $100 respectively.[19] The situation can be graphed as follows:

[18] *See* Kahan & Kamar, *supra* note 11, at 1215; Varian, *supra* note 12, at 598–99 (using book pricing example from GEORGE STIGLER, THE THEORY OF PRICE (4th ed. 1987)).

[19] HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE, § 1.1, at 4 (3d ed. 2005) ("A reservation price is the highest amount that a consumer is willing to pay for a product."); Russell Korobkin, *Aspirations and Settlement*, 88 CORNELL L. REV. 1, 5 (2002) ("In any bargaining situation, negotiators have a reservation price, defined as the maximum amount the negotiator is willing to give up or the minimum amount the negotiator is willing to accept, as the case may be, to consummate a transaction.").



If the seller, Sam, uniformly prices the item at $80, Adam, Betty and Charles all will buy the product. The seller will make three sales at $80 each for a total of $240, as indicated by shaded area A. The problem, from the seller's perspective, is that Betty and Charles both would have been willing to pay more than $80. The difference between what a seller is willing to accept and what the buyers are willing to pay is referred to as consumer surplus.[20] In the case above, the consumer surplus is $30, the difference between what the consumers would have been willing to pay in the aggregate ($270) and what they paid under a uniform pricing regime ($240). By pricing the item at $80, the entire surplus was allocated to the consumers, an outcome that displeases the seller. Sam will seek to recover this "lost" $30 of consumer surplus by engaging in some form of price discrimination, as will be explained shortly.

B. Three Degrees of Price Discrimination

Economists break down the concept of price discrimination into first, second, and third degree price discrimination.[21] All three are methods of

[20] *See* CARLTON & PERLOFF, *supra* note 9, at 70 ("Typically, consumers value the goods they purchase above the amount they actually pay for them. Consumer surplus is the amount above the price paid that a consumer would willingly spend, if necessary, to consume the units purchased."); Klock, *supra* note 14, at 324–25 ("Consumer surplus is summarized as the gains from trade. It represents the difference between what society would have been willing to pay for the product if differential prices had been charged on each unit and what society did pay for the product given that the price was the same for all units."); POSNER, *supra* note 12, at 279 ("Consumer surplus is a measure of the aggregate value that consumers attach to a product over and above the price they pay for it.").

[21] A.C. Pigou is generally credited for first elaborating these distinctions. *See* A. C. PIGOU, THE ECONOMICS OF WELFARE 278–79 (4th ed. 1962); *see also* PHLIPS, THE

extracting consumer surplus. Under first-degree price discrimination, which is also called "perfect" price discrimination,[22] the seller extracts the entire consumer surplus by "charging a different price for each unit of the good in such a way that the price charged for each unit is equal to the maximum willingness to pay for that unit."[23] For example, in the hypothetical above, Sam would like to sell to Adam at $80, Betty at $90 and Charles at $100, their respective reservation prices. This pricing strategy allows the seller to extract the entire consumer surplus, since each consumer is paying their maximum price, and no one is paying less than they would be willing to pay. From the seller's perspective,[24] this is superior to uniform pricing, which necessarily leads to some consumers being charged less than they are willing to pay.[25]

As appealing as it is to sellers, one problem with first-degree price discrimination is that buyers are unlikely to reveal voluntarily the highest price that they are willing to pay.[26] One possible solution to this quandary would be for the seller to engage in an individual negotiation or haggling with each potential buyer in an attempt to arrive at the highest price for each consumer.[27]

ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 136 (crediting Pigou); TIROLE, *supra* note 9, at 135 (same); Varian, *supra* note 12, at 600 (same).

[22] *See* CARLTON & PERLOFF, *supra* note 9, at 299; PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 137; TIROLE, *supra* note 9, at 135; Varian, *supra* note 12, at 600–01.

[23] Varian, *supra* note 12, at 600; *see also* CARLTON & PERLOFF, *supra* note 9, at 299; Kahan & Kamar, *supra* note 11, at 1216 ("First-degree, or perfect, price discrimination is the most profitable type of price discrimination because it extracts each consumer's entire surplus."); PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 137; PIGOU, *supra* note 21, at 279.

[24] The overall welfare effects of first-degree price discrimination are discussed *infra* Part IV.B.

[25] *See* CARLTON & PERLOFF, *supra* note 9, at 293 ("Price discrimination is profitable because consumers who value the good the most pay more than if prices were uniform."); Brett M. Frischmann, *An Economic Theory of Infrastructure and Commons Management*, 89 MINN. L. REV. 917, 979 (2005) ("When unchecked by competition or the government, producers often drive toward price discrimination for an intuitively obvious reason—differential pricing allows the producer to extract a greater proportion of the surplus than under uniform pricing."); Phillip Leslie, *Price Discrimination in Broadway Theater*, 35 RAND. J. ECON. 520, 520 (2004) ("Price discrimination allows firms to increase their revenue above what may be obtained from uniform pricing."); Meurer, *supra* note 14, at 69 (noting that "perfect price discrimination always yields sales that are at least as high as uniform pricing").

[26] David Gilo & Ariel Porat, *The Hidden Roles of Boilerplate and Standard-Form Contracts: Strategic Imposition of Transaction Costs, Segmentation of Consumers, and Anticompetitive Effects*, 104 MICH. L. REV. 983, 993 (2006) ("Even when price discrimination is permitted, the supplier could find it hard to implement. One main reason is that on many occasions a consumer's willingness to pay is unobservable to the supplier or the costs of verifying it are very high."). Conceivably, if the seller is dealing with the buyer's agent, he could bribe the buyer's agent to get her to reveal her principal's reservation price. *See* PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 12; *see also* PIGOU, *supra* note 21, at 280 (noting that individual bargaining "opens the way, not only to error, but also to the perversion of agents through bribery").

[27] *See* Robert H. Lande & Howard P. Marvel, *The Three Types of Collusion: Fixing Prices, Rivals, and Rules*, 2000 WIS. L. REV. 941, 977 n.163 (2000) ("When customers are

There are, however, two problems with this approach. First, negotiation may not be an effective method of revealing the customers' WTP.[28] In fact, if a buyer understands that the seller is attempting to determine her WTP, the buyer may even try to mislead the seller regarding her true reservation price.[29] Second, individualized negotiation is probably cost-prohibitive with mass-produced consumer goods.[30] Imagine, for example, the staffing which would be required for Wal-Mart to individually negotiate the terms of every DVD or toothpaste sale.

In part because of the difficulties that sellers have in determining the maximum amount that a buyer is willing to pay,[31] economists and legal scholars consider first-degree price discrimination to be quite difficult to achieve.[32] But the lure of appropriating the consumers' surplus is powerful, so sellers seek alternative price discrimination methods. In some cases, a seller knows that consumers can be broken into different groups based upon willingness to pay but the seller cannot determine who belongs in which groups based upon observable characteristics.[33] Airlines provide a good example:

> An airline, for example, may know that business travelers have a higher willingness to pay than leisure travelers, but not whether a particular passenger is a business or leisure traveler. To address this difficulty, the airline attempts to distinguish between the two groups by offering a lower round-trip fare for trips that include a weekend stay. Because leisure

presented with personalized offers, often in the form of take-it-or-leave it deals negotiated individually (as in the automobile market), the pricing may approximate first-degree price discrimination.").

[28] Meurer, *supra* note 11, at 871 ("In a negotiated transaction, the seller can observe general demographic characteristics but cannot force a prospective buyer to divulge her valuation any more than the buyer could force the seller to divulge his cost.").

[29] *See* Lee Anne Fennell, *Revealing Options*, 118 HARV. L. REV. 1399, 1427, 1468–69 (2005); Meurer, *supra* note 11, at 871.

[30] *See* Varian, *supra* note 12, at 604 (noting that any welfare analysis must take into consideration the cost of haggling).

[31] Another problem is the prevention of arbitrage. *See infra* Part II.C and accompanying text.

[32] *See* HOVENKAMP, *supra* note 19, § 14.4, at 575 ("Perfect price discrimination never exists in the real world. The costs of determining each customer's reservation price and structuring the market to enable the seller to charge that price would be prohibitive."); Kahan & Kamar, *supra* note 11, at 1216; Outterson, *supra* note 15, at 204 ("In reality, transaction costs almost always make first-degree differential pricing untenable: The seller's marginal costs of collecting and understanding all of the relevant factors for each buyer usually outweigh the gains in marginal revenue."); RICHARD A. POSNER, ANTITRUST LAW 80 (2d ed. 2001) (noting that perfect price discrimination is "never feasible"); POSNER, *supra* note 12, at 283 (stating that "the transaction costs of perfect . . . price discrimination are prohibitive"). *But see* sources cited *infra* Part II.D (addressing increasing ability of producers to price discriminate).

[33] ProCD, Inc. v. Zeidenberg, 86 F.3d 1447, 1450 (7th Cir. 1996) (Easterbrook, J.) ("Customers do not wear tags saying 'commercial user' or 'consumer user.'"); Janet S. Netz, *Price Regulation: A (Non-Technical) Overview*, *in* 3 ENCYCLOPEDIA OF LAW AND ECONOMICS 396 (Boudewijn Bouckaert & Gerrit de Geest eds., 2000) ("How could the firm classify consumers into the two pricing categories? No consumer would willingly admit that she was willing to pay the higher price.").

> travelers, unlike business travelers, rarely mind staying over the weekend, this pricing scheme enables the airline to charge a higher price to business travelers than to leisure travelers.[34]

Similarly, the airlines make one class of higher-priced, unrestricted tickets, which are easy to change or cancel without penalty (appealing to business travelers) and another class of lower-priced, restricted tickets, which are non-refundable and can only be changed with a penalty (appealing to more price-conscious leisure travelers).[35] Or airlines could charge higher prices for direct flights departing at desirable travel times and lower prices for flights with multiple connections that leave at less desirable travel times.[36] Presumably, these travel rules and options will help to separate business and leisure travelers.[37] The crux of second-degree price discrimination is that the seller varies the good or service in some way that causes buyers to sort themselves by their own choices into different WTP groups.[38] This "self-sorting" is a key benefit of second-degree price discrimination.[39]

Third-degree price discrimination involves separating buyers into different groups based upon some readily observable characteristic that can serve as a proxy for willingness to pay,[40] and then charging members of different groups

[34] Kahan & Kamar, *supra* note 11, at 1216–17; *see also* Klock, *supra* note 14, at 330–31, 361–62.

[35] *See* Avery Wiener Katz, *The Option Element in Contracting*, 90 VA. L. REV. 2187, 2224–25 (2004).

[36] *See* Michael E. Levine, *Price Discrimination Without Market Power*, 19 YALE J. ON REG. 1, 22 (2002).

[37] Gilo & Porat, *supra* note 26, at 993–94 ("[A]irlines charge consumers higher prices for short stays in the passenger's destination than for long stays. A possible explanation is that most short-journey travelers are businesspeople, while most long-journey travelers are people traveling on vacation, and on average, the former group, or their employers, are willing to pay higher prices than the latter group."). To be sure, these are imperfect methods for sorting airline travelers. For example, some business travelers will stay over a Saturday and some leisure travelers will be unable to work a Saturday into their plans.

[38] *See* Christopher S. Yoo, *Rethinking the Commitment to Free, Local Television*, 52 EMORY L.J. 1579, 1623 n.107 (2003) ("In second-degree price discrimination, the producer holds out certain purchase options designed to appeal differently to different classes of customers and allows customers' individual purchasing decisions to sort themselves into the appropriate group."); *see also* Hammer, *supra* note 8, at 885 (observing that "products and services may be differentiated in terms of time . . . quantity . . . or quality . . . all with the objective of maximizing the producer's profits by exploiting differences in consumer demand."); Outterson, *supra* note 15, at 204. Bulk sales are another example of second-degree price discrimination. *See* Varian, *supra* note 12, at 611 ("Second-degree price discrimination, or nonlinear price discrimination, occurs when individuals face nonlinear price schedules, i.e. the price paid depends on the quantity bought. The standard example of this form of price discrimination is quantity discounts.").

[39] *See* PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 15 (observing that a "reason why self-selecting devices are so common is that they provide a simple and cheap way of identifying different groups of customers when this identification is not given exogenously.").

[40] Recall that with second-degree price discrimination buyers do not have any identifiable characteristic that could be used as a proxy for greater willingness to pay. *See* Kahan & Kamar, *supra* note 11, at 1216 ("In the case of second-degree price discrimination,

different prices.[41] A common example of third-degree price discrimination is senior citizen's and children's movie discounts.[42] Theaters may assume, as a general rule, that adult non-seniors are likely willing to pay more than children and senior citizens to see a movie.[43] Thus, movie theaters charge children and seniors less than adult non-seniors. Such discounts are not typically controversial because they are framed as a benefit to certain groups and not as a penalty to those who do not receive the discount, and because the groups who typically benefit (children and seniors in the movie discount case) are sympathetic to the average consumer.[44] Nevertheless, a price differential structured as a benefit to a discrete group could be viewed as a detriment to non-favored buyers.[45]

C. Arbitrage

A firm that engages in price discrimination must try to prevent arbitrage, which "occurs when favored purchasers resell the product to disfavored purchasers at some price that is profitable to the favored purchasers but less than the disfavored purchasers were asked to pay."[46] For example, when a

the producer also knows that a certain group of consumers has on average a higher willingness to pay than another group. The producer, however, cannot tell to which group an individual consumer belongs."). Buyers identify themselves based upon their responses to the seller's rules or manipulation of the product offering. *See supra* notes 38–39 and accompanying text.

[41] *See* Kahan & Kamar, *supra* note 11, at 1216 ("For a producer to engage in third-degree price discrimination, the producer must be able to distinguish among groups of consumers with different average willingness to pay."); PIGOU, *supra* note 21, at 279 (noting that third-degree price discrimination can exist "if the monopolist were able to distinguish among his customers *n* different groups, separated from one another more or less by some practicable mark, and could charge a separate monopoly price to the members of each group."). For more detailed economic discussions of third-degree price discrimination, *see* CARLTON & PERLOFF, *supra* note 9, at 301–05; TIROLE, *supra* note 9, at 137–42; Varian, *supra* note 12, at 617–26; Stole, *supra* note 9, at 8–26.

[42] *See supra* note 14.

[43] Hammer, *supra* note 8, at 885 (observing that "[t]he demands of students and senior citizens are likely to be more elastic than those of ordinary filmgoers.").

[44] *See* Ellen Garbarino & Olivia F. Lee, *Dynamic Pricing in Internet Retail: Effects on Consumer Trust*, 20 PSYCHOL. & MARKETING 495, 498 (2003) (observing that "social norms for preferred treatment" have developed for children and seniors).

[45] *See* Klock, *supra* note 14, at 331 ("Although the price differentials charged to the different market segments are touted as discounts, the reality is that they reflect premiums being charged to the less price-sensitive group.")

[46] HOVENKAMP, *supra* note 19, § 14.4, at 575; *see also* CARLTON & PERLOFF, *supra* note 9, at 295–96 (addressing need of price discriminating firm to prevent or limit resales); Dennis S. Corgill, *Distributing Products Under the Nonprofit Institutions Act: Price Discrimination, Arbitrage, and Fraud in the Pharmaceutical Industry*, 2001 B.Y.U. L. REV. 1383, 1404 (2001) ("Crucial to any system of price discrimination . . . is the need to prevent arbitrage . . . This is the practice by which a purchaser who buys at the lower price is able to resell or divert to those who are willing to pay a higher price."); POSNER, *supra* note 12, at 283 (discussing arbitrage); ProCD, Inc. v. Zeidenberg, 86 F.3d 1447, 1450 (7th Cir. 1996) (Easterbrook, J.) ("To make price discrimination work . . . the seller must be able to control arbitrage.").

senior citizen buys a discounted ticket to the movies, the movie theater does not want the senior citizen to resell her ticket to a non-senior adult for less than the adult ticket price. If Microsoft sells discounted software to college students, it will seek to prevent students from reselling to other end-users.[47] Drug companies that sell AIDS drugs at a discount in Africa do not want to see the drugs resold at a great profit in Europe and North America.[48]

Sellers have several different ways of preventing arbitrage. Most obviously, a firm practicing price discrimination may impose a contract term on the initial buyer that prohibits resale.[49] Airlines, for example, do not permit a ticket buyer to transfer the ticket to another user.[50] In some situations, producers can restrict transfer of a good through technological barriers—streaming video over the Internet is harder to transfer from one buyer to another than easily copied videotape.[51] In many cases, however, the nature of the initial transaction itself makes arbitrage unlikely. For example, resale is far less likely where the product is a service and not a good.[52] Michael Meurer makes the point well:

> The favored customer of a hair stylist cannot purchase an extra haircut for resale. The favored customer of a dentist cannot resell a filling. Younger movie patrons cannot use senior movie tickets as long as the tickets indicate that they are for senior use and the ticket taker is vigilant.[53]

Moreover, arbitrage is only possible if transaction costs are not a barrier to resale.[54] A U.S. car dealer might learn that Mercedes is selling its cars for less in India, but the expense of purchasing the cars in India, importing them into

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[47] Versioning is a method of price discrimination that may prevent some arbitrage. *See infra* notes 70–77 and accompanying text.

[48] *See* Outterson, *supra* note 15, at 193 (discussing arbitrage in pharmaceuticals).

[49] *See* CARLTON & PERLOFF, *supra* note 9, at 296; Corgill, *supra* note 46, at 1405–06 (discussing contract provisions that attempt to limit arbitrage in the context of pharmaceutical sales).

[50] *See* Andrew Odlyzko, Privacy, Economics, and Price Discrimination on the Internet 4 (July 27, 2003), http://ssrn.com/abstract=429762 ("Airline yield management is as effective as it is because a ticket is a contract for carriage of a specific person, and is not transferable.")

[51] Meurer, *supra* note 11, at 875.

[52] *See* PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 14 ("Units of services applied directly to the person of the customer are entirely nontransferable: That is why physicians, lawyers, dentists and so forth can charge different fees to richer and poorer clients.").

[53] Meurer, *supra* note 11, at 874 n.145; Hammer, *supra* note 8, at 886 ("[I]t is more difficult to engage in arbitrage in markets for services. People cannot resell a haircut or an appendectomy. As such, markets for medical services are characterized by high degrees of price discrimination.").

[54] *See* CARLTON & PERLOFF, *supra* note 9, at 295 ("If consumers incur any large transaction costs to resell the product, resales are less likely. . . . In many markets, storage costs, search costs, or other transaction costs are too high for any resales to occur."); TIROLE, *supra* note 9, at 134 ("Transaction costs offer a clue as to when price discrimination is feasible.").

the United States, and marketing them to domestic U.S. consumers may render any attempted arbitrage unprofitable.

D. Price Discrimination in the Information/Internet Age

Technological advances have made it easier for firms to price discriminate both online and off-line, thus overcoming traditional barriers to effective price discrimination.[55] Many firms engage in sophisticated data-mining[56] to collect, organize, and analyze vast amounts of demographic information on consumers.[57] This information can be used for targeted marketing and pricing purposes,[58] thus putting consumers at a disadvantage in the negotiating process, in part by revealing cues about their willingness to pay or reservation prices.[59]

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55 *See generally* Andrew G. Celli, Jr. & Kenneth M. Dreifach, *Postcards from the Edge: Surveying the Digital Divide*, 20 CARDOZO ARTS & ENT. L.J. 53, 67–69 (2002); Weiss & Mehrotra, *supra* note 8.

56 For an introduction to data mining *see* Tal Z. Zarsky, *"Mine Your Own Business!": Making the Case for the Implications of the Data Mining of Personal Information in the Forum of Public Opinion*, 5 YALE J. L. & TECH. 1 (2003).

57 *See* Celli & Dreifach, *supra* note 55, at 67–69; Albert A. Foer, *E-Commerce Meets Antitrust: A Primer*, 20 J. PUB. POL'Y & MARKETING. 51, 61 (2001).

58 *See* Robert A. Hillman & Jeffrey J. Rachlinski, *Standard-Form Contracting in the Electronic Age*, 77 N.Y.U. L. REV. 429, 471 (2002) (discussing contract term differentiation and tailored advertising on the Internet). Merchants have been aided by the growth of "behavioral targeting" firms who specialize in the collection, analysis and utilization of consumer data. *See* ANNENBERG REPORT, *supra* note 4, at 7–9. These processes can be quite difficult for merchants to employ. *See* Tal Z. Zarsky, *Information Privacy in Virtual Worlds: Identifying Unique Concerns Beyond the Online and Offline Worlds*, 49 N.Y.L. SCH. L. REV. 231, 238, 259–61 (2004) (discussing special challenges that information collectors face online).

59 Janet Dean Gertz, Comment, *The Purloined Personality: Consumer Profiling in Financial Services*, 39 SAN DIEGO L. REV. 943, 964 (2002) ("[P]rofiling alters the economic balance between the individual consumer and the financial institution. By profiling consumers, financial institutions can predict an individual's demand and price point sensitivity and thus can alter the balance of power in their price and value negotiations with that individual."); Klock, *supra* note 14, at 330 ("Modern technology has made it possible to compile large databases on consumers, and it has been documented that firms conducting business on the Internet have used this information to assess customers' ability and willingness to pay, and have charged customer-specific prices based upon this information."); Marc Rotenberg, *Fair Information Practices and the Architecture of Privacy: (What Larry Doesn't Get)*, 2001 STAN. TECH. L. REV. 1, ¶ 110, http://stlr.stanford.edu/STLR/Articles/01_STLR_1/index.htm ("In bargaining, no one wants to give up their 'reservation' price to the other side. With profiling, the consumers give up the privacy of their reservation price, but the seller doesn't. So it changes the power in the bargaining, against consumers."); Zarsky, *supra* note 58, at 260 (observing that "enhanced capabilities to collect and analyze personal information enable online vendors to price products and services in ways that are detrimental to their users, and achieve an unfair advantage in these transactions"); Tal Z. Zarsky, *Thinking Outside the Box: Considering Transparency, Anonymity, and Psuedonymity As Overall Solutions to the Problems of Information Privacy in the Internet Society*, 58 U. MIAMI L. REV. 991, 1010 (2004) ("The collection and analysis of vast amounts of personal information pertaining to consumers' patterns of behavior, in conjunction with Internet websites' ability to provide consumers

In addition, merchants can analyze consumers' online shopping behavior; this includes more than simply purchasing activity—Internet surfing and pre-purchase shopping behavior also can be tracked and analyzed to gain a competitive advantage.[60] It is challenging for consumers to take defensive action against these practices, since online tracking is largely transparent[61]—consumers may have no idea of the extent to which firms are collecting and analyzing data to predict and influence consumer behavior.[62]

Price customization or differential pricing is also difficult to discern online,[63] thus making consumers vulnerable to what two government regulators termed a "sucker surcharge."[64] A consumer who walks into a brick and mortar store probably sees the product that he wants on display with a price posted. Prevailing norms will then determine whether the consumer feels free to haggle with the merchant over price. In cyberspace, however, two consumers may be confronted with very different virtual stores, as Tal Zarsky explains:

> At this time, vendors and marketers can make use of personal information they obtain to create different pricing schemes for different types of customers. The Internet and E-commerce environment provide fertile ground for such practices, since vendors can easily collect personal information about every user, and create a different "store" for every customer by providing them with a different screen or window. This way, the customer does not know he or she is receiving service and treatment that is different from others and will not suspect being overcharged.[65]

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with a customized shopping environment, allows marketers and vendors to discriminate among individuals with great precision and minimal effort.").

[60] *See* Gilo & Porat, *supra* note 26, at 1003 (observing that "it is relatively easy to track a consumer's moves from one page to another and learn about her preferences even if eventually she buys nothing."); Jerry Kang, *Information Privacy in Cyberspace Transactions*, 50 STAN. L. REV. 1193, 1198–99 (1998); ANNENBERG REPORT, *supra* note 4, at 6; Tal Z. Zarsky, Desperately Seeking Solutions: *Using Implementation-Based Solutions for the Troubles of Information Privacy in the Age of Data Mining and the Internet Society*, 56 ME. L. REV. 13, 18–19 (2004).

[61] Much of the newer offline tracking is also relatively transparent to consumers. *See* ANNENBERG REPORT, *supra* note 4, at 6–9.

[62] *See* ALAN E. WISEMAN, FED. TRADE COMM'N, ECONOMIC PERSPECTIVES ON THE INTERNET 39 (2000), *available at* http://www.ftc.gov/be/economicissues.pdf. ("[F]or the first time in history, it is technologically possible to learn details about the particular tastes of consumers without them being aware of it, and independent of their purchase decisions.").

[63] Celli & Dreifach, *supra* note 55, at 69 ("Internet price customization is not nearly as transparent to consumers as clip-and-save coupon deals. Consumers whose prices are inflated based on their navigational habits are unlikely to know that such clandestine tactics even exist, much less that these tactics are being directed at them personally."); ANNENBERG REPORT, *supra* note 4, at 10.

[64] Celli & Dreifach, *supra* note 55, at 69.

[65] Zarsky, *supra* note 60, at 52. In addition, online sellers can quickly react to consumer behavior and change prices. *See* Jeffrey M. Rosenfeld, *Spiders and Crawlers and Bots, Oh My: The Economic Efficiency and Public Policy of Online Contracts that Restrict Data Collection*, 2002 STAN. TECH. L. REV. 3, ¶ 29, http://stlr.stanford.edu/STLR/Articles/02_STLR_3/index.htm (citing WISEMAN, *supra* note 62, at 39).

One need only visit the Dell Computer website to get a sense of the many different ways that roughly equivalent products can be priced to different consumers. Undoubtedly, Dell is to be commended for the dazzling variety of hardware, software and service options that it offers to its customers, but we would be naïve not to see the price discrimination at work at Dell.com. For example, Dell posts different prices for business, academic and personal home users,[66] while varying the precise hardware and software options available on certain models to certain users.[67] Moreover, coupons for Dell computers, often reflecting savings of 25% to 40% off of the regular price, are offered routinely on websites that link to Dell.com.[68] Yet Dell makes no mention of these coupons on its website, though the company often offers discounts of its own in different amounts on its products. This amounts to a surcharge on the uninitiated—or those unwilling to spend the time and energy to learn the "game" of buying a Dell computer online. Even for those who are willing to master the system, the variety of software and hardware options makes true "apples to apples" comparison shopping for Dell computers a challenging task, and even savvy customers risk paying more than they would under a more simplified system.

Finally, price discrimination may be easier to accomplish in markets for services and information goods.[69] The growth of "versioning" demonstrates this point.[70] A firm can create different versions of goods that can appeal to different groups of consumers and then set different prices for different versions of the goods.[71] For example, software companies can sell educational versions of software to students at a discount with certain features of the premium version of the software disabled.[72] The marginal cost of producing the full version of the program is not likely to be much higher than the marginal cost of producing the student version of the program,[73] so the higher price charged on the premium version transfers surplus to the producer. Like airline business/leisure traveler rules,[74] versioning is a form of second-degree price

[66] Odlyzko, *supra* note 50, at 2.

[67] *See* Dell Home Page, http://www.dell.com (last visited Jan. 30, 2006).

[68] Simply running a search on any major search engine, such as Google or Yahoo, for "Dell coupon codes" brings up many of these sites.

[69] *See* Klock, *supra* note 14, at, 328–31 (discussing the increasing ability of monopolists to segment markets as the economy has become more service- and information-oriented). Weiss & Mehrotra, *supra* note 8, ¶¶ 8–9 (discussing variable pricing facilitated by airline reservation systems).

[70] For an excellent, accessible discussion of versioning, *see* CARL SHAPIRO & HAL R. VARIAN, INFORMATION RULES: A STRATEGIC GUIDE TO THE NETWORK ECONOMY 53–81 (1999); *see also* Odlyzko, *supra* note 50, at 8–9.

[71] *Id*.

[72] *See* Meurer, *supra* note 14, at 73; SHAPIRO & VARIAN, *supra* note 70, at 63.

[73] Actually, in some instances it may be more expensive to create the lower priced version with fewer features. *See* SHAPIRO & VARIAN, *supra* note 70, at 63 ("[W]ith information, it generally costs just about as much to distribute the fancy version as the plain version. In many cases, in fact, production of the low-quality version incurs additional costs, since it is often a degraded form of the high-quality version.").

[74] *See supra* notes 34–39 and accompanying text.

discrimination since the seller varies the good or service in some way that causes buyers to sort themselves by their own choices into different WTP groups.[75] If done shrewdly, the differentiation in the goods will be significant enough to prevent arbitrage because higher reservation price consumers will not want to buy versions aimed at lower reservation price consumers,[76] either from the producer or the initial purchaser.[77]

Undoubtedly, there are perils to the marketing and pricing tactics discussed above. Consumers may attempt to use technology to thwart merchant efforts at price discrimination if they are aware that it is taking place.[78] As such, a merchant may suffer financial repercussions if consumers do become aware of its actions and consider it to be a violation of their trust.[79] Beyond consumer self-help, one might argue that dynamic pricing in cyberspace is sufficiently different from normal offline forms of price discrimination to warrant a different level of regulatory scrutiny.[80] Whether or not this is the case, these evolving practices have drawn renewed attention to economic price discrimination, which leads naturally to the question of how it is currently treated under the law.

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75 *See id*.

76 It might be tempting to say that this is not price discrimination at all, since the good being sold is different. The point, however, is that the price difference does not reflect the production cost difference, so a form of price discrimination is being practiced. *See supra* note 18 and accompanying text.

77 *See* Meurer, *supra* note 11, at 872–73; *see also* Hammer, *supra* note 8, at 886 (discussing methods that producers use to prevent "other more subtle forms of demand-side arbitrage, where high-value consumers are able to select and consume the product actually intended for low-value users.").

78 *See* Garbarino & Lee, *supra* note 44, at 498 ("[T]ransparency and efficiency can go both ways; the Internet has also eased information search and increased interactions among customers, and hence has increased their potential awareness of such price differentiation through such mechanisms as electronic shopping agents, multiple Internet accounts, chat rooms, and customer complaint sites."); Hillman & Rachlinski, *supra* note 58, at 472 (noting that "e-businesses concerned with their reputations might avoid" price discrimination practices); Odlyzko, *supra* note 50, at 4 ("The public's dislike of price discrimination will be combined with new tools for detecting price discrimination. These tools are products of the same technologies that enable sellers to practice differential pricing."). Of course, not all consumers will be aware of the seller's pricing practices. *See* Fred M. Feinberg et al., *Do We Care What Others Get? A Behaviorist Approach to Targeted Promotions*, 39 J. MARKETING RES. 277, 288–89 (2002) ("Although the Internet has greatly increased the likelihood of consumers finding out about deals offered to others, it has not increased it to a certainty: Many consumers may remain unaware of competitive promotions or do not care much about them."); *see also supra* note 65.

79 *See* Joseph P. Bailey, *Internet Price Discrimination: Self-Regulation, Public Policy, and Global Electronic Commerce* 19 (Robert H. Smith Sch. of Bus., Univ. of Md., 1998), *available at* http://www.rhsmith.umd.edu/faculty/jbailey/pub/discrimination.pdf. (discussing potential consumer backlash against price discriminating firms on the Internet); Feinberg et al., *supra* note 78, at 288–89; Garbarino & Lee, *supra* note 44, at 499, 501.

80 Celli & Dreifach, *supra* note 55, at 69–70; Anita Ramasastry, *Web Sites Change Prices Based on Customers' Habits*, CNN.COM, June 24, 2005, http://www.cnn.com/2005/LAW/06/24/ramasastry.website.prices/.

III. AN OVERVIEW OF FEDERAL PRICE DISCRIMINATION LAW

A. The Basics of the Robinson-Patman Act

At the federal level,[81] price discrimination is governed by the Robinson-Patman Act ("RPA"),[82] an extraordinarily controversial law[83] that was passed as an amendment to the Clayton Act in 1936.[84] The Act states in part:

> It shall be unlawful for any person engaged in commerce . . . to discriminate in price between different purchasers of commodities of like

[81] State price discrimination laws are beyond my scope here. *See* 14 HERBERT HOVENKAMP, ANTITRUST LAW ¶ 2419 (2d ed. 2006) ("Several states have a differential pricing provision modeled more or less closely on the Robinson-Patman Act. By and large their coverage mimics that of the federal statute, with a few exceptions."); Erwin S. Barbre, *Annotation, Validity and Construction of State Statutes Forbidding Area Price Discrimination*, 67 A.L.R. 3d 26 (1975).

[82] For overviews of the RPA, *see* Hugh C. Hansen, *Robinson-Patman Law: A Review and Analysis*, 51 FORDHAM L. REV. 1113 (1983); HOVENKAMP, *supra* note 81, ch. 23; 3 EARL W. KINTNER & JOSEPH P. BAUER, FEDERAL ANTITRUST LAW (1983 & 2005 Supp.); THOMAS V. VAKERICS, ANTITRUST BASICS §§ 8.01–8.03 (2004). A brief, non-technical treatment of the RPA can be found in AMERICAN BAR ASSOCIATION SECTION OF ANTITRUST LAW, A PRIMER ON THE FEDERAL PRICE DISCRIMINATION LAWS: A GENERAL REVIEW OF THE ROBINSON-PATMAN ACT FOR BUSINESS MANAGERS (3d ed. 2005).

[83] As one treatise notes: "There are literally hundreds of pieces praising, criticizing and analyzing the Act." KINTNER & BAUER, *supra* note 82, at 689 n.5 (collecting a representative sample of sources); *see also* Sherie L. Coons, Note, *Robinson-Patman Act Jurisdiction over Retail Sales: A Reexamination of the Cases and the Case for Reform*, 21 J. CORP. L. 541, 545 n.30 (1996) (collecting criticisms of the RPA); HOVENKAMP, *supra* note 81, ¶ 2340; VAKERICS, *supra* note 82, § 8.01 (noting that "the Robinson-Patman Act has been criticized continually since it was passed by Congress in 1936").

[84] According to conventional historical accounts, the RPA was intended to protect small independent retailers from competition from large chain stores during the Great Depression. *See* Augusta News Co. v. Hudson News Co., 269 F.3d 41, 44–45 (1st Cir. 2001) ("The Robinson-Patman Act, unlike the ordinary antitrust laws, was designed less to protect competition than (in the midst of the Great Depression) to protect small businesses against chain stores. A particular target were the discounts that manufacturers furnished to large chain stores."); HOVENKAMP, *supra* note 81, ¶ 2302, at 11 ("The central 'evil' targeted by the Robinson-Patman Act was the *buying* power of large chain stores such as A&P."); Coons, *supra* note 83, at 545 ("Congress passed the Robinson-Patman Act during the Depression in an effort to protect small, independent businesses from the new buying power, profitability, and market share of grocery chain stores."); FREDERICK M. ROWE, PRICE DISCRIMINATION UNDER THE ROBINSON-PATMAN ACT 11–23 (1962) (tracing legislative history of the RPA). One scholar has questioned the conventional protectionist account of the RPA. *See* Andrew I. Gavil, *Secondary Line Price Discrimination and the Fate of* Morton Salt: *To Save It, Let It Go*, 48 EMORY L.J. 1057, 1074–80 (1999); *see also* JOHN S. MCGEE, THE ROBINSON-PATMAN ACT AND EFFECTIVE COMPETITION 172 (1979) ("[A] Congress which weighed the evidence and debated the problem of price discrimination almost entirely with respect to the chain store movement, wanted to prevent 'undue discriminations' wherever they might occur, even if doing so would deny consumers the benefit of cost-reducing techniques."). For a recent historical treatment, see Richard C. Schragger, *The Anti-Chain Store Movement, Localist Ideology, and the Remnants of the Progressive Constitution, 1920–1940*, 90 IOWA L. REV. 1011 (2005).

> grade and quality . . . where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them.[85]

Although the Supreme Court has stated that the term "price discrimination" found in the RPA covers any difference in price,[86] the scope of the RPA is narrower than it initially appears. First, as the text of the statute indicates, the Act covers only the sale of commodities,[87] not services, thus excluding a large swath of economic activity from its purview.[88] Second, the Act itself states that price discrimination is permissible if it is based upon cost differences,[89] meeting a competitor's price,[90] and changing market conditions.[91]

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[85] 15 U.S.C. § 13(a) (2000). The RPA also forbids other preferential behavior, such as granting promotional allowances and services. *See* 15 U.S.C. § 13(d), (e) (2000); *see also* Guides for Advertising Allowances and Other Merchandising Payments and Services, 16 CFR pt. 240 (also known as the "Fred Meyer Guidelines").

[86] *See* Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 220 (1993); FTC v. Anheuser-Busch, Inc., 363 U.S. 536, 549 (1960).

[87] *See* Hansen, *supra* note 82, at 1125–28 ("The Act applies only if two or more consummated sales of commodities of like grade and quality are made at discriminatory prices by the same seller to two or more different purchasers contemporaneously or within the same approximate time period."); 1 WILLIAM C. HOLMES, INTELLECTUAL PROPERTY AND ANTITRUST LAW § 7:4 (2006) ("Non-sale transactions such as, licenses, consignments, agencies and leases fall outside the proscriptions of the Robinson-Patman Act . . . In addition, both sales transactions constituting the alleged discrimination must have been entered into, so that a sale plus a mere offer to sell is insufficient, as is a sale plus a refusal to sell."). In addition, the sales must be actually completed. *See* Hansen, *supra* note 82, at 1125–26 n.79; Reeder-Simco GMC, Inc. v. Volvo GM Heavy Truck Corp., 374 F.3d 701, 708 (8th Cir. 2004), *rev'd*, 126 S. Ct. 860 (2006) (noting that many courts have held that "price discrimination in the competitive bidding process does not violate the RPA because only one of the two competitors actually makes a purchase").

[88] *See* HOVENKAMP, *supra* note 19, § 14.6d, at 583 (noting that the RPA does not cover intellectual property rights or business services and that "[t]his limitation is particularly irrational because price discrimination in service markets is much more prevalent than in the sale of goods"); Klock, *supra* note 14, at 358 (noting that the RPA is under-inclusive because it "does not apply to transactions involving services, which represent the bulk of our economy.").

[89] 15 U.S.C. § 13(a) (2000) ("[N]othing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered.").

[90] *See* 15 U.S.C. § 13(b) ("[N]othing herein contained shall prevent a seller rebutting the prima-facie case . . . by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor . . .").

[91] *See* 15 U.S.C. § 13(a):

> That nothing herein contained shall prevent price changes from time to time where in response to changing conditions affecting the market for or the marketability of the goods concerned, such as but not limited to actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned.

Third, the Act has a surprisingly stringent "interstate commerce" jurisdictional requirement,[92] which excludes many intrastate sales,[93] and makes the Act's reach narrower than other antitrust laws.[94]

B. The RPA's Competitive Harm Requirement

Most important, the RPA's competitive harm requirement[95] removes most differential or dynamic pricing practices in consumer goods from the purview of the Act. This point requires some explanation. The Supreme Court has stated: "Robinson-Patman does not 'ban all price differences charged to different purchasers of commodities of like grade and quality,' rather, the Act proscribes 'price discrimination only to the extent that it threatens to injure competition.'"[96] Courts typically recognize three types of injury under the RPA: primary line, secondary line and tertiary line discrimination.[97]

> Primary line discrimination is evaluated for its tendency to diminish competition between the discriminating seller and its rival, whose customers typically are the beneficiaries of the discriminating seller's lower prices. Secondary line discrimination is evaluated for its tendency to diminish competition between the recipient of the better price, the favored purchaser, and its rival, a disfavored purchaser. Tertiary line discrimination affects the competing customers of a favored and disfavored purchaser, respectively.[98]

[92] *See* Able Sales Co. v. Compania de Azucar, 406 F.3d 56, 62–65 (2005) (discussing and applying RPA's "in commerce" requirement).

[93] *See* Coons, *supra* note 83, at 541; Hansen, *supra* note 82, at 1128 n.86; HOLMES, *supra* note 87, § 7:3.

[94] VAKERICS, *supra* note 82, § 8.03[1][f] ("[C]hallenged transactions must be 'in' interstate commerce. By contrast, a transaction challenged under the Sherman Act need only 'affect' interstate commerce. Thus, the jurisdictional scope of the Robinson-Patman Act is narrower than that of the Sherman Act.").

[95] *See* 15 U.S.C. § 13(a) (forbidding price discrimination only "where the effect of such discrimination *may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition.*") (emphasis added).

[96] Volvo Trucks N. Am., Inc. v. Reeder-Simco GMC, Inc., 126 S. Ct. 860, 870 (2006) (quoting Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 220 (1993)).

[97] In theory, additional levels of discrimination are possible. *See* Perkins v. Standard Oil Co., 395 U.S. 642, 647–48 (1969) (finding "fourth level" injuries cognizable under the RPA).

[98] Gavil, *supra* note 84, at 1058 n.2; *see also* Coons, *supra* note 83, at 546–47 ("Where a plaintiff sues its competitor alleging that the competitor engaged in discriminatory pricing in the market in which the plaintiff and the defendant compete, the plaintiff alleges 'primary-line' injury. Where the plaintiff is a buyer suing its seller for differential pricing among sales to the buyer and the buyer's competitors, the plaintiff alleges a 'secondary-line' injury."); HOLMES, *supra* note 87, § 7:8; Hansen, *supra* note 82, at 1125–26 n.79; VAKERICS, *supra* note 82, § 8.03[h].

Primary and secondary line cases currently differ in terms of the RPA's "competitive harm" requirement.[99] Under *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*,[100] in primary line or predatory pricing cases[101] brought under either the RPA or Section 2 of the Sherman Act,[102] the Supreme Court explicitly requires plaintiffs to prove that the price discriminating firm is causing economic harm to overall consumer welfare, not simply injury to a rival firm.[103] To accomplish this, a plaintiff must show that "the prices complained of are below an appropriate measure of its rival's costs,"[104] and that the seller "had a reasonable prospect . . . of recouping its investment in below-cost prices."[105] As Herbert Hovenkamp explains, predatory pricing plaintiffs must allege that a rival firm is "charging below cost prices today in order to earn monopoly prices tomorrow."[106]

The competitive harm requirement in secondary line cases is less onerous. Recall that these are cases where a purchaser is claiming that a seller's discriminatory pricing practices favor other purchasers.[107] Currently, there are two ways to establish competitive harm in secondary line cases. First, such

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[99] Herbert Hovenkamp's comments were especially helpful as I worked through the issues regarding competitive harm that are discussed in this subsection. Although the overview presented in the text is sufficient for my purposes here, those who are interested in a deeper look at these issues are referred to Gavil, *supra* note 84; Herbert Hovenkamp, *The Robinson-Patman Act and Competition: Unfinished Business*, 68 ANTITRUST L.J. 125 (2000); Paul H. LaRue, *Robinson-Patman Act in the Twenty-First Century: Will the* Morton Salt *Rule Be Retired?*, 48 SMU L. REV. 1917 (1995).

[100] 509 U.S. 209, 220 (1993).

[101] *See* HOVENKAMP, *supra* note 19, § 8.8, at 364 (explaining that primary line cases involve claims of price predation).

[102] 15 U.S.C. § 2 (2000) ("Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony. . .").

[103] *See* Gavil, *supra* note 84, at 1061 (stating that the *Brooke Group* Court "suggested . . . that proof of generalized injury to competition may be required to establish certain types of primary line price discrimination"); Hovenkamp, *supra* note 99, at 134 (arguing that *Brooke Group* requires a "showing of probable anticompetitive effects in the traditional antitrust sense of reduced output and higher prices in a properly defined relevant market"); LaRue, *supra* note 99, at 1922–23 (discussing *Brooke Group*'s focus on harm to competition, not competitors, in primary line cases).

[104] *See Brooke Group Ltd.*, 509 U.S. at 222.

[105] *See id.* at 224. Herbert Hovenkamp makes the point a bit more clearly by explaining that the Supreme Court in *Brooke* held "the fundamental inquiry in Sherman Act and Robinson-Patman predatory pricing cases was the same: does the evidence indicate that the defendant engaged in predatory pricing with the reasonable expectation that present below-cost prices would be more than offset by future monopoly (or oligopoly) prices?" HOVENKAMP, *supra* note 19, § 8.8, at 368.

[106] HOVENKAMP, *supra* note 19, § 8.8, at 367.

[107] *See* Volvo Trucks N. Am., Inc. v. Reeder-Simco GMC, Inc., 126 S. Ct. 860, 870 (2006) ("Secondary-line cases . . . involve price discrimination that injures competition among the discriminating seller's customers . . . cases in this category typically refer to 'favored' and 'disfavored' purchasers."); Falls City Indus., Inc. v. Vanco Beverage, Inc., 460 U.S. 428 (1983).

harm can be proved directly by showing that disfavored competitors lost sales or profits as a result of the discrimination.[108] Second, a plaintiff can use the presumption set forth by the Court in *FTC v. Morton Salt Co.*,[109] under which an "injury to competition is established prima facie by proof of a substantial price discrimination between competing purchasers over time."[110] Some observers have argued that the *Morton Salt* presumption is too lenient[111] and that it is based on the unjustified factual assumption that competition itself is presumptively harmed by reseller price differentials.[112]

There is thus a tension between the current competitive harm standards in primary line price discrimination cases, which are governed by the strict rules set forth in *Brooke Group*, and the more lax standards enunciated by *Morton Salt* and its secondary line progeny.[113] One might argue that defendants in a secondary line case should be able to rebut the presumption of competitive harm by showing that overall competition or consumer welfare has not been harmed. As one author put it:

> The key dispute with regard to secondary line injury is whether the plaintiff must plead and prove an impairment of competition generally in a relevant market, as the U.S. Supreme Court seemed to suggest over a decade ago, or whether injury to a single plaintiff's ability to compete is enough to establish a violation, as several circuits have recently suggested.[114]

In a recent secondary line case, the Supreme Court made two relevant statements showing judicial suspicion of the traditional purposes of the RPA.[115] First, the court cited *Brooke Group* for the proposition that the RPA should be

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[108] *See Volvo Trucks N. Am., Inc.*, 126 S. Ct. at 870 ("A hallmark of the requisite competitive injury . . . is the diversion of sales or profits from a disfavored purchaser to a favored purchaser."); *Falls City Indus., Inc.*, 460 U.S. at 435, 437–38 (direct evidence of lost sales satisfied RPA § 2(a)).

[109] 334 U.S. 37 (1948).

[110] *Falls City Indus., Inc.*, 460 U.S. at 435 (citing *Morton Salt Co.*, 334 U.S. at 46, 50–51); *see also* LaRue, *supra* note 99, at 1920 ("In the majority of secondary line cases over the years, once the inference of injury was made, it was given virtually conclusive effect.").

[111] As one critic states: "Based on *Brooke Group*'s teaching, the *Morton Salt* rule appears to be too solicitous of competitors, too little concerned with competition, and not at all concerned with the consumer welfare." LaRue, *supra* note 99, at 1925.

[112] *See* Hovenkamp, *supra* note 99, at 129 (referring to the *Morton Salt* presumption as "not merely false" but "nonsense.").

[113] Courts have noted this tension. *See, e.g.*, George Haug Co. v. Rolls Royce Motor Cars Inc., 148 F.3d 136, 142 (2d Cir. 1998).

[114] Jeffrey W. Lorell, *Price Discrimination and the Robinson-Patman Act*, N.J. LAW., June 2004, at 30, 31–32. *See also* Chroma Lighting v. GTE Prods. Corp., 111 F.3d 653, 658 (9th Cir. 1997) (holding that "in a secondary-line Robinson-Patman case, the *Morton Salt* inference that competitive injury to individual buyers harms competition generally may not be overcome by proof of no harm to competition"); Coastal Fuels of Puerto Rico, Inc. v. Caribbean Petroleum Corp., 79 F.3d 182, 193 (1st Cir. 1996) (holding that "the *Morton Salt* rule continues to apply to secondary-line injury cases"); *George Haug Co.*, 148 F.3d at 144 (adopting view of First Circuit in *Coastal Fuels*); Gavil, *supra* note 84, at 1083–86 (surveying case law).

[115] Volvo Trucks N. Am., Inc. v. Reeder-Simco GMC, Inc., 126 S. Ct. 860 (2006).

construed "'consistently with broader policies of the antitrust laws.'"[116] Second, the Court indicated that it "would resist interpretation geared more to the protection of existing *competitors* than to the stimulation of *competition*."[117] Both of these statements suggest that the Court is troubled by the fact that Robinson-Patman seems to permit secondary line claims even where it is sellers not consumers who are harmed.

In the end, though, it is not important for our purposes whether it is desirable to make it even more difficult for plaintiffs to prove secondary-line price discrimination claims by adding a general "harm to competition prong."[118] Even under the most liberal current interpretation of the RPA, consumer price discrimination claims fail because end-use buyers are not in competition with other buyers who are receiving preferential pricing treatment.[119] Thus, the RPA does not require retailers to treat these consumers equally.[120] Mark Klock criticizes the Act on this basis:

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[116] *Id.* at 873 (quoting Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 220 (1993) (citing Great Atl. & Pac. Tea Co. v. FTC, 440 U.S. 69, 80 n.13 (1979))).

[117] *Id.* at 872.

[118] *See* John B. Kirkwood, *Buyer Power and Exclusionary Conduct: Should* Brooke Group *Set the Standards for Buyer-Induced Price Discrimination and Predatory Bidding?*, 72 ANTITRUST L.J. 625, 635 (2005):

> Both case law and legislative history indicate . . . that the fundamental purpose of prohibiting non-cost-justified secondary line discrimination is not to promote consumer welfare--the purpose of prohibiting primary line discrimination--but to protect small firms from "unfair" competition. As virtually all recent cases conclude, this distinct purpose indicates that *Brooke Group* should not apply to the secondary line offense.

[119] *See Volvo Trucks N. Am., Inc.*, 126 S. Ct. at 872 (plaintiff Volvo truck dealer could not show sufficient, actual competition between itself and a competing Volvo truck dealer to sustain RPA claim); Infusion Res., Inc. v. Minimed, Inc., 351 F.3d 688, 693 (5th Cir. 2003), (plaintiff failed to show "actual competition with a favored purchaser at the time of the alleged price discrimination"), *cert. denied*, 542 U.S. 920 (2004); Lycon, Inc. v. Juenke, 250 F.3d 285, 289 (5th Cir. 2001), *cert. denied*, 534 U.S. 892 (2001) (manufacturer's practice of charging wholesale distributors higher prices than end users who purchased equipment directly from manufacturer did not constitute illegal price discrimination because end users did not compete with distributors for resale); *George Haug Co.*, 148 F.3d at 144 (authorized automobile parts and service provider sufficiently alleged that it competed with favored purchaser in relevant market). *See also* Accurate Control Systems v. Neopost, Inc., No. 00C50128, 2002 WL 1379132, at *2 (N.D. Ill. June 25, 2002) (firm did not violate section 13(a) by making direct sales to end-user customers at prices lower than what it sold to its dealers); Chi. Sugar Co. v. Am. Sugar Refining Co., 176 F.2d 1, 10 (7th Cir. 1949), *cert. denied*, 338 U.S. 948 (1950) ("There is nothing in the Act that prevents a seller of a commodity from eliminating middlemen from its distributive system and selling its commodity directly to consumers if it wishes to do so; and if it chooses it may distribute a part of its commodity direct and a part through wholesale distributions."); Godfrey v. Pulitzer Publ'g Co., 276 F.3d 405, 410 (8th Cir. 2002) (secondary line claim failed as a matter of law because purchasers were not competitors).

[120] *See* Ramon A. Avila & Teresa K. Avila, *Rebates: An Ethical Issue?*, 1 MID-AM. J. BUS. 41, 44 (1986); CARLTON & PERLOFF, *supra* note 9, at 307 ("Apparently, it is not an antitrust violation to price discriminate among final consumers, but it is a violation to price discriminate among firms so as to affect their 'competition' under the Robinson-Patman Act."); Foer, *supra* note 57, at 61 (noting that "Robinson-Patman does not cover end-use

> [T]here are . . . problems with the requirement that price discrimination must result in a reduction in competition to be illegal . . . . [T]he requirement is often interpreted to mean that those who are discriminated against must be in a competitive relationship with those who are not discriminated against. This interpretation bars consumers from bringing actions for price discrimination and permits only businesses to bring actions for price discrimination. Thus, businesses are free to discriminate against consumers, while also being permitted to bring treble damage actions for discrimination. This is not a rational policy.[121]

An example may clarify this point. Absent any applicable statutory defense, Sony would be prohibited from selling its television sets to local electronics stores at higher prices than it charges Wal-Mart.[122] This is the classic secondary line case, since it is the buyer's purchasing power that forces the manufacturer to treat retailers differently. For the same reason, it would also be unlawful for Sony to provide Wal-Mart with advertising or promotional support that it did not also proportionately provide to local electronics stores.[123] On the other hand, absent fraud, it would not be unlawful for Wal-Mart salespeople to haggle with their customers and sell Sony television sets to consumers at different prices based upon their willingness to pay—the end consumers in this case are not in competition with each other.[124] In theory, customers who are displeased with such a pricing practice have a ready recourse in the marketplace—they can take their business to the seller's competitors, which in the long run will have the effect of driving out the objectionable pricing practice.[125] One scholar explains: "[T]he consumer, as ultimate beneficiary, falls outside the statutory scheme: Retailers are permitted—indeed, encouraged—to charge different prices to different consumers. But, as final beneficiary, the consumer must be free to extract the lowest prices from the most efficient competitors."[126]

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consumers"); Klock, *supra* note 14, at 358 (noting that the RPA "is not generally believed to apply to consumer transactions, although an argument could be made that it does apply to such transactions"); Weiss & Mehrotra, *supra* note 8, ¶ 25 ("[B]ecause the Act is concerned chiefly with preserving the structural integrity of competitive markets, business-to-consumer e-commerce is unlikely to be affected by the statute's provisions.").

[121] Klock, *supra* note 14, at 365–66; *see also* Avila & Avila, *supra* note 120, at 44:

> Price discrimination in commercial transactions is illegal under the Robinson-Patman Act . . . [S]ellers cannot charge competing buyers different prices for essentially the same products . . . The law seems to recognize the importance of equity in commercial but not consumer transactions. Despite recognition of the ethical principle in the Robinson-Patman Act, no legislation currently exists protecting consumers against this type of discrimination.

[122] *See* 15 U.S.C. § 13(a) (2000).

[123] *See Id.* § 13(e).

[124] There may be cases in which it is difficult to determine whether two buyers are truly in competition with each other, but end-use consumers will rarely present such a problem.

[125] Admittedly, a failure of such self-correction could indicate a market failure that requires some remediation. *See generally* Gilo & Porat, *supra* note 26.

[126] RUDOLPH J.R. PERITZ, COMPETITION POLICY IN AMERICA, 1888–1992: HISTORY, RHETORIC, LAW 153 (1996).

C. General Consumer Law Pricing Principles

The understanding that the RPA does not protect end-use consumers against differential pricing practices is consonant with general consumer law pricing principles. A consumer law treatise sums up the matter as follows: "As a general matter of federal law, retailers are under no obligation to disclose their pricing structure to consumers, and in the absence of some duty to disclose, retailers may charge different prices for the same goods or service to different groups of consumers without disclosing that fact."[127] In *Langford v. Rite Aid of Alabama, Inc.*,[128] the plaintiffs argued that Rite Aid violated state and federal law[129] by charging more to customers who lacked insurance and failing to disclose these pricing practices.[130] The Eleventh Circuit rejected the contention that Rite Aid had a legal obligation to disclose its differential pricing practices:

> As a general matter of federal law, retailers are under no obligation to disclose their pricing structure to consumers. . . . Plaintiffs have failed to identify any federal case where such a duty was imposed on retailers; in fact, variable pricing is the norm in many industries. Airlines frequently charge different groups of consumers different rates for the same seat, hotels often charge different rates to different consumers for the same room, and car dealerships sell identical vehicles for a variety of prices, depending upon the identity (and savvy) of the consumer. There are a number of legitimate business reasons for doing this, obnoxious as it may seem for the individual consumer forced to purchase an item at a different price from his friends. Differential pricing alone is not a fraudulent practice.[131]

Other courts have reached similar conclusions.[132] In *Katzman v. Victoria's Secret Catalogue*,[133] the plaintiff brought a civil RICO[134] action against Victoria's Secret, claiming that the company's practice of sending catalogs with different prices and discount offers to different consumers constituted mail fraud.[135] Although two commentators termed the plaintiff's arguments as

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[127] HOWARD J. ALPERIN & ROLAND F. CHASE, CONSUMER LAW: SALES PRACTICES AND CREDIT REGULATION § 71, at 39–40 (2004 Supp.); *see also* Langford v. Rite Aid of Ala., Inc., 231 F.3d 1308, 1313 (11th Cir. 2000) ("As a general matter of federal law, retailers are under no obligation to disclose their pricing structure to consumers.").

[128] 231 F.3d at 1308.

[129] The plaintiffs attempted to state a civil RICO action based upon mail and wire fraud. *See id.* at 1310–11.

[130] *Id*.

[131] *Id*. at 1313–14.

[132] *See, e.g.*, Bonilla v. Volvo Car Corp., 150 F.3d 62, 71 (1st Cir. 1998) (observing that "there is nothing in the law of fraud that prevents even a single seller from charging different markups in different markets so long as there is no affirmative misrepresentation").

[133] 167 F.R.D. 649 (S.D.N.Y. 1996), *aff'd*, 113 F.3d 1229 (2d Cir. 1997).

[134] Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961, 1962 (2000).

[135] *Katzman*, 167 F.R.D. at 653–54.

"innovative,"[136] the district court held that Victoria's Secret had no duty to sell their goods at the same price to different buyers.[137] In fact, the court found the RICO argument sufficiently groundless to warrant the imposition of Rule 11[138] sanctions upon the plaintiff's attorney.[139]

In sum, neither the RPA nor any other federal law mandates an equal pricing policy for end consumers,[140] unless the retailer's unequal pricing violates some other applicable statutory or constitutional provision.[141] The expectation, whether plausible or not, is that consumers are best situated to learn about seller pricing practices and to choose providers of goods and services whose pricing practices comport with their preferences.[142]

IV. THE INCHOATE, MISGUIDED CRY FOR CONSUMER EQUALITY

A. The Intuitive Appeal of Equality

The discussion thus far has illustrated that price discrimination in consumer goods and services is pervasive and generally legal. Moreover, if current trends hold, technological advances will make both on- and off-line price discrimination even more prevalent in the years ahead.[143] Nevertheless, although it is often lawful, price discrimination is extraordinarily unpopular with consumers, as James Boyle notes:

> Lay people often react to differential pricing for the same good with a sense of unfairness. No matter how many times they are lectured by the

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[136] Weiss & Mehrotra, *supra* note 8, ¶ 27.

[137] *See Katzman*, 167 F.R.D. at 656 ("Plaintiffs do not identify any duty which requires Defendants to sell their goods to all buyers at the same prices. Furthermore, they have not, and cannot, identify any basis in federal or state statutes or the common law for imposing on the Defendants a duty to disclose VSC's promotional practices.").

[138] *See* FED. R. CIV. P. 11.

[139] *See Katzman*, 167 F.R.D. at 659–61. The court explained:

> As even a cursory examination of the requirements for bringing suit under RICO would have revealed the impossibility of the claim's success, Plaintiffs' filing was objectively unreasonable and therefore constitutes a Rule 11 violation. . . . [W]here claims are so far deficient in alleging statutory requirements as in the present case, whether the violation is deliberate or merely the result of "extraordinarily shoddy" research, the filing warrants the imposition of sanctions.

Id. at 660–61.

[140] *See supra* notes 119–26 and accompanying text. There are specific, misleading pricing practices that may be forbidden under federal, state or local law. *See, e.g.*, Guides Against Deceptive Pricing, 16 C.F.R. pt. 233 (2005) (dealing with former price comparisons, retail price and comparable value comparisons, manufacturers' suggested retail/list prices, bargain offers based upon purchase of other merchandise, and other price comparisons).

[141] *See* Weiss & Mehrotra, *supra* note 8, ¶ 28 ("As long as the price differences are based on reasonable business practices such as rewarding loyal customers and do not discriminate against race, gender, or other impermissible categories, dynamic pricing appears to be legal.").

[142] *See* Langford v. Rite Aid of Ala., Inc., 231 F.3d 1308, 1314 (11th Cir. 2000).

[143] *See supra* Part II.D.

> economists that it is actually to the benefit of all that producers be able to charge different prices to groups with different ability and willingness to pay, the popular reaction is normally, "that's not fair."[144]

This anger was demonstrated after consumers learned that Amazon.com, the world's largest online retailer,[145] was charging different prices to different consumers for the same good.[146] Amazon.com claimed that it was merely conducting random price testing,[147] but skeptical consumers believed that the differential prices were based on personal demographic information and purchase histories possessed by Amazon.com.[148] To quell the controversy, the company gave refunds to affected consumers and Amazon.com founder and CEO Jeff Bezos stated that the company would never test prices based on customer demographics,[149] even though Amazon.com's actions were legal.[150]

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[144] James Boyle, *Cruel, Mean, or Lavish? Economic Analysis, Price Discrimination and Digital Intellectual Property*, 53 VAND. L. REV. 2007, 2038–39 (2000).

[145] Press accounts routinely refer to Amazon.com in this manner. *See, e.g.*, *Amazon.com to Cut Number of Merchants*, N. Y. TIMES, May 12, 2005, at C11; Bob Tedeschi, *Web Merchants Brace for the Inevitable*, N.Y. TIMES, June 27, 2005, at C8; Greg Wiles, *Harry Potter Books Flying Off the Shelves*, CHI. SUN-TIMES, July 19, 2005, at 55.

[146] For a newspaper account of the Amazon.com pricing controversy, see David Streitfeld, *On the Web, Price Tags Blur; What You Pay Could Depend on Who You Are*, WASH. POST, Sept. 27, 2000, at A1. Law review treatments can be found in the following sources: Celli & Dreifach, *supra* note 55, at 66–67; Tammy Renée Daub, Note, *Surfing The Net Safely and Smoothly: A New Standard for Protecting Personal Information from Harmful and Discriminatory Waves*, 79 WASH. U. L.Q. 913, 919–20 (2001); Weiss & Mehrotra, *supra* note 8, ¶ 1; Christopher Paul Boam, *The Internet, Information and the Culture of Regulatory Change: A Modern Renaissance*, 9 COMMLAW CONSPECTUS 175, 179–80 (2001).

[147] *See* Press Release, Amazon.com, Amazon.com Issues Statement Regarding Random Price Testing (Sept. 27, 2000), *available at* http://phx.corporate-ir.net/phoenix.zhtml?c=97664&p=irol-newsArticle_Print&ID=229620&highlight [hereinafter Amazon.com Press Release].

[148] *See* Michael Rappa, *Courting the Well-Informed Customer*, COMPUTERWORLD, Nov. 6, 2000, at 34; Daub, *supra* note 146, at 919–20 (noting that skepticism was heightened "in light of Amazon's announcement two weeks prior to the price variation discovery that customers' personal information (including past buying patterns and shopping preferences) was a business asset that could be shared with third parties") (citing Keith Regan, *Amazon's Friendly Deception*, E-COMMERCE TIMES, Sept. 18, 2000, http://www.ecommercetimes.com/news/viewpoint2000/view-000918-2.shtml); Keith Regan, *Amazon Announces Controversial Privacy Policy*, E-COMMERCE TIMES, Sept. 1, 2000, http://www.ecommercetimes.com/perl/story/4180.html. Ironically, consumers claimed that loyal customers were quoted *higher* prices. *See* Rappa, *supra* note 148, at 34.

[149] Amazon.com Press Release, *supra* note 147. This may have been Amazon.com's second experiment with dynamic pricing. *See* Jessica Davis, *American Consumers Will Force E-Tailers to Just Say No to Dynamic Pricing*, INFOWORLD, Oct. 9, 2000, at 116, *available at* http://www.infoworld.com/articles/op/xml/00/10/09/001009opprophet.html; Streitfeld, *supra* note 146. An Amazon.com spokesperson went somewhat further and stated that the company would never engage in variable pricing. *See* Annette Cardwell, *Now is the Price Right?*, ZIFF DAVIS SMART BUS. FOR NEW ECON., Feb. 2001, at 36.

[150] Astute commentators noted this shortly after the controversy subsided. *See* Weiss & Mehrotra, *supra* note 8, ¶¶ 24–28. For more on the legality of price discrimination, *see supra* Part III.C.

Regardless of whether Amazon.com was truly engaged in dynamic pricing, it is not surprising that the company's pricing experiment touched a nerve.[151] Public distaste with dynamic and differential pricing has been documented in a wide variety of contexts.[152] A report recently issued by the Annenberg Public Policy Center at the University of Pennsylvania[153] concluded that consumers "overwhelmingly object to . . . all forms of price discrimination as ethically wrong."[154] The Annenberg Report reported poll findings suggesting that consumers find price discrimination distasteful, even in contexts where there are benefits to the consumers, such as rewards for loyal customers.[155]

Not only do consumers have a "visceral negative" reaction to merchants selling the same good or services to different consumers at different prices,[156] but experts' discussions of price discrimination slip easily into rhetoric regarding the general unfairness of the unequal treatment that consumers face under a price discrimination regime.[157] New York Times columnist Paul Krugman, a professor of economics at Princeton University, followed a lucid explanation of the potential economic benefits of price discrimination with the statement that "dynamic pricing is undeniably unfair: some people pay more just because of who they are."[158] Mark Klock, a law professor with a Ph.D. in economics, has stated that while the perfectly discriminating monopolist is difficult to attack on economic grounds, "concepts of social justice and equity" make such monopolists "despicable."[159] Notably, neither Krugman nor Klock explain exactly why pricing based on willingness to pay is "unfair" or "despicable." But both comments show that the notion that all consumers

[151] Amazon.com is not the only company that has experimented with dynamic pricing. *See* Michael Vizard et al., *Suppliers Toy with Dynamic Pricing*, INFOWORLD, May 14, 2001, at 28 (discussing investigations of dynamic pricing by IBM, Compaq, Dell, and Hewlett-Packard).

[152] *See* Davis, *supra* note 149, at 116 ("Nothing breeds outrage in the heart of an American consumer as much as the notion that he or she was charged more than someone else was for the same product."); Garbarino & Lee, *supra* note 44, at 501 ("Consumers have historically considered demand-based pricing, such as dynamic pricing, to be unacceptable . . . [R]esearchers have found that the majority of consumers feel raising prices to cope with excess demand is unfair."); Levine, *supra* note 36, at 4 ("Price discrimination is often unpopular, at least among those paying the higher of the discriminatory prices."); Odlyzko, *supra* note 50, at 4 ("People do not like being subjected to dynamic pricing. There is abundant evidence of this, as shown, for example, in reactions to airline yield management and the moves to extend such practices to other areas.").

[153] *See* ANNENBERG REPORT, *supra* note 4, at 4.

[154] *See id*..

[155] *See id*. ("72% disagree that 'if a store I shop at frequently charges me lower prices than it charges other people because it wants to keep me as a customer more than it wants to keep them, that's OK.'").

[156] *See* Weiss & Mehrotra, *supra* note 8, ¶ 19.

[157] *See* Streitfeld, *supra* note 146 ("'Dynamic pricing is the new reality, and it's going to be used by more and more retailers,' said Vernon Keenan, a San Francisco Internet consultant. 'In the future, what you pay will be determined by where you live and who you are. It's unfair, but that doesn't mean it's not going to happen.'").

[158] Paul Krugman, *What Price Fairness?*, N.Y. TIMES, Oct. 4, 2000, at A35.

[159] *See* Klock, *supra* note 14, at 328 (citing Krugman, *supra* note 158).

should be treated equally has intuitive appeal.[160] There is no need to resort to complex economic principles or socio-legal jargon to explain the basic idea of consumer equality to producers, consumers, and legislators.[161] In fact, we have a long, distinguished history of equality-based jurisprudence in constitutional law, to which supporters of equality in consumer law can analogize.[162] An equality standard seems to clearly and easily remedy the complaint that it is wrong or unfair to treat consumers differently based upon who they are no matter what the circumstances. The equality ideal is so appealing, so evidently correct, that it seems to be churlish to ask: why shouldn't all consumers be treated equally? The next subsection aims to answer this question.

B. The Benefits of Inequality

Equality is an enticing but ill-suited standard for consumer pricing policy. A broad, enthusiastically enforced principle of consumer equality would mean the end of all forms of economic price discrimination. While this outcome might be appealing from the perspective of consumers who feel ripped off by particular differential pricing practices, economic analysis suggests that a complete ban on price discrimination might not be good for society as a whole. Understanding why this is so requires a discussion of the welfare effects of perfect and imperfect forms of price discrimination.

Under perfect (first-degree) price discrimination, every possible sale is being made—no one who values the product at greater than the seller's reservation price is denied the opportunity to buy the product. Accordingly, the outcome under first-degree price discrimination is arguably socially optimal, though producers benefit to the detriment of consumers by obtaining the consumers' entire surplus.[163] James Boyle explains:

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[160] Because the intellectual or social movement in favor of consumer equality is embryonic, my comments here may be taken as an attack on a straw person. Although I admit that this is a possibility, I think that it is important to identify the central tenets of this emerging intellectual position so that commentators and scholars can challenge advocates who rely on consumer equality as a normative principle.

[161] Contrast this with the economics required to explain the potential benefits of price discrimination. *See infra* notes 163–76 and accompanying text.

[162] *See generally* ERWIN CHEMERINSKY, CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES §§ 9.1–9.7.4 (1997) (surveying equal protection law).

[163] *See* Boyle, *supra* note 144, at 2026 ("We know that *either* perfect competition or monopoly with perfect price discrimination will produce Pareto optimal results. (No change in the distribution of entitlements will produce a gain large enough for the 'winners' under such a change, to compensate the 'losers' and still come out ahead.)") (emphasis in original); Gilo & Porat, *supra* note 26, at 1021 ("If the supplier were able to charge each consumer exactly what the consumer was willing to pay ('perfect price discrimination') such pricing would be socially efficient and superior to uniform pricing since all consumers who value the product more than the marginal costs of supplying it would receive the product."). One must also take into account the social costs of implementing and maintaining first-degree price discrimination. *See* POSNER, *supra* note 12, at 284; HOVENKAMP, *supra* note 19, § 14.5, at 577.

> Either perfect competition, or monopoly with perfect price discrimination will produce an optimal economic outcome. The differences are distributional. Perfect competition moves consumer surplus to the pockets of consumers. Monopoly coupled with perfect price discrimination moves the surplus to the pockets of the producer.[164]

It is more difficult to generalize about the general welfare effects of imperfect price discrimination.[165] Depending on the specific factual context, second and third-degree price discrimination can be either welfare-enhancing or welfare-diminishing.[166] In some cases, price discrimination may permit a seller to offer some goods at a lower price than would be possible under a uniform pricing regime. This can reduce what economists term "deadweight loss,"[167] by increasing total output and opening markets to consumers who would not otherwise have bought the product because they value the product at more than its marginal cost but less than the uniform price the seller would have charged in the absence of price discrimination.[168] Thus, the leading

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164 Boyle, *supra* note 144, at 2025–26 (emphasis removed); *see also* CARLTON & PERLOFF, *supra* note 9, at 306 ("There is no ambiguity about the welfare effects of perfect price discrimination. Output is at the efficient, competitive level, but consumers are poorer than they are under competition; therefore, perfect price discrimination does not distort efficiency but does affect the distribution of income."); Daniel A. Farber & Brett H. McDonnell, "*Is There a Text in This Class?" The Conflict Between Textualism and Antitrust*, 14 J. CONTEMP. LEGAL ISSUES 610, 648 (2005) ("Economists view price discrimination as potentially beneficial. They point out that price discrimination frequently allows monopolists to raise output above the one-price monopoly level, removing some of the inefficiency which monopoly creates, although also transforming consumer surplus into producer surplus") (citing PHILLIP E. AREEDA & HERBERT HOVENKAMP, 3 ANTITRUST LAW ¶ 721d (1996)); HOVENKAMP, *supra* note 19, § 14.4, at 575 ("[O]ne result of perfect price discrimination is that customers are far poorer and the seller far richer."); Meurer, *supra* note 14, at 69 (noting that perfect price discrimination "maximizes total surplus" but "distributes the entire surplus to the seller").

165 Frischmann, *supra* note 25, at 979 (observing that "the welfare implications of imperfect price discrimination are ambiguous and vary considerably by context" (citing TIROLE, *supra* note 9, at 139–40, 149)).

166 William W. Fisher III, *Property and Contract on the Internet*, 73 CHI.-KENT L. REV. 1203, 1241 (1998) (arguing in copyright context that price discrimination enables creators to make more money, should enhance consumer welfare and increase access to works of the intellect).

167 *See* CARLTON & PERLOFF, *supra* note 9, at 71 ("The cost to society of a market's not operating efficiently is called deadweight loss (DWL). It is the welfare loss—the sum of the consumer surplus and producer surplus lost—from a deviation from the competitive equilibrium."); POSNER, *supra* note 12, at 278–79 (discussing deadweight loss).

168 Fisher III, *supra* note 166, at 1237–38 (explaining how price discrimination can limit deadweight loss); Gilo & Porat, *supra* note 26, at 1023 (discussing welfare effects of price discrimination via contract boilerplate contract terms and concluding "it would be extremely difficult to identify cases in which discrimination via boilerplate language is welfare-reducing"); Hammer, *supra* note 8, at 889 ("Price discrimination can often increase social welfare. Welfare enhancements typically occur when charging a single uniform price results in the exclusion of otherwise willing purchasers from the market or, when a uniform price leads to the foreclosure or non-development of markets entirely."); Meurer, *supra* note 14, at 97–100; Jonathan Weinberg, *Hardware-Based ID, Rights Management, and Trusted Systems*, 52 STAN. L. REV. 1251, 1274 (2000); Yoo, *supra* note 38, at 1623 ("Imperfect price

antitrust treatise concludes "most price discrimination is socially beneficial in that it produces higher output and thus yields greater consumer benefits than forced nondiscriminatory pricing."[169]

A simple example will illustrate this point. Assume that we have a software manufacturer who has developed a new missile defense software program. The costs of developing the program were great, but the program can be copied and distributed at a very low cost, say $10 per copy. There are two defense contractors who would be willing to pay $1 million each for the software. There are also 500 universities that would like to use the software for instructional purposes. The universities would be willing to pay $1,000 each for the software. If the manufacturer is forced to offer the software at a single price, it will choose $1 million, and it will make two sales at $1 million for a total of $2 million.[170] The 500 universities would be deprived of the use of the software, which they each value at $1,000, thus creating deadweight loss. If the manufacturer were permitted to sell at two prices—$1 million for private defense contractors and $1,000 for universities—overall social welfare would be maximized, since sales now made to the 500 universities would have been priced out of the market altogether under the uniform price regime. (Assuming of course that there is no arbitrage.[171])

Admittedly, this output-expanding, welfare-maximizing theory of price discrimination cannot be generalized to all contexts.[172] In some situations,

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discrimination can reduce the efficiency losses caused by deadweight loss by making it possible for the producer to expand production by offering discounts to some consumers who would not purchase the product at the price the producer would charge were it limited to charging a single price.").

Richard Posner has a less sanguine view of third-degree price discrimination. *See* Richard A. Posner, *Vertical Restraints and Antitrust Policy*, 72 U. CHI. L. REV. 229, 235–36 (2005) ("In third-degree price discrimination, the customers are segmented according to their elasticity of demand and a separate price is charged to each segment. As a result, some customers are charged more than in a single-price system, others less, and the net effect on output is on average neutral."). This analysis does not, however, lead Posner to suggest greater price discrimination regulation:

> Even in the case of second-degree price discrimination, the fact that the net effect on economic welfare is probably negative would not be a persuasive ground for forbidding such discrimination. Such a project would be quixotic at best, if only because of the difficulty for courts of distinguishing between cost-based and purely discriminatory price differences.

Id. at 236.

[169] HOVENKAMP, *supra* note 81, ¶ 2340c, at 139.

[170] If the manufacturer knew the buyers' willingness to pay, it would not price the item between $1000 and $999,999 because it would not gain any sales, while it would experience a diminishment in revenue. Setting the price at $1000 would result in more customers but less revenue, since the two defense contractors and the 500 universities all would purchase the software at $1000 a piece for total sales of $502,000.

[171] *See supra* notes 46–54 and accompanying text.

[172] *See* Robinson, *supra* note 13, at 1506 ("[A]s a matter of general economic theory, systematic price discrimination can be efficient or inefficient depending on whether it increases total output or merely reallocates output between buyers with different price elasticities.").

imperfect price discrimination might cause production to decrease.[173] Moreover, as with perfect price discrimination, there are costs involved in implementing and maintaining second and third-degree price discrimination regimes, which any welfare analysis must consider. Producers must accurately categorize consumers based upon their willingness to pay and take potentially costly actions to prevent arbitrage.[174] In sum, determining whether imperfect price discrimination is socially beneficial cannot be answered in a theoretical vacuum; empirical inquiry is needed to determine the overall costs and benefits and distributional effects of a specific price discrimination regime.[175] Such an inquiry must take account of the specific form of imperfect price discrimination being practiced as well as the type of good or service being sold.[176]

In contrast to this context-dependent empirical inquiry, a rigidly enforced consumer equality rule would prohibit all forms of price discrimination regardless of their effects on social welfare or any further inquiry into their morality or efficacy in any particular case.[177] Consider this partial list of

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[173] *See* CARLTON & PERLOFF, *supra* note 9, at 306–07; Meurer, *supra* note 14, at 100 (providing examples of how price discrimination might reduce output); Yoo, *supra* note 38, at 1623 (stating that "it is theoretically possible that imperfect price discrimination would cause the deadweight loss to grow by causing overall production to decrease," while noting that the consensus is that it is more likely that price discrimination will reduce deadweight loss).

[174] *See* Yochai Benkler, *An Unhurried View of Private Ordering in Information Transactions*, 53 VAND. L. REV. 2063, 2072 (2000) ("Implementing price discrimination is costly. The producer must invest in identifying discrete market categories that would bear different prices. It must also take measures—technical, contractual, marketing, or any combination—to prevent arbitrage of the good from low value users to high value users."); Meurer, *supra* note 11, at 872 ("The distinction between second and third degree discrimination is important because second degree discrimination is usually more costly to implement. The greater cost arises from the need to get buyers to sort themselves in a manner that makes discrimination possible."); Neil Weinstock Netanel, *Market Hierarchy and Copyright in Our System of Free Expression*, 53 VAND. L. REV. 1879, 1914–15 (2000) (discussing costs of effective price discrimination in the market for digital technology); Posner, *supra* note 168, at 236 (noting "the costs of implementing third-degree price discrimination, which involve obtaining information on the elasticities of demand of different types of customer, setting different prices, and preventing arbitrage").

[175] *See, e.g.*, James Gibson, *Re-Reifying Data*, 80 NOTRE DAME L. REV. 163, 210–15 (2004) (discussing potential welfare effects of price discrimination in database markets); Meurer, *supra* note 14 (copyrighted works); Daniel J. Gifford, *How Do the Social Benefits and Costs of the Patent System Stack Up in Pharmaceuticals?*, 12 J. INTELL. PROP. L. 75 (2004) (pharmaceutical patents). Policymakers must also determine whether they are agnostic as to the distributional effects of price discrimination—the fact that price discrimination transfers surplus from consumers to producers. *See infra* notes 182-85 and accompanying notes for more on this point.

[176] *See* Stole, *supra* note 9, at 83 (observing that "[c]onclusions regarding profit and welfare typically depend upon the form of consumer heterogeneity, the goods for sale and the available instruments of price discrimination").

[177] *See* Damien Geradin & Nicolas Petit, *Price Discrimination Under EC Competition Law: The Need for a Case-By-Case Approach* 7 (Global Competition Law Centre Working Papers Series, Working Paper No. 07/05, 2005) (arguing that "a *per se* prohibition on price discrimination cannot be justified on the basis of economic theory as price discrimination may, depending on the facts of each case, enhance welfare").

dynamic or differential pricing practices that conceivably could be prohibited by a consumer equality rule:

- Senior citizen and student discounts for entertainment venues.
- All forms of individualized negotiation or haggling, including car sales.
- Variable pricing for airplane, train and bus tickets based upon when the ticket is purchased and other restrictions placed on the tickets.
- Variable pricing on tickets to theatrical and sporting events.
- Different versions of intellectual property goods (e.g., professional vs. educational versions of software).
- Mail-in and online rebates.
- Store and manufacturer coupons.
- Merchant loyalty/discount cards.
- Discounts granted by professional service providers (including doctors and lawyers) to loyal or less affluent clients.
- Scholarly publishers and database providers charging less to small or less wealthy libraries than they charge to wealthy or larger institutions.
- Staff discounts.
- Lower pharmaceutical prices charged to certain needy consumers.
- Bulk sale discounts.
- Need-based financial aid and sports scholarships at colleges and universities.[178]

In addition to potential welfare losses that uniform pricing can cause, a harsh consumer equality rule might have another negative effect: it could lead to endless debates between producers and consumers as to whether certain

[178] *See* Mark D. Bauer, *Small Liberal Arts Colleges, Fraternities, and Antitrust: Rethinking* Hamilton College, 53 CATH. U. L. REV. 347, 404–05 (2004) ("[T]hough charitable in purpose, financial aid is inherently a form of price discrimination because it charges consumers different rates for the same services.") (citing Ted Bergstrom, College Tuition and Price Discrimination, http://www.econ.ucsb.edu/~tedb/eep/news/tuition.html; Peter Passell, *The New Economics of Higher Education*, N.Y. TIMES, Apr. 22, 1997, at D1; AMERICAN COUNCIL ON EDUCATION, STRAIGHT TALK ABOUT COLLEGE COSTS AND PRICES, REPORT OF THE NATIONAL COMMITTEE ON THE COST OF HIGHER EDUCATION (1998)); Donald Robert Carlson & George Bobrinskoy Shepherd, *Cartel On Campus: The Economics and Law of Academic Institutions' Financial Aid Price-Fixing*, 71 OR. L. REV. 563 (1992); Richard Morrison, Comment, *Price Fixing Among Elite Colleges and Universities*, 59 U. CHI. L. REV. 807 (1992); Odlyzko, *supra* note 50, at 7.

pricing differences are caused by legitimate cost differentials and whether the goods or services being offered are equivalent enough to require equal prices.[179] This shows that one potential virtue of a clear equality rule, ease of application, is illusory. In actuality, courts and regulators would be forced to review and evaluate myriad pricing choices to determine whether consumers are being treated equally.[180]

C. Alternatives to Equality

In the previous subsection, I explained why I feel that equality is a poor standard for the design of consumer pricing regulation. Rejecting equality, however, does not mean that observers must abandon all progressive critiques of laissez faire approaches to consumer pricing. The point is not that price discrimination must be permitted in all contexts, but rather that norms or principles other than pure equality may be better suited to informing the regulatory process. Thus, before closing, I will briefly note some alternative possibilities. This treatment is meant to be illustrative rather than comprehensive. Although I am not endorsing any of these principles, they all have one major advantage over a broad equality norm—they permit policy makers to carve out permissible areas of price discrimination where it is deemed desirable.

1. Maximizing Overall Social Welfare

As discussed earlier, the welfare effects of imperfect price discrimination are highly context-dependent.[181] Policymakers thus could consider whether or not in a particular market price discrimination tends to increase production and overall social welfare. In addition, welfare analysis also could take into account the value that consumers arguably obtain when sellers better understand their desires and are able to target them for mutually beneficial commercial transactions.[182]

2. Minimizing Normatively Disfavored Wealth Distribution

Policymakers could consider whether discriminatory pricing practices influence the distribution of wealth between buyers and sellers or between different classes of consumers or different classes of producers[183] in a way that

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[179] The case of airline ticket pricing is instructive—would equal treatment mean that all passengers in a certain class on a specific flight must pay the same fare? Or would airlines be able to argue that tickets bought at different points in time are actually not identical commodities? *See* PHLIPS, THE ECONOMICS OF PRICE DISCRIMINATION, *supra* note 9, at 9–10.

[180] *See* Posner, *supra* note 168, at 236 (noting "difficulty for courts of distinguishing between cost-based and purely discriminatory price differences").

[181] *See supra* notes 165–176 and accompanying text.

[182] *See* Zarsky, *supra* note 60, at 35–39.

[183] *See* Netanel, *supra* note 174, at 1915 ("To the extent that an expansive copyright and ownership of a vast and varied content portfolio enhance possibilities for price discrimination and bundling, they will favor wealthy speakers over others, further propelling media concentration.").

they find normatively objectionable.[184] As discussed above, under perfect price discrimination (like perfect competition) output is efficient, but consumer surplus is allocated to sellers rather than buyers.[185] Given a choice, then, policymakers may want to push surplus into the hands of consumers as a class, rather than producers (or vice versa in some contexts), or may wish to privilege one group of producers or consumers over another.[186] To engage in this type of regulation, policymakers must have a policy on wealth distribution and have determined that regulating consumer prices is a legitimate vehicle for effectuating this policy.

3. Combating Invidious Forms of Discrimination

Policymakers may consider whether the decision to price discriminate is being made in a manner that violates well-established anti-discrimination norms.[187] Decisions to discriminate based upon race, religion, national origin, gender, age, and disability could fall into this category.[188] California's Gender Tax Repeal Act of 1995[189] illustrates this approach. The Act states that "[n]o business establishment of any kind whatsoever may discriminate, with respect to the price charged for services of similar or like kind, against a person because of the person's gender."[190] At the same time, the statute explicitly permits "price differences based specifically upon the amount of time, difficulty, or cost of providing the services."[191] The threshold inquiry for any such legislation is determining who should be granted protection under the law, and the California Legislature felt that it was abundantly clear that women deserved such protection.[192] Contrast this with Mark Klock's explicit comparison between price discrimination based on willingness to pay and racial discrimination:

> If a big corporation selling washing machines or a street vendor selling ice cream charged one price for white customers and a higher price to other customers solely based on their color, society would be outraged.

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[184] Rotenberg, *supra* note 59, ¶ 111 (noting that while "allocation of goods might still be considered 'efficient,'. . . the distributional effects as well as the market effects would be a basis for concern").

[185] *See supra* notes 163–64 and accompanying text.

[186] *See* Gilo & Porat, *supra* note 26, at 1022–23 (discussing distributional effects of price discrimination via contract boilerplate contract terms); Meurer, *supra* note 14, at 92–94 (discussing potential redistributive effects of various copyright price regulation policies); TIROLE, *supra* note 9, at 139 (discussing income redistribution effects of third-degree price discrimination).

[187] *See* Ian Ayres, *Fair Driving: Gender and Race Discrimination in Retail Car Negotiations*, 104 HARV. L. REV. 817, 850 (1991); Ayres, *supra* note 17; Zarsky, *supra* note 60, at 53 (noting that price discrimination may be motivated by bigotry).

[188] This list is not meant to be exhaustive.

[189] *See* CAL. CIV. CODE § 51.6 (West 2002). For a lucid discussion of the Gender Tax Repeal Act, *see* Recent Legislation, *Cal. Civ. Code 51.6*, 109 HARV. L. REV. 1839 (1996).

[190] CAL. CIV. CODE § 51.6 (b).

[191] *Id*.

[192] *See* Recent Legislation, *supra* note 189, at 1839–40 (discussing legislative history of the Gender Tax Repeal Act of 1995).

> Suppose different prices are charged, not because of differences in color, but because of differences in some other attribute, such as the willingness to pay. Why should society not object to this? Sometimes the people discriminated against are poorer and less educated, are affluent or educated, or are corporate entities. Does it make a difference? If so, is that not analogous to suggesting that it is acceptable to steal from insurance companies, but not from individuals?[193]

The simple answer to Klock's questions is that we do not yet have a well-established norm against discrimination based on willingness to pay.[194] In contrast, we have determined that other antidiscrimination norms, such as those based on race,[195] should trump efficiency concerns[196] or the discriminator's desire for wealth maximization,[197] at least in certain contexts. It seems to me that those who would seek to implement such an anti-discrimination principle should justify its application in much the same way that civil rights advocates argued in favor of establishing certain protected classes in the law.[198]

4. Protecting Privacy Interests

Policymakers could consider whether price discriminating firms are violating consumers' privacy interests.[199] Once again the issue is whether there is a privacy norm that should, in a particular set of circumstances, trump other economic or moral considerations. For example, imagine that I write a letter to my friend in which I mention that I want to take a trip to Las Vegas, Nevada. We would not permit a travel agent to intercept and read this letter, even if it meant that the travel agent might inform me of a great bargain vacation package to Las Vegas. The fact that the travel agent and I might both benefit is

[193] Klock, *supra* note 14, at 382.

[194] *See* Hillman & Rachlinski, *supra* note 58, at 472 ("Price discrimination based on identifying customers who value goods and services more than others is relatively common and benign.").

[195] Examples of antidiscrimination statutes include the Fair Housing Act, 42 U.S.C. §§ 3601–3631 (2000); the Equal Credit Opportunity Act, 15 U.S.C. § 1691 (2000); and the civil rights protections found at 42 U.S.C. §§ 1981–1982 (2000).

[196] *See* Recent Legislation, *supra* note 189, at 1843 ("Ultimately, considerations of economic efficiency should be balanced against considerations of justice and nondiscrimination. As scholars have noted, American society has determined that economic efficiency alone cannot justify discriminatory practices. Preventing economic discrimination through prohibitive legislation should take precedence over considerations of economic efficiency.") (citing Robert H. Jerry, II & Kyle B. Mansfield, *Justifying Unisex Insurance: Another Perspective*, 34 AM. U. L. REV. 329, 333 (1985)).

[197] A decision to engage in race-based discrimination may be based on a determination that it will be wealth-maximizing for the discriminator. *See* John Yinger, *Evidence on Discrimination in Consumer Markets*, 12 J. ECON. PERSP. 23, 36–38 (1998).

[198] Mark Klock suggests that those who would discriminate bear the burden of proof here. *See* Klock, *supra* note 14, at 362 ("If we are prepared to say that discrimination against certain groups is tolerable, then we must also be prepared to clearly and precisely define those groups."). I am sympathetic to this perspective, but traditionally the burden has been on those who seek to change the status quo.

[199] *See* ANNENBERG REPORT, *supra* note 4, at 11 (noting privacy concerns raised by database-guided price discrimination).

not legally relevant—the violation of my privacy interests presumably trumps these mutual gains. Scholars and government agencies have combined to develop a rich privacy rights literature that can assist policymakers who wish to pursue privacy as a normative standard for evaluating price discrimination behavior.[200]

5. *Fighting Monopoly or Excessive Market Power*

Traditional economic theory suggests that producers must have market power[201] to engage in price discrimination, since this practice involves pricing at least some of their goods at greater than marginal cost. Michael Levine sketches out the conventional economic account: "In thinking about price discrimination, economists have historically constructed the following argument: In a competitive market, price equals marginal cost. Wherever there is price discrimination, price deviates from marginal cost. Therefore, if there is price discrimination, the market must not be competitive and there must be market power."[202] Other legal and economics scholars have made similar points.[203] Therefore, one might seek to regulate price discrimination as a method of combating monopoly or excessive market power.

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200 *See, e.g.*, FED. TRADE COMM'N, PRIVACY ONLINE: FAIR INFORMATION PRACTICES IN THE ELECTRONIC MARKETPLACE, A REPORT TO CONGRESS (2000), http://www.ftc.gov/reports/privacy2000/privacy2000.pdf.; Kang, *supra* note 60; Elbert Lin, Article, *Prioritizing Privacy: A Constitutional Response to the Internet*, 17 BERKELEY TECH. L.J. 1085 (2002); Paul M. Schwartz, *Privacy and Democracy in Cyberspace*, 52 VAND. L. REV. 1609 (1999); Paul M. Schwartz, *Internet Privacy and the State*, 32 CONN. L. REV. 815 (2000); Zarsky, *supra* note 60.

201 For discussions of the relationship between market power and monopoly, see Andrew I. Gavil, Copperweld *2000: The Vanishing Gap Between Sections 1 and 2 of the Sherman Act*, 68 ANTITRUST L.J 87, 102–03 (2000); Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 ANTITRUST L.J. 3, 11–14 (2004); Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 257–60, 330–37 (2003).

202 Levine, *supra* note 36, at 3.

203 *See* CARLTON & PERLOFF, *supra* note 9, at 294 (stating that market power, the ability to set price above marginal cost profitably, is a condition of successful price discrimination); Einer Elhauge, *Why Above-Cost Price Cuts to Drive Out Entrants Are Not Predatory—and the Implications for Defining Costs and Market Power*, 112 YALE L.J. 681, 726 (2003) ("[P]ricing above cost seems to meet a standard definition of market power, given the normal premise that firms in a competitive market price at marginal cost. Relatedly, standard analysis assumes that an ability to price discriminate implies the firm must have market power."); Gibson, *supra* note 175, at 209 ("[P]rice discrimination requires sufficient market power on the part of the producer—a lack of competition. A producer in a competitive industry confronts elastic demand and thus a flatter demand curve that does not allow for price discrimination."); Klock, *supra* note 14, at 327; HOVENKAMP, *supra* note 19, § 14.3, at 574 ("*Sporadic* price discrimination is an every-day occurrence in competitive markets. However, persistent price discrimination requires that a seller (or group of sellers) have at least some market power."); Kahan & Kamar, *supra* note 11, at 1210–11:

> In markets that are not competitive, some producers possess market power, which is defined as the ability to charge more for a product than its marginal cost. Since charging more for a product than its marginal cost is a condition for earning a profit, the ability to earn a profit over an extended period of time is evidence that a producer has market power.

Although a full analysis of this issue is beyond my scope here, it should be noted that a growing economics literature challenges the "price discrimination proves market power" theory.[204] Instead, many scholars and commentators now contend that price discrimination can and does exist in competitive markets.[205] I am quite dubious about overbroad generalizations regarding the connection between price discrimination and monopoly. But for my purposes here I will accept the possibility that there are some situations where price discrimination does indicate antitrust market power. In those factual circumstances, there might be an argument for limiting price discrimination if it can be shown that the differential pricing practices not only provide evidence of what is considered to be excessive market power, but also help to facilitate or reinforce this market power.[206]

V. CONCLUSION

Price discrimination is a prominent feature of the economic landscape, and differential or dynamic pricing practices are likely to become even more prevalent as technological advances enable sellers to estimate and predict consumers' willingness to pay for goods and services. Under current federal

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[204] *See generally* Symposium, *Competitive Price Discrimination*, 70 ANTITRUST L.J. 593 (2003).

[205] *See* William J. Baumol & Daniel G. Swanson, *The New Economy and Ubiquitous* Competitive *Price Discrimination: Identifying Defensible Criteria of Market Power*, 70 ANTITRUST L.J. 661 (2003); Shane Carbonneau et al., Price Discrimination and Market Power (June 7, 2004), http://ssrn.com/abstract=594442 (finding a negative correlation between price discrimination and market power in the U.S. airlines industry); Levine, *supra* note 36; Weiss & Mehrotra, *supra* note 8, ¶ 17 ("Just about any industry that faces a high set of fixed costs and relatively low variable costs—such as book publishing or the movie industry—will resort to some form of price discrimination."); Sherwin Rosen & Andrew M. Rosenfield, *Ticket Pricing*, 40 J. L. & ECON. 351, 351 (1997):

> [Price discrimination] is widespread and hardly confined to traditional monopolists. It occurs in such highly competitive businesses as restaurants, airlines, hotels, bars, and private colleges, where many alternative sellers are available to customers and barriers to entry are nil. Price discrimination tends to be observed in activities where inventory/capacity constraints make the marginal costs of providing service to any one user smaller than the average cost. For example, so long as capacity is slack, the marginal user cost of hotel rooms or airplane seats to customers is trivial once the hotel has been built and the airplane has been configured.

For more on market power and price discrimination, *see* Gloria J. Hurdle & Henry B. McFarland, *Criteria for Identifying Market Power: A Comment on Baumol and Swanson*, 70 ANTITRUST L.J. 687, 688 (2003); Jonathan B. Baker, *Competitive Price Discrimination: The Exercise of Market Power Without Anticompetitive Effects*, 70 ANTITRUST L.J. 643, 644–45 (2003); Benjamin Klein & John Shepard Wiley Jr., *Market Power in Economics and in Antitrust: Reply to Baker*, 70 ANTITRUST L.J. 655, 658 (2003).

[206] *See* Gilo & Porat, *supra* note 26, at 999–1000. Wendy Gordon has argued persuasively that complete welfare analysis of price discrimination in intellectual property goods must include consideration of the initial allocation of IP rights that create the monopoly that is being ameliorated through price discrimination. *See* Wendy J. Gordon, *Intellectual Property as Price Discrimination: Implications for Contract*, 73 CHI.-KENT L. REV. 1367, 1386–89 (1998).

law, price discrimination against end-use consumers is typically legal. This Article has argued that this approach reflects good public policy. Although consumers are deeply offended when they learn that they have been treated differently than others in the marketplace, the law should not respond to this frustration by mandating equality in pricing. A rigidly enforced principle of consumer equality, while superficially appealing to consumers, could have negative effects on consumer welfare by driving out forms of differential pricing that are socially beneficial.

Instead of endorsing equality, critics of laissez faire approaches to consumer pricing should continue to focus on arguments based upon enhancing consumers' economic welfare, protecting privacy rights, eradicating invidious forms of discrimination, and fighting monopolies. Legal rules based upon these well-established principles can protect consumers against odious business practices while still preserving the potentially beneficial effects of price discrimination.