V. HORIZONTAL RESTRAINTS

A. Overview

Antitrust analysis generally divides agreements, and provisions in them that may restrain competition, into two categories: "horizontal" restraints among actual or potential competitors, and "vertical" restraints among parties at different levels of the same supply chain or suppliers of complements. Of these, horizontal restraints are much more likely to raise competitive concerns: businesses generally have more good reasons to enter into agreements with their trading partners than they do with their competitors! We will consider horizontal restraints in this chapter, and will turn to vertical restraints in Chapter VI.

The category of horizontal restraints includes a very broad spectrum of agreements and practices. At the most troubling end of this spectrum we find hardcore cartelization and equivalent practices, including price fixing, market allocation, and bid-rigging. As we saw in Chapter IV, a small set of such nakedly anticompetitive practices are *per se* illegal in civil litigation: these may be subject to criminal punishment too. DOJ seeks and obtains extradition, criminal fines, and terms of imprisonment for conduct in this category. The classic formulation of the competitive concern with such agreements is that they harm competition—increasing prices and reducing output, quality, and innovation—but offer no redeeming public benefit in the vast majority of cases, making a flat ban appropriate and efficient. The imposition of criminal penalties, among other things, reflects an effort to offset the difficulties of detecting such agreements, which are typically kept secret by the participants. DOJ also operates a criminal "leniency" program, which provides businesses with significant protection from criminal and civil enforcement in exchange for informing on cartel activity and cooperating with prosecutors. We will turn to criminal enforcement briefly in Chapter XI.

Outside the zone of hardcore antitrust violations, horizontal practices and restraints may take almost any form, and may present almost any level of concern under the antitrust laws, from very mild to very considerable. These agreements come in all shapes and sizes, but you may encounter some or all of the following:

- **Standard-setting activities.** Groups of businesses, including competitors, may participate in so-called "standard setting" or "standards development" activities in order to establish technical and commercial standards for certain kinds of activity. This process may involve some government participation or it may be wholly private. There are countless standard setting organizations, large and small, in the national and global economy that design, promulgate, review, and amend standards for markets of all kinds.[331] Possible competitive concerns include worries that standard-setting may become a cloak for collusion (*e.g.*, competitors fixing prices or dividing markets) or a tool for exclusion (*e.g.*, manipulation, deception, or distortion of the standard setting process in a manner that may exclude competition, and wrongfully create or maintain market power). But standard setting can also offer tremendous procompetitive benefits, including the opportunity to spur innovation and investment in areas where the lack of a focal point might otherwise act as a deterrent, as well as the opportunity to promote valuable forms of interoperability.[332] Congress recognized the procompetitive benefits of standard setting in the Standards Development Organization Act of 2004, protecting participants from the threat of *per se* liability.[333] Standard setting activities are analyzed under the rule of reason. We will return to standard-setting in Chapter X.
- **Joint buying or selling arrangements.** Competing firms may aim to coordinate their selling or buying activities: for example, through a group purchasing organization. Such arrangements, even

[331] *See generally*, *e.g.*, Maureen K. Ohlhausen, *The Elusive Role of Competition In The Standard-Setting Antitrust Debate*, 20 Stan. Tech. L. Rev. 93 (2017); Mark A. Lemley, *Intellectual Property Rights and Standard-Setting Organizations*, 90 Calif. L. Rev. 1889 (2002)

[332] *See*, *e.g.*, Deborah Platt Majoras, *Recognizing the Procompetitive Potential of Royalty Discussions in Standard Setting* (remarks of Sept. 23, 2005).

[333] 15 U.S.C. § 4301 *et seq.* The Act excludes from its protection from per se liability exchanges of competitively sensitive information, market allocation, and price fixing. *Id.* at § 4301(c).

among competitors, may be benign, such as when they do not involve participants that individually or collectively hold market power, enable the participants to access efficiencies of scope and scale that would otherwise be unavailable, and are structured to avoid or minimize coordination on terms of dealing. But the potential competitive concerns are obvious: after all, a cartel is a form of "joint selling arrangement," and conduct that involves coordination with competitors on terms of trading raises evident hazards. Joint buying or selling may invite *per se* condemnation when it lacks arguable procompetitive benefits in the form of some economic integration among the participants, and particularly if the participants hold market power. Courts and agencies tend to apply the rule of reason to less nakedly harmful versions of such practices.

- **"Joint ventures."** You will often hear the term "joint venture" in the study of Section 1. This phrase is a vague catchall. It encompasses everything from informal and short-term projects of cooperation among separate businesses to the creation or merger of co-owned incorporated businesses[334]—and everything in between. Some joint ventures involve mergers or acquisitions that are subject to Section 7 of the Clayton Act. But any joint venture that involves an agreement is also subject to review under Section 1 of the Sherman Act, and in this chapter our focus will be on Section 1 analysis. Joint ventures are analyzed in a manner reflecting their economic structure and operation: in some cases, courts have condemned as *per se* illegal conduct that would be fairly described as a plausible joint venture,[335] in other cases, joint ventures are recognized as plainly procompetitive under the rule of reason.[336] However, in most modern cases, a venture will be analyzed under the rule of reason rather than the *per se* rule if it is reasonably related to the achievement of a procompetitive purpose.[337] You may remember from Chapter IV that an economically integrated joint venture may be a single enterprise for the purposes of antitrust analysis of its decisions, taking it outside the scope of Section 1, but the creation of the enterprise itself usually remains an agreement subject to antitrust challenge under Section 1.[338]
- **Trade associations and information sharing.** Antitrust lawyers often love to quote Adam Smith's aphoristic warning about trade associations.[339] But trade association activity is by no means all bad. It is ubiquitous in the economy, and it invariably involves competitors' employees meeting with one another, communicating about matters of interest, and undertaking joint projects. Certainly, this kind of contact can lead to illegal conduct like price-fixing, particularly when participants are imprudent (or poorly counseled!). But it can also lead to conduct that may violate the rule of reason (*e.g.*, anticompetitive sharing of competitively sensitive information), as well as plenty of conduct that is clearly procompetitive and lawful (*e.g.*, joint analysis of market conditions in a manner that does not harm competition and may improve it). Antitrust lawyers often play an important role in helping participants in trade associations stay on the right side of the line—and in dealing with the consequences if they do not!
- **Agreements involving IP.** Sometimes IP licenses or other agreements may involve actual or potential rivals. Licensing negotiations, a license agreement, or a settlement of an infringement claim may all have implications for competition between the parties. We will consider IP issues, and these concerns, in Chapter X.

Analytically, the appraisal of horizontal restraints typically involves two critical stages: first, determining the standard of legality that will govern the agreement (*per se* illegal, full rule of reason, or intermediate scrutiny such

---

334 *See*, *e.g.*, Analysis of Agreement Containing Consent Order to Aid Public Comment, In the Matter of The Boeing Company, Lockheed Martin Corporation, and United Launch Alliance, FTC File No. 051-0165 (Oct. 3, 2006) (incorporated joint venture between Boeing and Lockheed Martin to offer space launch services).

335 *See*, *e.g.*, United States v. Topco Associates, 405 U.S. 596 (1972) (cooperative buying and selling arrangement *per se* illegal); United States v. Sealy, Inc., 388 U.S. 350 (1967) (cooperative marketing and selling venture was *per se* illegal).

336 *See*, *e.g.*, Toscano v. PGA Tour, Inc., 201 F. Supp. 2d 1106, 1123 (E.D. Cal. 2002).

337 *See*, *e.g.*, Med. Ctr. at Elizabeth Place, LLC v. Atrium Health Sys., 922 F.3d 713, 728 (6th Cir. 2019) ("If the record in this case reveals a plausible way in which the challenged restraints contribute to the procompetitive efficiencies of the joint venture, then "the possibility of countervailing procompetitive effects" is not remote and per se treatment is improper.").

338 *See supra* § IV.B.1.

339 Adam Smith, 1 THE WEALTH OF NATIONS (1776) ("People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.").

as "quick look"); second, applying that standard to determine whether the agreement is an unreasonable restraint.

The antitrust agencies have issued a set of guidelines for competitor collaborations that provide some helpful guidance regarding the analysis of horizontal cooperation. Although these guidelines are not binding on courts, they helpfully summarize the ways in which agencies and courts tend to approach such practices, and are sometimes cited by courts in adjudicating such cases.[340] They also shed some helpful light on the agencies' views about the application of Section 1 to horizontal practices more generally.

U.S. Department of Justice and FTC, Antitrust Guidelines for Collaborations Among Competitors (2000)

Section 2: General Principles For Evaluating Agreements Among Competitors

2.1 Potential Procompetitive Benefits

[1] The Agencies recognize that consumers may benefit from competitor collaborations in a variety of ways. For example, a competitor collaboration may enable participants to offer goods or services that are cheaper, more valuable to consumers, or brought to market faster than would be possible absent the collaboration. A collaboration may allow its participants to better use existing assets, or may provide incentives for them to make output-enhancing investments that would not occur absent the collaboration. The potential efficiencies from competitor collaborations may be achieved through a variety of contractual arrangements including joint ventures, trade or professional associations, licensing arrangements, or strategic alliances.

[2] Efficiency gains from competitor collaborations often stem from combinations of different capabilities or resources. For example, one participant may have special technical expertise that usefully complements another participant's manufacturing process, allowing the latter participant to lower its production cost or improve the quality of its product. In other instances, a collaboration may facilitate the attainment of scale or scope economies beyond the reach of any single participant. For example, two firms may be able to combine their research or marketing activities to lower their cost of bringing their products to market, or reduce the time needed to develop and begin commercial sales of new products. Consumers may benefit from these collaborations as the participants are able to lower prices, improve quality, or bring new products to market faster.

2.2 Potential Anticompetitive Harms

[3] Competitor collaborations may harm competition and consumers by increasing the ability or incentive profitably to raise price above or reduce output, quality, service, or innovation below what likely would prevail in the absence of the relevant agreement. Such effects may arise through a variety of mechanisms. Among other things, agreements may limit independent decision making or combine the control of or financial interests in production, key assets, or decisions regarding price, output, or other competitively sensitive variables, or may otherwise reduce the participants' ability or incentive to compete independently.

[4] Competitor collaborations also may facilitate explicit or tacit collusion through facilitating practices such as the exchange or disclosure of competitively sensitive information or through increased market concentration. Such collusion may involve the relevant market in which the collaboration operates or another market in which the participants in the collaboration are actual or potential competitors.

2.3 Analysis of the Overall Collaboration and the Agreements of Which It Consists

[5] A competitor collaboration comprises a set of one or more agreements, other than merger agreements, between or among competitors to engage in economic activity, and the economic activity resulting therefrom.

---

[340] *See*, *e.g.*, Impax Labs., Inc. v. FTC, 994 F.3d 484, 496 (5th Cir. 2021); Viamedia, Inc. v. Comcast Corp., 951 F.3d 429, 478 (7th Cir. 2020); Med. Ctr. at Elizabeth Place, LLC v. Atrium Health Sys., 922 F.3d 713, 726 (6th Cir. 2019).

. . . Two or more agreements are assessed together if their procompetitive benefits or anticompetitive harms are so intertwined that they cannot meaningfully be isolated and attributed to any individual agreement. . . .

2.4 Competitive Effects Are Assessed as of the Time of Possible Harm to Competition

[6] The competitive effects of a relevant agreement may change over time, depending on changes in circumstances such as internal reorganization, adoption of new agreements as part of the collaboration, addition or departure of participants, new market conditions, or changes in market share. The Agencies assess the competitive effects of a relevant agreement as of the time of possible harm to competition, whether at formation of the collaboration or at a later time, as appropriate. . . . However, an assessment after a collaboration has been formed is sensitive to the reasonable expectations of participants whose significant sunk cost investments in reliance on the relevant agreement were made before it became anticompetitive.

Section 3: Analytical Framework For Evaluating Agreements Among Competitors

3.1 Introduction

[7] . . . Certain types of agreements are so likely to be harmful to competition and to have no significant benefits that they do not warrant the time and expense required for particularized inquiry into their effects. Once identified, such agreements are challenged as per se illegal.

[8] Agreements not challenged as per se illegal are analyzed under the rule of reason. Rule of reason analysis focuses on the state of competition with, as compared to without, the relevant agreement. Under the rule of reason, the central question is whether the relevant agreement likely harms competition by increasing the ability or incentive profitably to raise price above or reduce output, quality, service, or innovation below what likely would prevail in the absence of the relevant agreement. Given the great variety of competitor collaborations, rule of reason analysis entails a flexible inquiry and varies in focus and detail depending on the nature of the agreement and market circumstances. Rule of reason analysis focuses on only those factors, and undertakes only the degree of factual inquiry, necessary to assess accurately the overall competitive effect of the relevant agreement.

3.2 Agreements Challenged as Per Se Illegal

[9] Agreements of a type that always or almost always tends to raise price or reduce output are per se illegal. The Agencies challenge such agreements, once identified, as per se illegal. Typically these are agreements not to compete on price or output. Types of agreements that have been held per se illegal include agreements among competitors to fix prices or output, rig bids, or share or divide markets by allocating customers, suppliers, territories or lines of commerce. The courts conclusively presume such agreements, once identified, to be illegal, without inquiring into their claimed business purposes, anticompetitive harms, procompetitive benefits, or overall competitive effects. The Department of Justice prosecutes participants in hard-core cartel agreements criminally.

[10] If, however, participants in an efficiency-enhancing integration of economic activity enter into an agreement that is reasonably related to the integration and reasonably necessary to achieve its procompetitive benefits, the Agencies analyze the agreement under the rule of reason, even if it is of a type that might otherwise be considered per se illegal. . . . In an efficiency enhancing integration, participants collaborate to perform or cause to be performed (by a joint venture entity created by the collaboration or by one or more participants or by a third party acting on behalf of other participants) one or more business functions, such as production, distribution, marketing, purchasing or R&D, and thereby benefit, or potentially benefit, consumers by expanding output, reducing price, or enhancing quality, service, or innovation. Participants in an efficiency-enhancing integration typically combine, by contract or otherwise, significant capital, technology, or other complementary assets to achieve procompetitive benefits that the participants could not achieve separately. The mere coordination of decisions on price, output, customers, territories, and the like is not integration, and cost savings without integration are not a basis for avoiding per se condemnation. The integration must be of a type that plausibly would generate procompetitive benefits cognizable under the [agencies' approach to] efficiencies

analysis . . . . Such procompetitive benefits may enhance the participants' ability or incentives to compete and thus may offset an agreement's anticompetitive tendencies. . . .

[11] An agreement may be "reasonably necessary" without being essential. However, if the participants could achieve an equivalent or comparable efficiency-enhancing integration through practical, significantly less restrictive means, then the Agencies conclude that the agreement is not reasonably necessary. In making this assessment, except in unusual circumstances, the Agencies consider whether practical, significantly less restrictive means were reasonably available when the agreement was entered into, but do not search for a theoretically less restrictive alternative that was not practical given the business realities.

[12] Before accepting a claim that an agreement is reasonably necessary to achieve procompetitive benefits from an integration of economic activity, the Agencies undertake a limited factual inquiry to evaluate the claim. Such an inquiry may reveal that efficiencies from an agreement that are possible in theory are not plausible in the context of the particular collaboration. Some claims—such as those premised on the notion that competition itself is unreasonable—are insufficient as a matter of law, and others may be implausible on their face. In any case, labeling an arrangement a "joint venture" will not protect what is merely a device to raise price or restrict output; the nature of the conduct, not its designation, is determinative.

3.3 Agreements Analyzed under the Rule of Reason

[13] Agreements not challenged as per se illegal are analyzed under the rule of reason to determine their overall competitive effect. Rule of reason analysis focuses on the state of competition with, as compared to without, the relevant agreement. The central question is whether the relevant agreement likely harms competition by increasing the ability or incentive profitably to raise price above or reduce output, quality, service, or innovation below what likely would prevail in the absence of the relevant agreement.

[14] Rule of reason analysis entails a flexible inquiry and varies in focus and detail depending on the nature of the agreement and market circumstances. The Agencies focus on only those factors, and undertake only that factual inquiry, necessary to make a sound determination of the overall competitive effect of the relevant agreement. Ordinarily, however, no one factor is dispositive in the analysis.

[15] Under the rule of reason, the Agencies' analysis begins with an examination of the nature of the relevant agreement, since the nature of the agreement determines the types of anticompetitive harms that may be of concern. As part of this examination, the Agencies ask about the business purpose of the agreement and examine whether the agreement, if already in operation, has caused anticompetitive harm. If the nature of the agreement and the absence of market power[26] together demonstrate the absence of anticompetitive harm, the Agencies do not challenge the agreement. . . . Alternatively, where the likelihood of anticompetitive harm is evident from the nature of the agreement, or anticompetitive harm has resulted from an agreement already in operation, then, absent overriding benefits that could offset the anticompetitive harm, the Agencies challenge such agreements without a detailed market analysis.

[16] If the initial examination of the nature of the agreement indicates possible competitive concerns, but the agreement is not one that would be challenged without a detailed market analysis, the Agencies analyze the agreement in greater depth. The Agencies typically define relevant markets and calculate market shares and concentration as an initial step in assessing whether the agreement may create or increase market power or facilitate its exercise and thus poses risks to competition. The Agencies examine factors relevant to the extent to which the participants and the collaboration have the ability and incentive to compete independently, such as whether an agreement is exclusive or non-exclusive and its duration. The Agencies also evaluate whether entry would be timely, likely, and sufficient to deter or counteract any anticompetitive harms. In addition, the Agencies assess any other market circumstances that may foster or impede anticompetitive harms.

[26] That market power is absent may be determined without defining a relevant market. For example, if no market power is likely under any plausible market definition, it does not matter which one is correct. Alternatively, easy entry may indicate an absence of market power.

[17] If the examination of these factors indicates no potential for anticompetitive harm, the Agencies end the investigation without considering procompetitive benefits. If investigation indicates anticompetitive harm, the Agencies examine whether the relevant agreement is reasonably necessary to achieve procompetitive benefits that likely would offset anticompetitive harms.

3.31 Nature of the Relevant Agreement: Business Purpose, Operation in the Marketplace and Possible Competitive Concerns

[18] The nature of the agreement is relevant to whether it may cause anticompetitive harm. For example, by limiting independent decision making or combining control over or financial interests in production, key assets, or decisions on price, output, or other competitively sensitive variables, an agreement may create or increase market power or facilitate its exercise by the collaboration, its participants, or both. An agreement to limit independent decision making or to combine control or financial interests may reduce the ability or incentive to compete independently. An agreement also may increase the likelihood of an exercise of market power by facilitating explicit or tacit collusion, either through facilitating practices such as an exchange of competitively sensitive information or through increased market concentration.

[19] In examining the nature of the relevant agreement, the Agencies take into account inferences about business purposes for the agreement that can be drawn from objective facts. The Agencies also consider evidence of the subjective intent of the participants to the extent that it sheds light on competitive effects. The Agencies do not undertake a full analysis of procompetitive benefits . . . , however, unless an anticompetitive harm appears likely. The Agencies also examine whether an agreement already in operation has caused anticompetitive harm. Anticompetitive harm may be observed, for example, if a competitor collaboration successfully mandates new, anticompetitive conduct or successfully eliminates procompetitive pre-collaboration conduct, such as withholding services that were desired by consumers when offered in a competitive market. If anticompetitive harm is found, examination of market power ordinarily is not required. In some cases, however, a determination of anticompetitive harm may be informed by consideration of market power.

* * *

In the rest of this chapter, we will explore some issues specific to the classification and evaluation of horizontal restraints. In Section B we will encounter some *per se* unlawful restraints that go beyond simple price-fixing cartels, including wage-fixing agreements, bid-rigging practices, hub-and-spoke conspiracies, and group boycotts. In Section C we will focus on the border between the *per se* rule and the rule of reason, and investigate how courts and agencies classify horizontal restraints on that boundary. In Section D we will focus on the border between rule of reason and intermediate (or "quick look") scrutiny, and the standards that courts have applied to determine when a horizontal restraint merits elevated skepticism rather than open-minded rule-of-reason review.

B. *Per Se* Unlawful Collusion—Beyond Price Fixing

The classic case of *per se* illegality is the simple price-fixing cartel, as we saw in Chapter IV.[341] Although the *per se* zone is fairly narrow, it covers more than just literal price fixing, as the extract from the Competitor Collaboration Guidelines above suggests. Any naked coordination on terms of dealing among competitors—*i.e.*, coordination unrelated to a genuine procompetitive purpose or an economic integration among the participants—may invite *per se* treatment by courts. This may include coordination among buyers as well as among sellers; coordination on output and quality as well as on price; and agreements to divide markets or rig bids.

[341] *See*, *e.g.*, United States v. Trenton Potteries Co., 273 U.S. 392 (1927); *see generally supra* § IV.C.1.

1. Price Fixing, Buyers' Cartels, and Wage Fixing

The naked price-fixing cartel is the clearest imaginable violation of the antitrust laws. The core insight underpinning a cartel is that, if the participants can collectively exercise market power by coordinating to raise prices or reduce output, without attracting entry or expansion, it may be possible to move market supply and demand toward monopoly levels and to split the resulting monopoly profits. In order to achieve this goal, a cartel must coordinate the pricing and output decisions of its members to avoid "cheating" (*i.e.*, individual cartelists lowering their own price or increasing their own output in an effort to win share), and must have some reason to believe that other actors—including existing competitors and potential entrants—will not be able to defeat the cartel by expanding their capacity and/or lowering their price.

But antitrust doctrine punishes cartel agreements—and all "naked" agreements not to compete—regardless of their success or economic effects. As we saw in the previous chapter, the underlying idea is that naked collusion (that is, collusion not related to any procompetitive purpose) is so reliably harmful that the socially optimal rule is a flat ban. (Procompetitive justifications for a particular cartel are as irrelevant in criminal cases as in civil ones.[342]) Even this ban, however, is subject to a small number of narrow exceptions and immunities—such as the immunity for labor unions—that we will discuss in Chapter IX.

This rule of automatic illegality places tremendous load on two distinctions in the law of Section 1. The first is the distinction between the treatment of price-fixing "cartels," which are *per se* illegal and criminally prosecuted, and the treatment of tacit collusion without an agreement, which is *per se* legal. That distinction turns on whether there is an *agreement* among the parties to coordinate their conduct: and, as we saw in Chapter IV, defining and proving an agreement can be harder than it sounds. But the distinction is utterly critical. In the 1980s, the FTC tried to work around Section 1's agreement criterion by leaning on the broad language of Section 5 of the FTC Act, which prohibits "unfair methods of competition," to challenge tacit collusion. But the Second Circuit shot the effort down, re-affirming the rule that "[t]he mere existence of an oligopolistic market structure in which a small group of manufacturers engage in consciously parallel pricing of an identical product does not violate the antitrust laws."[343] (The FTC has been successful, however, in establishing the principle that a unilateral *invitation* to fix price violates Section 5.[344] Why do you think this effort has been successful when challenges to tacit collusion have not been? We will talk more about Section 5 of the FTC Act in Chapter XI.)

The second is the distinction between "naked" collusion, which is unrelated to any procompetitive purpose, and coordination that is sufficiently related (or "ancillary") to a broader procompetitive purpose or economic integration among the participants. This distinction—usually dated to then-Judge Taft's decision in *Addyston Pipe*[345]—turns on whether the parties are merely eliminating competition between themselves in some way, or by contrast are attempting to pursue some broader procompetitive enterprise. As we saw in Chapter IV, agreements in the first category are *per se* illegal while those in the second are judged under the rule of reason. Figuring out whether an activity should be treated as an illegal cartel or as a legitimate joint endeavor has often challenged the courts: we will meet some of these cases in Section C below.

The hardcore cartels that are often described as the "supreme evil" of antitrust involve both an agreement and a resulting naked restraint on competition.[346] Examples in recent memory include:

- **Auto parts.** A "supercartel" involving dozens of overlapping price-fixing and bid-rigging agreements, a vast network of auto-parts cartels was the subject of intensive prosecution by multiple international

[342] *See*, *e.g.*, United States v. Aiyer, 33 F.4th 97 (2d Cir. 2022) (holding that it "would have been legal error" to consider claimed procompetitive justifications for price-fixing, "absent a properly asserted exception to the *per se* rule").

[343] E.I. du Pont de Nemours & Co. v. FTC, 729 F.2d 128, 139 (2d Cir. 1984).

[344] *See*, *e.g.*, Analysis to Aid Public Comment, In the Matter of Fortiline, LLC, File No. 151-0000 (F.T.C. Aug. 9, 2016); Analysis to Aid Public Comment, In the Matter of U-Haul Int'l, Inc., File No. 081-0157 (F.T.C. June 9, 2010).

[345] United States v. Addyston Pipe & Steel Co., 85 F. 271, 282–84 (6th Cir. 1898) (distinguishing restrictive agreements that have "no main lawful purpose" and of which "the sole object is to restrain trade" from those that are "merely ancillary to the main purpose of a lawful contract, and necessary to protect the covenantee in the full enjoyment of the legitimate fruits of the contract, or to protect him from the dangers of an unjust use of those fruits by the other party").

[346] Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 408 (2004).

antitrust enforcers over about a decade from 2008 onward, resulting in the imposition of billions of dollars in penalties and fines, charges against dozens of companies, and indictments of many executives.[347]

- **Capacitors.** A major cartel of electrolytic capacitor manufacturers that operated between 1998 and 2012 has been the subject of significant penalties (amounting to hundreds of millions of dollars, in addition to U.S. criminal sanctions) in Europe and the United States.[348]
- **Lysine.** In a rare overlap between the world of antitrust and the world of Matt Damon, the blockbuster detection and prosecution of the lysine cartel is the subject of the 2009 movie *The Informant*, based on Kurt Eichenwald's book of the same name. The cartel, which involved suppliers of lysine, an additive to animal feed, included participants in the United States, Japan, and Korea, and led to prison time for multiple executives.[349] It is regarded as a watershed moment in modern cartel policy, and kicked off an era of increased criminal antitrust enforcement.

The following remarks of a senior DOJ official give a window into the life of the lysine cartel.

Scott D. Hammond, Caught in the Act: Inside an International Cartel

(Remarks of Oct. 18, 2005)

[1] Today you will experience the sensation of being a fly on the wall, watching as a crime is being committed. Actually, to be precise, you will be looking through the lens of a hidden camera, and the view is not from the wall but rather from a lamp tucked away in the corner of the room. However, the effect is still the same—these tapes will put you in the smoke-filled rooms with the members of an international price-fixing cartel as they formulate, agree upon, attempt to conceal, and carry out their conspiracy.

[2] The undercover audio and video tapes that you will see today were recorded by U.S. Federal Bureau of Investigation (FBI) agents with the help of a cooperating witness. The tapes capture an international cartel in the act of fixing prices and carving up the worldwide market for the feed additive, lysine, a product used by farmers around the world. Worldwide sales of lysine were over $600 million annually. The tapes reveal how the world's major lysine producers were able to secretly meet at trade association meetings around the world and agree on the exact tonnage each of them would produce and sell the next year, and then fix the price of it down to the penny in the United States and countries around the world, effective the very next day.

[3] One of the characteristics we see over and over again in international cartels is the brazen or lawless nature of the conspiracies. By that, I refer to the contempt and disregard that the members of the cartel typically have for antitrust laws and enforcement. I think this is a good place to begin because we are sometimes asked by defense counsel to treat a certain member of a cartel more favorably because he/she resides in a country where cartel activity is treated differently than it is in the United States. The fundamental problem with this argument is that it is our experience, without exception, that the conspirators are fully aware that they are violating the law in the United States and elsewhere, and their only concern is avoiding detection. The international cartels that we have cracked have not involved international business persons who for cultural, linguistic, or some other innocent reason find themselves mistakenly engaged in a violation of U.S. antitrust laws. Rather, the cartels that we have prosecuted criminally have invariably involved hard core cartel activity—price-fixing, bid-rigging, and market and customer-allocation agreements. The conspirators have discussed the criminal nature of their agreements; they have discussed the need to avoid detection by antitrust enforcers in the United States and abroad; and they have gone to great lengths to cover-up their actions—such as using code names with one another, meeting in secret venues around the world, creating false "covers"—*i.e.* facially legal justifications—for

---

[347] John M. Connor, *Twilight of Prosecutions of the Global Auto-Parts Cartels*, American Antitrust Institute Working Paper (July 17, 2019); Sharis A. Pozen, U.S. Dept. of Justice, *Briefing on Department's Enforcement Action in Auto Parts Industry* (remarks of Jan. 30, 2012).

[348] European Commission, Press Release, *Antitrust: Commission fines eight producers of capacitors €254 million for participating in cartel* (Mar. 21, 2018); U.S. Dept. of Justice, Press Release, *Leading Electrolytic Capacitor Manufacturer Ordered to Pay $60 Million Criminal Fine for Price Fixing* (Oct. 3, 2018).

[349] *See*, *e.g.*, Kurt Eichenwald, *The Tale of the Secret Tapes*, N.Y. TIMES (Nov. 16, 1997); U.S. Dept. of Justice, Press Release, Former Top ADM Executives, Japanese Executive, Indicted in Lysine Price Fixing Conspiracy (Dec. 3, 1996).

their meetings, using home phone numbers to contact one another, and giving explicit instructions to destroy any evidence of the conspiracy. Moreover, the cartels typically involve senior executives at firms—executives who have received extensive antitrust compliance counseling, and who often have significant responsibilities in the firm's antitrust compliance programs.

[4] The first tape segment captures this lawlessness and the contempt that the members of the cartel have for law enforcement and their victims. The meeting that you are about to see was attended by executives from the world's five dominant lysine producers. As you will see in this tape, the cartel members took steps to conceal their meeting, including staggering their arrival and departure times for the meeting so as not to arouse suspicion by having the entire group enter and leave the room at the same time. The members of the cartel had to be careful because the meeting coincided with the largest poultry industry trade association convention, so all of their customers were in town for the trade show. But, as you will see, the lysine executives laughed at the thought of being observed by their customers or by law enforcement. The videotaped recording of this meeting shows that, as the meeting begins, there are some empty seats around the table because of the staggered arrival times. The cartel members are captured on tape jokingly discussing who will fill those empty seats. One cartel member offered that one empty chair was for Tyson Foods, the largest purchaser of lysine in the United States, and that another chair was for ConAgra Foods, also a large U.S. customer. Another cartel member mocked, ironically, that one chair was for the FBI, and a third cartel executive added that the remaining chairs were for the Federal Trade Commission.

{*Eds.: a transcript of the clip played here is available at https://www.justice.gov/atr/tab-1-cartel-members-show-disdain-customers-and-antitrust-enforcement.*}

[5] The knock at the door heard at the very end of this tape segment, in fact, was an FBI agent, disguised as a hotel employee returning to the cooperating witness the briefcase containing a hidden audio recorder he had mistakenly left in the hotel restaurant. [. . .]

[6] While cartel members know full well that their conduct is illegal under the antitrust laws of many countries, they often have a particular fear of detection and prosecution by U.S. antitrust authorities resulting in jail sentences. Shortly after this investigation became public in 1995 and cartel members realized that the FBI might be watching, we learned from cooperating defendants in several investigations that the cartels changed their practices in order to avoid having meetings or calls in the United States and tried, where possible, to exclude the participation of U.S. personnel in the conspiracies. These same cartels continued to target U.S. businesses and consumers, but the meetings, the calls, the documents, and the participants largely resided safely overseas, or so they thought. This next segment demonstrates the initial reluctance of one of the foreign cartel members in the lysine conspiracy to conduct cartel activity in the United States for fear of detection. The conversation is between an ADM executive, who also was a cooperating witness, and an executive at the Japanese firm, Ajinomoto. They are discussing the location for the next cartel meeting. As you will hear, the Ajinomoto executive is clearly reluctant to have a cartel meeting in Hawaii, but ultimately agrees to consider it because Hawaii is a convenient location for everyone and because of the lure of the golf courses located near the meeting site. The Ajinomoto executive's reluctance was well founded, as the meeting was video taped by the FBI and became a critical piece of evidence in the prosecution of the lysine conspirators.

{*Eds.: a transcript of the clip played here is available at https://www.justice.gov/atr/tab-2-foreign-co-conspirator-expresses-reluctance-meet-united-states.*}

[7] Another characteristic of international cartels is that they frequently use trade associations as a means of providing "cover" for their cartel activities. In order to avoid arousing suspicion about the meetings they attended, the lysine conspirators actually created an amino acid working group or subcommittee of the European Feed Additives Association, a legitimate trade group. The sole purpose of the new subcommittee was to provide a false, but facially legitimate, explanation as to why they were meeting. [. . .]

{*Eds.: a transcript of the clip played here is available at https://www.justice.gov/atr/tab-3-cartel-members-use-trade-association-cover-conspiracy-meetings.*}

[8] Many cartels recognize that price-fixing schemes are more effective if the cartel also allocates sales volume among the firms. For example, the lysine, vitamin, graphite electrode, and citric acid cartels prosecuted by the Division all utilized volume-allocation agreements in conjunction with their price-fixing agreements. Cartel members typically meet to determine how much each producer has sold during the preceding year and to calculate the total market size. Next, the cartel members estimate the market growth for the upcoming year and allocate that growth among themselves. The volume-allocation agreement then becomes the basis for (1) an annual "budget" for the cartel, (2) a reporting and auditing function, and (3) a compensation scheme—three more common characteristics of international cartels.

[9] In this next tape segment, you will see the lysine cartel members divide up the world's lysine market. The meeting was attended by two high-ranking ADM executives. Representing all of the Japanese and Korean cartel members were two senior executives from Ajinomoto. Earlier in the meeting, the cartel members had determined how much each producer had sold in the prior year. Then, they used those figures to determine the total market size. Next, they estimated what they believed the sales growth would be in the coming year. All of these figures were written down on the easel board by one of the cartel members. On the tape, you'll see them decide how they are going to allocate that sales growth among the five cartel members. As you will hear, the growth in the market is estimated to be 14,000 tons, and the question posed by the senior ADM executive is: how do we divide this market growth? [. . .]

[10] Another common feature of international cartels is the use of a compensation scheme to discourage cheating. The compensation scheme used by the lysine cartel worked as follows. Any firm that had sold more than its allocated or budgeted share of the market at the end of the calendar year would compensate the firm or firms that were under budget by purchasing that quantity of lysine from any under-budget firms. This compensation agreement reduced the incentive to cheat on the sales volume-allocation agreement by selling additional product, which, of course, also reduced the incentive to cheat on the price-fixing agreement by lowering the price on the volume allocated to each conspirator firm.

[11] In this next segment, one of the lysine conspirators from ADM explains the importance of a compensation scheme to the cartel and gives the other cartel members a motivational speech that has to be one of the best pieces of evidence ever obtained in a cartel investigation. {*Eds.: this speech can be found here https://www.justice.gov/atr/tab-6-co-conspirator-explains-how-end-year-compensation-scheme-eliminates-incentive-cheat-cartel.*} *[. . .]*

[12] These tapes demonstrate the awesome power of cartels to rip-off businesses and consumers. Unbeknownst to their customers, five executives sitting in a hotel room can raise and fix prices around the world effective the very next day. International cartels, like the one involving vitamins, can operate profitably for a decade or more wholly undetected. The fact is that the obstacles to cracking cartels are huge. These are sophisticated, premeditated crimes committed by highly-educated individuals in absolute secrecy. In most cases, there will be no smoking guns left around and no cameras hidden in the lamps to capture the moment. Today's workshop will examine effective strategies for fighting cartels, but their successful deployment in a particular jurisdiction depends in large part on how seriously the jurisdiction views the threat posed by cartels to its economy. I hope that viewing these tapes has set the stage for today's program by making the case that hardcore cartel offenses deserve to be treated as crimes and that, wherever possible, competition authorities and public prosecutors must work closely together to prosecute these harmful offenses.

[13] The three U.S. executives representing ADM at the meetings—defendants Andreas, Wilson, and Whitacre—were convicted by a jury of violating the Sherman Antitrust Act and were sentenced to lengthy terms of imprisonment. The investigation also resulted in the conviction of all of the world's major lysine producers -- including one U.S. company, two Japanese companies, and two Korean companies. All of the producers pled guilty before trial and received substantial fines, including what was then a record-breaking $100 million fine imposed on ADM. Two Japanese executives and a Korean executive also agreed to plead guilty and cooperate after the search warrants were executed in the investigation, and they paid heavy individual fines. The lysine investigation eventually led the Division to evidence that exposed additional worldwide cartels operating in other chemical markets, including citric acid, sodium gluconate, sodium erythorbate, and maltol. In all, 10 companies

and 11 individuals from 7 different countries were convicted and paid over $225 million in criminal fines (in the United States alone) as a result of these five inter-connected investigations.

* * *

The classic cartel, like the lysine cartel itself, involves sellers of a product or service. But a cartel of buyers that agree on purchase prices is every bit as unlawful as a cartel of sellers that agree on sale prices.[350] And in the absence of an applicable antitrust exemption, the rule against naked collusion applies just as strongly in labor markets as in any others.[351] Putting these two propositions together suggests that wage-fixing by employers, like price-fixing by suppliers, is *per se* illegal.

In 2021 DOJ put this proposition to the test, prosecuting employers of physical therapy professionals for fixing wages. Although the defendants were ultimately acquitted of violating the law, the district court emphatically confirmed the *per se* illegality of wage fixing in the following passage.

United States v. Jindal

Case No. 4:20-CR-358, 2021 WL 5578687 (E.D. Tex. Nov. 29, 2021)

Judge Mazzant.

[1] For over 100 years, the Supreme Court has consistently held that price-fixing agreements are unlawful *per se* under the Sherman Act. In fact, the Supreme Court has stated that no antitrust offense is more pernicious than price fixing. Defendants do not dispute that the Supreme Court has designated price fixing as a per se Sherman Act violation. But Defendants do dispute that the Indictment in-fact alleges a price-fixing agreement.

[2] The core of Defendants' argument is that the Indictment does not allege a price-fixing agreement because it at most alleges an agreement to fix wages. . . . Defendants argue that the Indictment does not allege any agreement to fix prices because wages do not fall within the definition of price fixing, which is defined as fixing the price of a. commodity. Further, according to Defendants, merely substituting the word "prices" for "wages" does not transform the factual allegations from alleging a wage-fixing agreement to alleging a price-fixing agreement. But Defendants' narrow view of horizontal price-fixing agreements reveals the flaw in their arguments.

[3] The scope of conduct found to constitute horizontal price-fixing agreements warranting application of the per se rule is broad. For example, courts have applied the per se rule to price-fixing agreements: 1) establishing minimum prices, 2) setting maximum prices, 3) fixing credit terms, 4) setting fee schedules, 5) purchasing surplus product to keep it off the market, 6) refusing to advertise prices, and 7) excluding purchasers unless they increased the price they paid for a service. Thus, contrary to Defendants' argument, "price fixing" has not been limited to conduct that literally directly fixes the price of a commodity. Instead, as the above cases and many more have recognized, the definition of horizontal price-fixing agreements cuts broadly. As such, any naked agreement among competitors—whether by sellers or buyers—that fixes components that affect price meets the definition of a horizontal price-fixing agreement.

[4] The Court recognizes that the facts of this case do not present those typical of a price-fixing agreement. For example, the classic horizontal price-fixing scheme involves an agreement among sellers to fix the prices of goods they sell. But just because the typical price-fixing conspiracy involves certain hallmarks does not mean that other less prevalent forms of price-fixing agreements are not likewise unlawful. Indeed, Courts have not limited price-fixing conspiracies to agreements concerning the purchase and sale of goods but have found them to cover the purchase and sale of services. More importantly, courts have also not only found price-fixing agreements among

---

[350] *See, e.g.*, Mandeville Island Farms v. American Crystal Sugar Co., 334 U.S. 219, 235 (1948) ("It is clear that the agreement is the sort of combination condemned by the Act, even though the price-fixing was by purchasers, and the persons specially injured under the treble damage claim are sellers, not customers or consumers."); Vogel v. Am. Soc. of Appraisers, 744 F.2d 598, 601 (7th Cir. 1984) ("[B]uyer cartels, the object of which is to force the prices that suppliers charge the members of the cartel below the competitive level, are illegal per se."); Nat'l Macaroni Mfrs. Ass'n v. FTC, 345 F.2d 421 (7th Cir. 1965).

[351] *See infra* Chapter X (describing labor exemptions).

sellers, but also among buyers. In sum, price-fixing agreements come in many forms and include agreements among competing buyers of services.

[5] The Supreme Court has made clear that the Sherman Act applies equally to all industries and markets—to sellers and buyers, to goods and services, and consequently to buyers of services—otherwise known as employers in the labor market. . . . .

[6] With these principles in mind, the Court turns to the Indictment to determine if it alleges a price-fixing agreement that is per se illegal. The Indictment alleges that Jindal, Rodgers, and co-conspirators knowingly entered into and engaged in a conspiracy to suppress competition by agreeing to fix prices by lowering the pay rates to [physical therapists and physical therapy assistants ("PTs" and "PTAs")]. The Indictment thus alleges a naked price-fixing conspiracy among buyers in the labor market to fix the pay rates of the PTs and PTAs. As such, the Indictment describes a price-fixing conspiracy that is per se unlawful. . . . Accordingly, the Indictment sufficiently alleges a price-fixing conspiracy that warrants the per se rule.

[7] Defendants do not dispute that price-fixing agreements are per se illegal; they do, however, challenge how the Government labeled the offense and whether the charged conduct constitutes a per se offense. But, contrary to Defendants' argument, whether the Indictment refers to the "pay rates" of the PTs and PTAs as "prices" or "wages" does not affect the outcome. The antitrust laws fully apply to the labor markets, and price-fixing agreements among buyers—like therapist staffing companies—are prohibited by the Sherman Act. At bottom, the alleged agreement between Defendants and co-conspirators had the purpose and effect of fixing the pay rates of the PTs and PTAs—the price of labor.

[8] When the price of labor is lowered, or wages are suppressed, fewer people take jobs, which always or almost always tend[s] to restrict competition and decrease output. This type of agreement is plainly anticompetitive and has no purpose except stifling competition. [. . .]

[9] The Indictment charges Defendants with price fixing. For more than 100 years, courts have repeatedly held price fixing as per se illegal under the Sherman Act. Thus, Defendants could not have had any reasonable doubt that any price-fixing agreement was per se illegal. Defendants do not dispute this conclusion and instead insist that the novel construction of the statute to construe wage fixing as per se unlawful fails to give fair warning of the prohibited conduct. But this argument relies on the same semantical arguments this Court already rejected.

[10] Regardless of whether the Indictment characterizes Defendants' conduct as wage fixing or price fixing, the Sherman Act, in conjunction with the decades of case law, made it reasonably clear that Defendants' conduct was unlawful. Indeed, most criminal statutes deal with untold and unforeseen variations in factual situations, so no more than a reasonable degree of certainty can be demanded. Belaboring the point discussed in Part I, the Supreme Court has long recognized that price-fixing agreements come in many forms. And the Supreme Court has long recognized that § 1 categorically prohibits per se unlawful restraints across all markets and industries—including restraints on the buyer side and in the labor market. Thus, decades of precedent gave Defendants more than sufficient notice that agreements among competitors to fix the price of labor are per se illegal. Moreover, the numerous district court decisions holding that agreements to fix the compensation of employees are per se unlawful reinforce this conclusion. At a minimum, these decisions foreclose Defendants' argument because it cannot be said that no prior judicial decision has fairly disclosed Defendants' conduct to be within the scope of the Sherman Act.

[11] Moreover, the holding today is not a "novel" construction of the Sherman Act—it comports with previous broad interpretations of the Act and is a logical application of precedent. Similarly, that no court has found that purported wage-fixing agreements constitute criminal conduct under the Sherman Act does not mean that Defendants' did not have fair notice. Rather, the lack of criminal judicial decisions only indicates Defendants' unlucky status as the first two individuals that the Government has prosecuted for this type of conduct before.

[12] But, to find unfair notice whenever a court specified new types of acts to which a criminal statute applied would stifle courts' ability to interpret and fairly apply criminal statutes. Rather, . . . lack of prior court interpretations fundamentally similar to the case in question does not create unfair notice. Instead, so long as the prior decisions gave reasonable warning that the conduct was unlawful, then fair notice was satisfied. And, here,

decades of judicial interpretations gave Defendants more than reasonably clear notice that their conduct was unlawful.

[13] [E]ven accepting Defendants' argument that their conduct was not literally price fixing, Defendants were still on notice that their conduct was perilously close to a line that subjected them to criminal prosecution. Thus, Defendants received fair notice that their conduct was illegal.

NOTES

1) Suppose that you organize a group of consumers to boycott a store whose prices you feel are too high, or whose products are not safe enough. Is that a *per se* illegal—and potentially criminal—violation of Section 1?
2) As we saw in Chapter II, a buyers' cartel that exercises monopsony power can reduce purchase prices to infracompetitive levels, which in turn reduces output in the upstream market. But it might also lower the costs of the cartel participants, including in ways that might be passed on (at least to some extent) to consumers. Does this fact suggest that *per se* treatment is inappropriate?
3) Do you think a buyers' cartel should be treated more leniently if it is facing sellers with market or monopoly power, or who may be themselves engaging in unlawful conduct?
4) In 2010, DOJ settled with six tech companies for agreeing not to approach each others' employees with job offers.[352] What standard should apply to such an agreement in litigation? Why do you think DOJ settled?
5) Why do you think the prosecution of wage-fixing cartels has not been a prominent theme in the history of antitrust enforcement?

2. Bid Rigging and Market Division

The *per se* rule is not limited to literal fixing of sale and purchase prices. Naked agreements among competitors to simply refrain from competition with one another are equally unlawful. Two common ways in which this might be done are through the division or allocation of markets (in which the participants effectively agree to stay out of each other's way) and through the rigging of bids (in which the participants collusively pre-bake the operation and outcome of a competitive tender or bidding process). Such practices are *per se* illegal, just like the simple fixing of sale and purchase prices, and may be the subject of criminal enforcement attention.

In *Palmer*, for example, rather than fixing their prices, two bar-review prep service providers simply agreed to stay out of each other's geographic markets. The Supreme Court was not impressed. (Why do you think the trade name license was not enough to transmute the market-division agreement into a procompetitive collaboration?)

Palmer v. BRG of Georgia, Inc.

498 U.S. 46 (1990)

Per Curiam.

[1] In preparation for the 1985 Georgia Bar Examination, petitioners contracted to take a bar review course offered by respondent BRG of Georgia, Inc. (BRG). In this litigation, they contend that the price of BRG's course was enhanced by reason of an unlawful agreement between BRG and respondent Harcourt Brace Jovanovich Legal and Professional Publications (HBJ), the Nation's largest provider of bar review materials and lecture services. The central issue is whether the 1980 agreement between respondents violated § 1 of the Sherman Act.[. . .]

[2] HBJ began offering a Georgia bar review course on a limited basis in 1976, and was in direct, and often intense, competition with BRG during the period from 1977–1979. BRG and HBJ were the two main providers of bar review courses in Georgia during this time period. In early 1980, they entered into an agreement that gave BRG an exclusive license to market HBJ's material in Georgia and to use its trade name "Bar/Bri." The

[352] U.S. Dept. of Justice, Press Release, Justice Department Requires Six High Tech Companies to Stop Entering into Anticompetitive Employee Solicitation Agreements (Sept. 24, 2010).

parties agreed that HBJ would not compete with BRG in Georgia and that BRG would not compete with HBJ outside of Georgia. Under the agreement, HBJ received $100 per student enrolled by BRG and 40% of all revenues over $350. Immediately after the 1980 agreement, the price of BRG's course was increased from $150 to over $400.

[3] The 1980 agreement contained two provisions, one called a "Covenant Not to Compete" and the other called "Other Ventures." The former required HBJ not to "directly or indirectly own, manage, operate, join, invest, control, or participate in or be connected as an officer, employee, partner, director, independent contractor or otherwise with any business which is operating or participating in the preparation of candidates for the Georgia State Bar Examination." The latter required BRG not to compete against HBJ in states in which HBJ currently operated outside the state of Georgia.

[4] On petitioners' motion for partial summary judgment as to the § 1 counts in the complaint and respondents' motion for summary judgment, the District Court held that the agreement was lawful. The United States Court of Appeals for the Eleventh Circuit, with one judge dissenting, agreed with the District Court that *per se* unlawful horizontal price fixing required an explicit agreement on prices to be charged or that one party have the right to be consulted about the other's prices. The Court of Appeals also agreed with the District Court that to prove a *per se* violation under a geographic market allocation theory, petitioners had to show that respondents had subdivided some relevant market in which they had previously competed. The Court of Appeals denied a petition for rehearing en banc that had been supported by the United States.

[5] In dissent, Judge Clark explained that, in his view, HBJ and BRG were capable of engaging in *per se* horizontal restraints because they had competed against each other, and then had joined forces. He believed the District Court's analysis was flawed because it had failed to recognize that the agreements could be price-fixing agreements even without explicit reference to price, and because it had failed to recognize that allocation, rather than subdivision, of markets could also constitute a *per se* antitrust violation.

[6] The United States, as *amicus curiae*, had urged the court to adopt the views of the dissent.

[7] In United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940), we held that an agreement among competitors to engage in a program of buying surplus gasoline on the spot market in order to prevent prices from falling sharply was unlawful, even though there was no direct agreement on the actual prices to be maintained. We explained that [u]nder the Sherman Act, a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal *per se*.

[8] The revenue-sharing formula in the 1980 agreement between BRG and HBJ, coupled with the price increase that took place immediately after the parties agreed to cease competing with each other in 1980, indicates that this agreement was "formed for the purpose and with the effect of raising" the price of the bar review course. It was, therefore, plainly incorrect for the District Court to enter summary judgment in respondents' favor. Moreover, it is equally clear that the District Court and the Court of Appeals erred when they assumed that an allocation of markets or submarkets by competitors is not unlawful unless the market in which the two previously competed is divided between them.

[9] In United States v. Topco Associates, Inc., 405 U.S. 596 (1972), we held that agreements between competitors to allocate territories to minimize competition are illegal:

> One of the classic examples of a *per se* violation of § 1 is an agreement between competitors at the same level of the market structure to allocate territories in order to minimize competition. . . . This Court has reiterated time and time again that horizontal territorial limitations . . . are naked restraints of trade with no purpose except stifling of competition. Such limitations are *per se* violations of the Sherman Act.

[10] The defendants in *Topco* had never competed in the same market, but had simply agreed to allocate markets. Here, HBJ and BRG had previously competed in the Georgia market; under their allocation agreement, BRG received that market, while HBJ received the remainder of the United States. Each agreed not to compete in the other's territories. Such agreements are anticompetitive regardless of whether the parties split

a market within which both do business or whether they merely reserve one market for one and another for the other. Thus, the 1980 agreement between HBJ and BRG was unlawful on its face.

* * *

Just like market allocation, the collusive rigging of a competitive bidding process is a *per se* illegal activity. This might be done in a variety of ways: for example, competitors might agree to "rotate" the role of bidding to avoid head-to-head competition, or might just fix the prices at which bids will be submitted, to create the appearance of competition without the reality.[353] In 1992, for example, the Fifth Circuit upheld criminal verdicts against a group of pipe distributors for participating in a cartel run by one of their customers: the customer would win client contracts on a "cost-plus" basis, and then run a rigged "bidding" process among the distributors, passing on the inflated cost to the customer and sharing the overcharge.[354] "[D]efendants cannot escape the per se rule," the court held, "simply because their conspiracy depended upon the participation of a 'middle-man,' even if that middleman conceptualized the conspiracy, orchestrated it by bringing the distributors together . . . , and collected most of the booty."[355]

NOTES

1) *Palmer* emphasizes that *per se* liability neither requires an explicit agreement on price, nor (in the context of a market allocation agreement) that the parties must have previously been competitors in the market they are sub-dividing. Do these understandings of the *per se* rule make sense? Why do you think the *Palmer* Court made these points?'
2) In *Palmer* the parties had entered into an exclusive license. So why was their activity considered nakedly anticompetitive, rather than a procompetitive joint economic investment in the Bar/Bri brand? Isn't this the kind of joint economic activity that the rule of reason is intended to evaluate? Or is that the wrong way to think about what was going on in *Palmer*?

3. Group Boycotts

Agreements among competitors to refrain from dealing with trading partners—"group boycotts," or "concerted refusals to deal"—are often described as *per se* illegal. But this rule is a controversial one, and the Supreme Court has sheepishly conceded that its application is particularly confusing.[356] In this section we will meet a trinity of famous Supreme Court boycott cases: *Klor's* (1959), *Northwest Stationers* (1985), and *Superior Court Trial Lawyers* (1990). In the first and third, the Supreme Court applied the *per se* rule; in the second, the Court applied the rule of reason.

As you read, think about the wide variety of contexts in which competitors might jointly refuse to deal with others. In the first two cases, the group boycott takes place in a purely commercial setting: in *Klor's*, the plaintiff alleges (perhaps implausibly) that suppliers have agreed to boycott a disfavored retailer; in *Northwest Stationers*, the plaintiff complains of being excluded from a joint buying group. But in the third case, the group boycott is not purely commercial—it involves lawyers agreeing not to represent indigent criminal defendants until the local

[353] *See*, *e.g.*, United States v. Romer, 148 F.3d 359, 363 (4th Cir. 1998) ("Appellants are real estate speculators who, together with others, participated in a conspiracy to limit bidding competition at certain public foreclosure auctions in Fairfax County, Virginia. The purpose of the conspiracy was to hold down the price of auctioned properties by agreeing not to bid against one another at auctions—an activity commonly known as "bid-rigging." During an auction, most members of the conspiracy would refrain from bidding, while one designated member would bid on and receive the property at a much-reduced price. Following the auction, members of the conspiracy would hold a private auction amongst themselves, at which point they would discuss the price they each would have bid for the property. The person with the highest bid would be given the deed, and the conspirators would divide amongst themselves the money saved by artificially holding down the price of the property."). *See also*, *e.g.*, United States v. Heffernan, 43 F.3d 1144 (7th Cir. 1994) (considering the application of federal sentencing guidelines to "bid rigging" in comparison to other forms of naked collusion).

[354] United States v. All Star Industries, 962 F.2d 465 (5th Cir. 1992).

[355] United States v. All Star Industries, 962 F.2d 465, 473 (5th Cir. 1992).

[356] *See* Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co., 472 U.S. 284, 294 (1985) ("Exactly what types of activity fall within the forbidden category is, however, far from certain. There is more confusion about the scope and operation of the per se rule against group boycotts than in reference to any other aspect of the per se doctrine.") (internal quotation marks and citation omitted).

government raised the wage for doing so: it could fairly be described as an effort to ensure that indigent defendants receive competent counsel in criminal cases.

Read together, do the opinions provide a compelling case for applying the *per se* rule to a subset of group boycotts? Is the treatment of group boycotts rational and consistent?

CASENOTE: Klor's v. Broadway-Hale Stores

359 U.S. 207 (1959)

Klor's is probably the most famous (or infamous?) decision applying the *per se* rule to a group boycott. Klor's was a retailer of televisions, refrigerators, and other appliances on Mission Street in San Francisco: Broadway-Hale, a chain of department stores, owned a store next door. Klor's alleged that Broadway-Hale had conspired with a number of appliance manufacturers to cut off Klor's from access to appliances, and that this violated Section 1 (and 2!) of the Sherman Act. In other words, Klor's argued that manufacturers were boycotting Klor's at Broadway-Hale's request.

The district court granted summary judgment for Broadway-Hale, among other reasons because the challenged conduct had no discernible effect on competition: that is, no impact on the overall availability, price, output, quality, or variety of appliances. In fact, the very same appliances were widely available elsewhere on the same street. The district court noted that "a member of the public desiring to purchase an appliance and strolling down Mission Street for a span of but 11 blocks, of which [Klor's] is approximately in the center, would pass the shops of 43 retailers, selling the specific items and brands referred to in the complaint." Klor's appealed to the Ninth Circuit, which affirmed the district court. In doing so, the court of appeals emphasized that "[t]he purpose of the antitrust statutes is to protect the public from the harm which follows from concerted or monopolistic conduct designed to acquire control of a market," and had concluded that there was no evidence that the decision by manufacturers to sell to Broadway-Hale instead of Klor's had caused such public harm. Indeed, the court noted, even Klor's seemed to have plenty of alternatives: "there are numerous brands of appliances to which plaintiff was not denied access and which compete favorably with those he was denied."

But the Supreme Court reversed. Writing for the Court, Justice Black framed the central issue as whether "a group of powerful businessmen may act in concert to deprive a single merchant, like Klor, of the goods he needs to compete effectively." Noting that some forms of conduct are *per se* illegal, the Court held that "[g]roup boycotts, or concerted refusals by traders to deal with other traders, have long been held to be in the forbidden category. They have not been saved by allegations that they were reasonable in the specific circumstances, nor by a failure to show that they fixed or regulated prices, parcelled out or limited production, or brought about a deterioration in quality. Even when they operated to lower prices or temporarily to stimulate competition they were banned." He continued: "This is not a case of a single trader refusing to deal with another, nor even of a manufacturer and a dealer agreeing to an exclusive distributorship. Alleged in this complaint is a wide combination consisting of manufacturers, distributors and a retailer. This combination takes from Klor's its freedom to buy appliances in an open competitive market and drives it out of business as a dealer in the defendants' products." Thus, summary judgment for Broadway-Hale was inappropriate.

Klor's stands as a landmark authority for the proposition that group boycotts among competitors can, at least sometimes, be illegal *per se*. Later cases like *Northwest Stationers* and *Superior Court Trial Lawyers* have struggled to articulate the bounds of this *per se* rule. But *Klor's* remains a puzzling and frustrating case. Most importantly, there did not seem to be any reason to infer a horizontal agreement among manufacturers: or even to think that one was particularly plausible. At most, what seems to have happened is that a department store asked its suppliers not to sell literally identical appliances to the store literally next door, even though those very same appliances were broadly available from other stores on the same street. That, of course, would be a series of vertical agreements between Broadway-Hale and its suppliers, involving no coordination among competitors, and with no suggestion that these vertical agreements created market power or generated anticompetitive effects. Nor does there seem to be any reason to think the manufacturers would have needed or wanted to agree with one another to cut off Klor's.

In sum: *Klor's* leaves us with the knowledge that some group boycotts are illegal *per se*—and the sense that if the same facts came before the Court today they would probably not be considered a group boycott at all.

Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.

472 U.S. 284 (1985)

Justice Brennan.

[1] This case requires that we decide whether a per se violation of § 1 of the Sherman Act, 15 U.S.C. § 1, occurs when a cooperative buying agency comprising various retailers expels a member without providing any procedural means for challenging the expulsion. The case also raises broader questions as to when per se antitrust analysis is appropriately applied to joint activity that is susceptible of being characterized as a concerted refusal to deal. [. . .]

[2] Petitioner Northwest Wholesale Stationers is a purchasing cooperative made up of approximately 100 office supply retailers in the Pacific Northwest States. The cooperative acts as the primary wholesaler for the retailers. Retailers that are not members of the cooperative can purchase wholesale supplies from Northwest at the same price as members. At the end of each year, however, Northwest distributes its profits to members in the form of a percentage rebate on purchases. Members therefore effectively purchase supplies at a price significantly lower than do nonmembers. Northwest also provides certain warehousing facilities. The cooperative arrangement thus permits the participating retailers to achieve economies of scale in purchasing and warehousing that would otherwise be unavailable to them. In fiscal 1978 Northwest had $5.8 million in sales.

[3] Respondent Pacific Stationery & Printing Co. sells office supplies at both the retail and wholesale levels. Its total sales in fiscal 1978 were approximately $7.6 million; the record does not indicate what percentage of revenue is attributable to retail and what percentage is attributable to wholesale. Pacific became a member of Northwest in 1958. In 1974 Northwest amended its bylaws to prohibit members from engaging in both retail and wholesale operations. A grandfather clause preserved Pacific's membership rights. In 1977 ownership of a controlling share of the stock of Pacific changed hands, and the new owners did not officially bring this change to the attention of the directors of Northwest. This failure to notify apparently violated another of Northwest's bylaws.

[4] In 1978 the membership of Northwest voted to expel Pacific. Most factual matters relevant to the expulsion are in dispute. No explanation for the expulsion was advanced at the time, and Pacific was given neither notice, a hearing, nor any other opportunity to challenge the decision. Pacific argues that the expulsion resulted from Pacific's decision to maintain a wholesale operation. Northwest contends that the expulsion resulted from Pacific's failure to notify the cooperative members of the change in stock ownership. The minutes of the meeting of Northwest's directors do not definitively indicate the motive for the expulsion. It is undisputed that Pacific received approximately $10,000 in rebates from Northwest in 1978, Pacific's last year of membership. Beyond a possible inference of loss from this fact, however, the record is devoid of allegations indicating the nature and extent of competitive injury the expulsion caused Pacific to suffer.

[5] Pacific brought suit in 1980 in the United States District Court for the District of Oregon alleging a violation of § 1 of the Sherman Act. The gravamen of the action was that Northwest's expulsion of Pacific from the cooperative without procedural protections was a group boycott that limited Pacific's ability to compete and should be considered per se violative of § 1. On cross-motions for summary judgment the District Court rejected application of the per se rule and held instead that rule-of-reason analysis should govern the case. Finding no anticompetitive effect on the basis of the record as presented, the court granted summary judgment for Northwest.

[6] The Court of Appeals for the Ninth Circuit reversed, holding that the uncontroverted facts of this case support a finding of per se liability. The court reasoned that the cooperative's expulsion of Pacific was an anticompetitive concerted refusal to deal with Pacific on equal footing, which would be a per se violation of § 1 in the absence of any specific legislative mandate for self-regulation sanctioning the expulsion. [. . .]

[7] This Court has long held that certain concerted refusals to deal or group boycotts are so likely to restrict competition without any offsetting efficiency gains that they should be condemned as per se violations of § 1 of the Sherman Act. The question presented in this case is whether Northwest's decision to expel Pacific should fall within this category of activity that is conclusively presumed to be anticompetitive. The Court of Appeals held that the exclusion of Pacific from the cooperative should conclusively be presumed unreasonable on the ground that Northwest provided no procedural protections to Pacific. Even if the lack of procedural protections does not justify a conclusive presumption of predominantly anticompetitive effect, the mere act of expulsion of a competitor from a wholesale cooperative might be argued to be sufficiently likely to have such effects under the present circumstances and therefore to justify application of the per se rule. [. . .]

[8] This case . . . turns . . . on whether the decision to expel Pacific is properly viewed as a group boycott or concerted refusal to deal mandating per se invalidation. Group boycotts are often listed among the classes of economic activity that merit per se invalidation under § 1. Exactly what types of activity fall within the forbidden category is, however, far from certain. There is more confusion about the scope and operation of the per se rule against group boycotts than in reference to any other aspect of the per se doctrine. Some care is therefore necessary in defining the category of concerted refusals to deal that mandate per se condemnation.

[9] Cases to which this Court has applied the per se approach have generally involved joint efforts by a firm or firms to disadvantage competitors by either directly denying or persuading or coercing suppliers or customers to deny relationships the competitors need in the competitive struggle. In these cases, the boycott often cut off access to a supply, facility, or market necessary to enable the boycotted firm to compete, and frequently the boycotting firms possessed a dominant position in the relevant market. In addition, the practices were generally not justified by plausible arguments that they were intended to enhance overall efficiency and make markets more competitive. Under such circumstances the likelihood of anticompetitive effects is clear and the possibility of countervailing procompetitive effects is remote.

[10] Although a concerted refusal to deal need not necessarily possess all of these traits to merit per se treatment, not every cooperative activity involving a restraint or exclusion will share with the per se forbidden boycotts the likelihood of predominantly anticompetitive consequences. For example, we recognized last Term in *National Collegiate Athletic Assn. v. Board of Regents of University of Oklahoma* [468 U.S. 85 (1984)] that per se treatment of the NCAA's restrictions on the marketing of televised college football was inappropriate—despite the obvious restraint on output—because the "case involves an industry in which horizontal restraints on competition are essential if the product is to be available at all."

[11] Wholesale purchasing cooperatives such as Northwest are not a form of concerted activity characteristically likely to result in predominantly anticompetitive effects. Rather, such cooperative arrangements would seem to be designed to increase economic efficiency and render markets more, rather than less, competitive. The arrangement permits the participating retailers to achieve economies of scale in both the purchase and warehousing of wholesale supplies, and also ensures ready access to a stock of goods that might otherwise be unavailable on short notice. The cost savings and order-filling guarantees enable smaller retailers to reduce prices and maintain their retail stock so as to compete more effectively with larger retailers.

[12] Pacific, of course, does not object to the existence of the cooperative arrangement, but rather raises an antitrust challenge to Northwest's decision to bar Pacific from continued membership. It is therefore the action of expulsion that must be evaluated to determine whether per se treatment is appropriate. The act of expulsion from a wholesale cooperative does not necessarily imply anticompetitive animus and thereby raise a probability of anticompetitive effect. Wholesale purchasing cooperatives must establish and enforce reasonable rules in order to function effectively. Disclosure rules, such as the one on which Northwest relies, may well provide the cooperative with a needed means for monitoring the creditworthiness of its members. Nor would the expulsion characteristically be likely to result in predominantly anticompetitive effects, at least in the type of situation this case presents. Unless the cooperative possesses market power or exclusive access to an element essential to effective competition, the conclusion that expulsion is virtually always likely to have an anticompetitive effect is not warranted. Absent such a showing with respect to a cooperative buying arrangement, courts should apply a rule-of-reason analysis. At no time has Pacific made a threshold showing that these structural characteristics are present in this case.

[13] The District Court appears to have followed the correct path of analysis—recognizing that not all concerted refusals to deal should be accorded per se treatment and deciding this one should not. The foregoing discussion suggests, however, that a satisfactory threshold determination whether anticompetitive effects would be likely might require a more detailed factual picture of market structure than the District Court had before it. Nonetheless, in our judgment the District Court's rejection of per se analysis in this case was correct. A plaintiff seeking application of the per se rule must present a threshold case that the challenged activity falls into a category likely to have predominantly anticompetitive effects. The mere allegation of a concerted refusal to deal does not suffice because not all concerted refusals to deal are predominantly anticompetitive. When the plaintiff challenges expulsion from a joint buying cooperative, some showing must be made that the cooperative possesses market power or unique access to a business element necessary for effective competition. Focusing on the argument that the lack of procedural safeguards required per se liability, Pacific did not allege any such facts. Because the Court of Appeals applied an erroneous per se analysis in this case, the court never evaluated the District Court's rule-of-reason analysis rejecting Pacific's claim. A remand is therefore appropriate for the limited purpose of permitting appellate review of that determination.

[14] The per se rule is a valid and useful tool of antitrust policy and enforcement. It does not denigrate the per se approach to suggest care in application. In this case, the Court of Appeals failed to exercise the requisite care and applied per se analysis inappropriately. The judgment of the Court of Appeals is therefore reversed, and the case is remanded for further proceedings consistent with this opinion.

* * *

In the following extract, Justice Stevens' opinion for the Court refers to the doctrine that conduct is immune from antitrust liability if it involves constitutionally protected petitioning of government. This principle, often called the "*Noerr-Pennington*" doctrine (after the decisions in *Eastern Railroad Presidents Conference* v. *Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961) and *United Mine Workers of America v. Pennington*, 381 U.S. 657 (1965)), will be on our menu in Chapter IX. For now, all you need to know to make sense of the following is that the doctrine exists!

FTC v. Superior Court Trial Lawyers Ass'n

493 U.S. 411 (1990)

Justice Stevens.

[1] Pursuant to a well-publicized plan, a group of lawyers agreed not to represent indigent criminal defendants in the District of Columbia Superior Court until the District of Columbia government increased the lawyers' compensation. The questions presented are whether the lawyers' concerted conduct violated § 5 of the Federal Trade Commission Act and, if so, whether it was nevertheless protected by the First Amendment to the Constitution.

[2] The burden of providing competent counsel to indigent defendants in the District of Columbia is substantial. During 1982, court-appointed counsel represented the defendant in approximately 25,000 cases. In the most serious felony cases, representation was generally provided by full-time employees of the District's Public Defender System (PDS). Less serious felony and misdemeanor cases constituted about 85 percent of the total caseload. In these cases, lawyers in private practice were appointed and compensated pursuant to the District of Columbia Criminal Justice Act (CJA).

[3] Although over 1,200 lawyers have registered for CJA appointments, relatively few actually apply for such work on a regular basis. In 1982, most appointments went to approximately 100 lawyers who are described as "CJA regulars." These lawyers derive almost all of their income from representing indigents. In 1982, the total fees paid to CJA lawyers amounted to $4,579,572.

[4] In 1974, the District created a Joint Committee on Judicial Administration with authority to establish rates of compensation for CJA lawyers not exceeding the rates established by the federal Criminal Justice Act of 1964. After 1970, the federal Act provided for fees of $30 per hour for court time and $20 per hour for out-of-court

time. These rates accordingly capped the rates payable to the District's CJA lawyers, and could not be exceeded absent amendment to either the federal statute or the District Code.

[5] Bar organizations began as early as 1975 to express concern about the low fees paid to CJA lawyers. Beginning in 1982, respondents, the Superior Court Trial Lawyers Association (SCTLA) and its officers, and other bar groups sought to persuade the District to increase CJA rates to at least $35 per hour. Despite what appeared to be uniform support for the bill, it did not pass. It is also true, however, that nothing in the record indicates that the low fees caused any actual shortage of CJA lawyers or denied effective representation to defendants.

[6] In early August 1983, in a meeting with officers of SCTLA, the Mayor expressed his sympathy but firmly indicated that no money was available to fund an increase. The events giving rise to this litigation then ensued.

[7] At an SCTLA meeting, the CJA lawyers voted to form a "strike committee." The eight members of that committee promptly met and informally agreed "that the only viable way of getting an increase in fees was to stop signing up to take new CJA appointments, and that the boycott should aim for a $45 out-of-court and $55 in-court rate schedule."

[8] On August 11, 1983, about 100 CJA lawyers met and resolved not to accept any new cases after September 6 if legislation providing for an increase in their fees had not passed by that date. Immediately following the meeting, they prepared (and most of them signed) a petition stating:

> We, the undersigned private criminal lawyers practicing in the Superior Court of the District of Columbia, agree that unless we are granted a substantial increase in our hourly rate we will cease accepting new appointments under the Criminal Justice Act.

[9] On September 6, 1983, about 90 percent of the CJA regulars refused to accept any new assignments. Thereafter, SCTLA arranged a series of events to attract the attention of the news media and to obtain additional support. These events were well publicized and did engender favorable editorial comment, but the Administrative Law Judge (ALJ) found that "there is no credible evidence that the District's eventual capitulation to the demands of the CJA lawyers was made in response to public pressure, or, for that matter, that this publicity campaign actually engendered any significant measure of public pressure."

[10] As the participating CJA lawyers had anticipated, their refusal to take new assignments had a severe impact on the District's criminal justice system. The massive flow of new cases did not abate, and the need for prompt investigation and preparation did not ease. . . . The overall response of the uptown lawyers to the PDS call for help was feeble, reflecting their universal distaste for criminal law, their special aversion for compelled indigency representation, the near epidemic siege of self-doubt about their ability to handle cases in this field, and their underlying support for the demands of the CJA lawyers. . . .

[11] Within 10 days, the key figures in the District's criminal justice system "became convinced that the system was on the brink of collapse because of the refusal of CJA lawyers to take on new cases." On September 15, they hand-delivered a letter to the Mayor describing why the situation was expected to "reach a crisis point" by early the next week and urging the immediate enactment of a bill increasing all CJA rates to $35 per hour. The Mayor promptly met with members of the strike committee and offered to support an immediate temporary increase to the $35 level as well as a subsequent permanent increase to $45 an hour for out-of-court time and $55 for in-court time.

[12] At noon on September 19, 1983, over 100 CJA lawyers attended an SCTLA meeting and voted to accept the $35 offer and end the boycott. The city council's Judiciary Committee convened at 2 o'clock that afternoon. The committee recommended legislation increasing CJA fees to $35, and the council unanimously passed the bill on September 20. On September 21, the CJA regulars began to accept new assignments and the crisis subsided.

[13] The Federal Trade Commission (FTC) filed a complaint against SCTLA and four of its officers (respondents) alleging that they had "entered into an agreement among themselves and with other lawyers to restrain trade by refusing to compete for or accept new appointments under the CJA program beginning on

September 6, 1983, unless and until the District of Columbia increased the fees offered under the CJA program." The complaint alleged that virtually all of the attorneys who regularly compete for or accept new appointments under the CJA program had joined the agreement. The FTC characterized respondents' conduct as "a conspiracy to fix prices and to conduct a boycott" and concluded that they were engaged in "unfair methods of competition in violation of Section 5 of the Federal Trade Commission Act." {*Eds.: The FTC's complaint was filed in "Part 3" administrative proceedings, before an Administrative Law Judge ("ALJ") at the Federal Trade Commission, who heard the arguments of the FTC's "complaint counsel" and of the defendants. The FTC's unique statutory power to file antitrust enforcement actions in administrative court is discussed in more detail in Chapter XI below.*}

[14] After a 3-week hearing, the ALJ found that the facts alleged in the complaint had been proved, and rejected each of respondents' three legal defenses—that the boycott was adequately justified by the public interest in obtaining better legal representation for indigent defendants; that as a method of petitioning for legislative change it was exempt from the antitrust laws under our decision in *Eastern Railroad Presidents Conference* v. *Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); and that it was a form of political action protected by the First Amendment under our decision in *NAACP* v. *Claiborne Hardware Co.*, 458 U.S. 886 (1982). The ALJ nevertheless concluded that the complaint should be dismissed because the District officials, who presumably represented the victim of the boycott, recognized that its net effect was beneficial. The increase in fees would attract more CJA lawyers, enabling them to reduce their caseloads and provide better representation for their clients. "I see no point," he concluded, "in striving resolutely for an antitrust triumph in this sensitive area when the particular case can be disposed of on a more pragmatic basis—there was no harm done."

[15] The ALJ's pragmatic moderation found no favor with the FTC. Like the ALJ, the FTC rejected each of respondents' defenses. It held that their "coercive, concerted refusal to deal" had the "purpose and effect of raising prices" and was illegal *per se.* Unlike the ALJ, the FTC refused to conclude that the boycott was harmless, noting that the "boycott forced the city government to increase the CJA fees from a level that had been sufficient to obtain an adequate supply of CJA lawyers to a level satisfactory to the respondents. The city must, as a result of the boycott, spend an additional $4 million to $5 million a year to obtain legal services for indigents. We find that these are substantial anticompetitive effects resulting from the respondents' conduct." Finally, the FTC determined that the record did not support the ALJ's conclusion that the District supported the boycott. The FTC also held that such support would not in any event excuse respondents' antitrust violations. Accordingly, it entered a cease-and-desist order "to prohibit the respondents from initiating another boycott . . . whenever they become dissatisfied with the results or pace of the city's legislative process."

[16] The Court of Appeals vacated the FTC order and remanded for a determination whether respondents possessed "significant market power." The court began its analysis by recognizing that absent any special First Amendment protection, the boycott "constituted a classic restraint of trade within the meaning of Section 1 of the Sherman Act." The Court of Appeals was not persuaded by respondents' reliance on *Claiborne Hardware* or *Noerr*, or by their argument that the boycott was justified because it was designed to improve the quality of representation for indigent defendants. It concluded, however, that "the SCTLA boycott did contain an element of expression warranting First Amendment protection." It noted that boycotts have historically been used as a dramatic means of expression and that respondents intended to convey a political message to the public at large. It therefore concluded that under *United States* v. *O'Brien*, 391 U.S. 367 (1968), a restriction on this form of expression could not be justified unless it is no greater than is essential to an important governmental interest. This test, the court reasoned, could not be satisfied by the application of an otherwise appropriate *per se* rule, but instead required the enforcement agency to "prove rather than presume that the evil against which the Sherman Act is directed looms in the conduct it condemns."

[17] Because of our concern about the implications of the Court of Appeals' unique holding, we granted the FTC's petition for certiorari as well as respondents' cross-petition.

[18] We consider first the cross-petition, which contends that respondents' boycott is outside the scope of the Sherman Act or is immunized from antitrust regulation by the First Amendment. We then turn to the FTC's petition.

[19] Reasonable lawyers may differ about the wisdom of this enforcement proceeding . . . . Respondents' boycott may well have served a cause that was worthwhile and unpopular. We may assume that the pre-boycott rates were unreasonably low, and that the increase has produced better legal representation for indigent defendants. Moreover, given that neither indigent criminal defendants nor the lawyers who represent them command any special appeal with the electorate, we may also assume that without the boycott there would have been no increase in District CJA fees at least until the Congress amended the federal statute. These assumptions do not control the case, for it is not our task to pass upon the social utility or political wisdom of price-fixing agreements.

[20] As the ALJ, the FTC, and the Court of Appeals all agreed, respondents' boycott "constituted a classic restraint of trade within the meaning of Section 1 of the Sherman Act." As such, it also violated the prohibition against unfair methods of competition in § 5 of the FTC Act. Prior to the boycott CJA lawyers were in competition with one another, each deciding independently whether and how often to offer to provide services to the District at CJA rates. The agreement among the CJA lawyers was designed to obtain higher prices for their services and was implemented by a concerted refusal to serve an important customer in the market for legal services and, indeed, the only customer in the market for the particular services that CJA regulars offered. This constriction of supply is the essence of price-fixing, whether it be accomplished by agreeing upon a price, which will decrease the quantity demanded, or by agreeing upon an output, which will increase the price offered. The horizontal arrangement among these competitors was unquestionably a naked restraint on price and output.

[21] It is, of course, true that the city purchases respondents' services because it has a constitutional duty to provide representation to indigent defendants. It is likewise true that the quality of representation may improve when rates are increased. Yet neither of these facts is an acceptable justification for an otherwise unlawful restraint of trade. As we have remarked before, the "Sherman Act reflects a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services." *National Society of Professional Engineers* v. *United States*, 435 U.S. 679, 695 (1978) . . . .

[22] The social justifications proffered for respondents' restraint of trade thus do not make it any less unlawful. The statutory policy underlying the Sherman Act "precludes inquiry into the question whether competition is good or bad." . . . .

[23] Our decision in *Noerr* in no way detracts from this conclusion. In *Noerr*, we "considered whether the Sherman Act prohibited a publicity campaign waged by railroads" and "designed to foster the adoption of laws destructive of the trucking business, to create an atmosphere of distaste for truckers among the general public, and to impair the relationships existing between truckers and their customers." Interpreting the Sherman Act in the light of the First Amendment's Petition Clause, the Court noted that "at least insofar as the railroads' campaign was directed toward obtaining governmental action, its legality was not at all affected by any anticompetitive purpose it may have had."

[24] It of course remains true that "no violation of the Act can be predicated upon mere attempts to influence the passage or enforcement of laws," even if the defendants' sole purpose is to impose a restraint upon the trade of their competitors. But in the *Noerr* case the alleged restraint of trade was the intended *consequence* of public action; in this case the boycott was the *means* by which respondents sought to obtain favorable legislation. The restraint of trade that was implemented while the boycott lasted would have had precisely the same anticompetitive consequences during that period even if no legislation had been enacted. In *Noerr*, the desired legislation would have created the restraint on the truckers' competition; in this case the emergency legislative response to the boycott put an end to the restraint. [. . .]

[25] SCTLA argues that if its conduct would otherwise be prohibited by the Sherman Act and the Federal Trade Commission Act, it is nonetheless protected by the First Amendment rights recognized in *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886 (1982). That case arose after black citizens boycotted white merchants in Claiborne County, Mississippi. The white merchants sued under state law to recover losses from the boycott. We found that the "right of the States to regulate economic activity could not justify a complete prohibition against a nonviolent, politically motivated boycott designed to force governmental and economic

change and to effectuate rights guaranteed by the Constitution itself." We accordingly held that "the nonviolent elements of petitioners' activities are entitled to the protection of the First Amendment."

[26] SCTLA contends that because it, like the boycotters in *Claiborne Hardware*, sought to vindicate constitutional rights, it should enjoy a similar First Amendment protection. It is, of course, clear that the association's efforts to publicize the boycott, to explain the merits of its cause, and to lobby District officials to enact favorable legislation—like similar activities in *Claiborne Hardware*—were activities that were fully protected by the First Amendment. But nothing in the FTC's order would curtail such activities, and nothing in the FTC's reasoning condemned any of those activities.

[27] The activity that the FTC order prohibits is a concerted refusal by CJA lawyers to accept any further assignments until they receive an increase in their compensation; the undenied objective of their boycott was an economic advantage for those who agreed to participate. It is true that the *Claiborne Hardware* case also involved a boycott. That boycott, however, differs in a decisive respect. Those who joined the *Claiborne Hardware* boycott sought no special advantage for themselves. They were black citizens in Port Gibson, Mississippi, who had been the victims of political, social, and economic discrimination for many years. They sought only the equal respect and equal treatment to which they were constitutionally entitled. They struggled "to change a social order that had consistently treated them as second class citizens." As we observed, the campaign was not intended "to destroy legitimate competition." Equality and freedom are preconditions of the free market, and not commodities to be haggled over within it.

[28] The same cannot be said of attorney's fees. As we recently pointed out, our reasoning in *Claiborne Hardware* is not applicable to a boycott conducted by business competitors who "stand to profit financially from a lessening of competition in the boycotted market." No matter how altruistic the motives of respondents may have been, it is undisputed that their immediate objective was to increase the price that they would be paid for their services. Such an economic boycott is well within the category that was expressly distinguished in the *Claiborne Hardware* opinion itself. [. . .]

[29] In any event, however, we cannot accept the Court of Appeals' characterization of this boycott or the antitrust laws. Every concerted refusal to do business with a potential customer or supplier has an expressive component. At one level, the competitors must exchange their views about their objectives and the means of obtaining them. The most blatant, naked price-fixing agreement is a product of communication, but that is surely not a reason for viewing it with special solicitude. [. . .]

[30] In sum, there is thus nothing unique about the "expressive component" of respondents' boycott. A rule that requires courts to apply the antitrust laws "prudently and with sensitivity" whenever an economic boycott has an "expressive component" would create a gaping hole in the fabric of those laws. Respondents' boycott thus has no special characteristics meriting an exemption from the *per se* rules of antitrust law. [. . .]

[31] The judgment of the Court of Appeals is accordingly reversed insofar as that court held the *per se* rules inapplicable to the lawyers' boycott. The case is remanded for further proceedings consistent with this opinion.

When Is a Boycott* Per Se *Illegal?

In thinking about the tangled law of group boycotts, it may be helpful to think of two categories of case in which *per se* condemnation may be appropriate. The first category includes naked agreements among groups of competitors not to deal with trading partners (*e.g.*, customers) *except* on certain terms, such as at a supracompetitive price. This kind of boycott is just another way of thinking about naked collusion: every cartel works in this way! The second category includes naked agreements among competitors, exercising market power, not to deal with trading partners that deal with rivals of the group, without apparent procompetitive justifications.[357] This kind of boycott raises the same concerns as classical vertical exclusivity, as we shall see in

[357] *See*, *e.g.*, FTC v. Indiana Federation of Dentists, 476 U.S. 447, 458 (1986) ("[T]he per se approach has generally been limited to cases in which firms with market power boycott suppliers or customers in order to discourage them from doing business with a competitor.").

the next chapter. *Superior Court Trial Lawyers* is an example of an agreement in the first category. The second category appears to be the kind of thing the *Northwest Stationers* Court had in mind at paragraph 9 of the extract above. The first category involves collusion on terms of dealing; the second involves naked collusion to exclude non-participant rivals of the colluders. Both are generally *per se* illegal.

In a variation on the first category, we could imagine a group of competitors agreeing to restrict output in some way other than by a simple price increase. For example, competitors might agree to restrict their use of retail or other distribution channels—"boycotting" certain, perhaps discounting, sellers—especially in partnership with, or at the request of, a single downstream retailer or distributor that held, or hoped to acquire, downstream market power. That was the kind of agreement alleged in *Klor's* (although it is not clear why such an agreement was plausible in that case, given the ample other channels that remained open and the lack of reason to believe that Broadway-Hale had any chance of gaining market power). And, as we will see later in the chapter, something similar was alleged in the FTC's case against Toys R Us and in the DOJ's case against Apple and the e-book publishers.

NOTES

1) Under what circumstances is a group boycott *per se* illegal? When should it be? Do you agree with the Court's characterization in FTC v. Indiana Federation of Dentists, 476 U.S. 447, 458 (1986), that in group boycott cases "the *per se* approach has generally been limited to cases in which firms with market power boycott suppliers or customers in order to discourage them from doing business with a competitor"? Would that be a good rule?
2) Does *Northwest Stationers* hold that the existence of a possible procompetitive justification for a boycott means that the *per se* rule does not apply? If so, does that mean that there is no *per se* rule in the first place?
3) Could the collective enterprise in *Superior Court Trial Lawyers* have been described as a procompetitive one? Should it matter that the lawyers were not otherwise economically integrated outside the scope of their boycott?
4) What seems to have been going on to prompt the complaint in *Klor's*? Do you think that the allegations described by the Court would pass muster under *Twombly* today?
5) Was the Court in *Klor's* correct to find a "monopolistic tendency" in the practice in question? In what market?
6) In general, do you think the category of group boycotts (or "concerted refusals to deal") less threatening, equally threatening, or more threatening to competition than other forms of *per se* illegal conduct?
7) What kind of remedy do you think is likely to be sensible and effective in a group boycott case?
8) Do you agree that the two-part typology in the breakout box above is a helpful way to divide the cases? Is there another way to think about group boycotts that makes better sense of the cases?
9) How should courts analyze a boycott motivated by ESG concerns?

4. Hub and Spoke Conspiracies

Sometimes a horizontal agreement is implemented through a set of vertical interactions, in what is known as a "hub and spoke conspiracy." In a traditional horizontal conspiracy, of course, the competitors directly agree on price: for example, competing retailers might get together and fix prices or other terms of dealing. In a hub-and-spoke conspiracy, however, the conspirators (the "spokes") do not directly coordinate with one another: instead, the means of coordination is through parallel agreements with a central facilitator (the "hub"), which acts as a go-between and facilitates a conscious commitment to a common scheme among the spokes.

This is an important analytical insight, because it means that under some circumstances courts will pierce through the fact that interactions seem to be formally vertical, in order to conclude that the agreement in question was "really" horizontal. This, in turn, may result in the applicability of the *per se* rule.

Two famous antitrust cases illustrate how this can work in practice. In *Toys R Us*, a downstream retailer, unhappy with competition from "warehouse club" stores, served as an intermediary to facilitate an agreement among various toy manufacturers, each of whom was willing to restrict sales to the discounting warehouse stores on the condition that other manufacturers did the same. In *Apple*, competing e-book publishers, unhappy with

competitive pressure resulting from aggressive discounting by Amazon, entered into parallel vertical agreements with Apple regarding the terms on which their respective e-books could be distributed, as part of an implicit agreement to switch to a higher-priced sale model.

In both cases, the court held, the relevant agreement was *horizontal* in substance and that *per se* treatment was appropriate, even though a noncompetitor served as an intermediary. The court also held that the noncompetitor hub was liable on the same terms with as the participating direct competitors.

Note that the *Toys R Us* case also touches on an issue we discussed in Chapter IV: the nature and cogency of evidence required before an agreement can be inferred. Why might this be a particularly complex issue in hub-and-spoke cases? The *Toys R Us* court draws a thoughtful parallel to the facts of *Interstate Circuit*, a case summarized in Chapter IV.[358]

Toys "R" Us, Inc. v. FTC

221 F.3d 928 (7th Cir. 2000)

Judge Wood.

[1] What happened in this case, according to the Commission, was fairly simple. For a long time, [Toys R Us, a/k/a] TRU had enjoyed a strong position at the low price end for toy sales, because its only competition came from traditional toy stores who could not or did not wish to meet its prices, or from general discounters like Wal-Mart or K-Mart, which could not offer anything like the variety of items TRU had and whose prices were not too far off TRU's mark.

[2] The advent of the warehouse clubs changed all that. They were a retail innovation of the late 1970s: the first one opened in 1976, and by 1992 there were some 600 individual club stores around the country. Rather than earning all of their money from their mark-up on products, the clubs sell only to their members, and they charge a modest annual membership fee, often about $30. As the word "warehouse" in the name suggests, the clubs emphasize price competition over service amenities. Nevertheless, the Commission found that the clubs seek to offer name-brand merchandise, including toys. During the late 1980s and early 1990s, warehouse clubs selected and purchased from the toy manufacturers' full array of products, just like everyone else. In some instances they bought specialized packs assembled for the "club" trade, but they normally preferred stocking conventional products so that their customers could readily compare the price of an item at the club against the price of the same item at a competing store.

[3] To the extent this strategy was successful, however, TRU did not welcome it. By 1989, its senior executives were concerned that the clubs were a threat to TRU's low-price image and, more importantly, to its profits. A little legwork revealed that as of that year the clubs carried approximately 120–240 items in direct competition with TRU, priced as much as 25 to 30% below TRU's own price levels.

[4] TRU put its President of Merchandising, a Mr. Goddu, to work to see what could be done. The response Goddu and other TRU executives formulated to beat back the challenge from the clubs began with TRU's decision to contact some of its suppliers, including toy manufacturing heavyweights Mattel, Hasbro, and Fisher Price. At the Toy Fair in 1992 (a major event at which the next Christmas season's orders are placed), Goddu informed the manufacturers of a new TRU policy, which was reflected in a memo of January 29, 1992. The policy set forth the following conditions and privileges for TRU:

- The clubs could have no new or promoted product unless they carried the entire line.
- All specials and exclusives to be sold to the clubs had to be shown first to TRU to see if TRU wanted the item.
- Old and basic product had to be in special packs.

[358] *See supra* § IV.B.2.

• Clearance and closeout items were permissible provided that TRU was given the first opportunity to buy the product.

• There would be no discussion about prices.

[5] TRU was careful to meet individually with each of its suppliers to explain its new policy. Afterwards, it then asked each one what it intended to do. Negotiations between TRU and the manufacturers followed, as a result of which each manufacturer eventually agreed that it would sell to the clubs only highly differentiated products (either unique individual items or combo packs) that were not offered to anything but a club (and thus of course not to TRU). As the Commission put it, "[t]hrough its announced policy and the related agreements discussed below, TRU sought to eliminate the competitive threat the clubs posed by denying them merchandise, forcing the clubs' customers to buy products they did not want, and frustrating customers' ability to make direct price comparisons of club prices and TRU prices."

[6] The agreements between TRU and the various manufacturers were, of course, vertical agreements, because they ran individually from the supplier/manufacturer to the purchaser/retailer. The Commission found that TRU reached about 10 of these agreements. After the agreements were concluded, TRU then supervised and enforced each toy company's compliance with its commitment.

[7] But TRU was not content to stop with vertical agreements. Instead, the Commission found, it decided to go further. It worked for over a year and a half to put the vertical agreements in place, but the biggest hindrance TRU had to overcome was the major toy companies' reluctance to give up a new, fast-growing, and profitable channel of distribution. The manufacturers were also concerned that any of their rivals who broke ranks and sold to the clubs might gain sales at their expense, given the widespread and increasing popularity of the club format. To address this problem, the Commission found, TRU orchestrated a horizontal agreement among its key suppliers to boycott the clubs. The evidence on which the Commission relied showed that, at a minimum, Mattel, Hasbro, Fisher Price, Tyco, Little Tikes, Today's Kids, and Tiger Electronics agreed to join in the boycott on the condition that their competitors would do the same.

[8] The Commission first noted that internal documents from the manufacturers revealed that they were trying to expand, not to restrict, the number of their major retail outlets and to reduce their dependence on TRU. They were specifically interested in cultivating a relationship with the warehouse clubs and increasing sales there. Thus, the sudden adoption of measures under which they decreased sales to the clubs ran against their independent economic self-interest. Second, the Commission cited evidence that the manufacturers were unwilling to limit sales to the clubs without assurances that their competitors would do likewise. Goddu himself testified that TRU communicated the message "I'll stop if they stop" from manufacturer to competing manufacturer. He specifically mentioned having such conversations with Mattel and Hasbro, and he said more generally "We communicated to our vendors that we were communicating with all our key suppliers, and we did that I believe at Toy Fair 1992. We made a point to tell each of the vendors that we spoke to that we would be talking to our other key suppliers."

[9] Evidence from the manufacturers corroborated Goddu's account. A Mattel executive said that it would not sell the clubs the same items it was selling to TRU, and that this decision was "based on the fact that competition would do the same." A Hasbro executive said much the same thing: "because our competitors had agreed not to sell loaded [that is, promoted] product to the clubs, that we would go along with this." TRU went so far as to assure individual manufacturers that no one would be singled out.

[10] Once the special warehouse club policy (or, in the Commission's more pejorative language, boycott) was underway, TRU served as the central clearinghouse for complaints about breaches in the agreement. The Commission gave numerous examples of this conduct in its opinion.

[11] Last, the Commission found that TRU's policies had bite. In the year before the boycott began, the clubs' share of all toy sales in the United States grew from 1.5% in 1991 to 1.9% in 1992. After the boycott took hold, that percentage slipped back by 1995 to 1.4%. Local numbers were more impressive. Costco, for example, experienced overall growth on sales of all products during the period 1991 to 1993 of 25%. Its toy sales increased during same period by 51%. But, after the boycott took hold in 1993, its toy sales decreased by 1.6%

even while its overall sales were still growing by 19.5%. The evidence indicated that this was because TRU had succeeded in cutting off its access to the popular toys it needed. In 1989, over 90% of the Mattel toys Costco and other clubs purchased were regular (i.e. easily comparable) items, but by 1993 that percentage was zero. Once again, the Commission's opinion is chock full of similar statistics.

[12] The Commission also considered the question whether TRU might have been trying to protect itself against free riding, at least with respect to its vertical agreements. It acknowledged that TRU provided several services that might be important to consumers, including advertising, carrying an inventory of goods early in the year, and supporting a full line of products. Nevertheless, it found that the manufacturers compensated TRU directly for advertising toys, storing toys made early in the year, and stocking a broad line of each manufacturer's toys under one roof. A 1993 TRU memorandum confirms that advertising is manufacturer-funded and is "essentially free." In 1994, TRU's net cost of advertising was a tiny 0.02% of sales, or $750,000, out of a total of $199 million it spent on advertising that year. As the Commission saw it, "advertising was a service the toy manufacturers provided for TRU and not the other way around." TRU records also showed that manufacturers routinely paid TRU credits for warehousing services, and that they compensated it for full line stocking. In short, the Commission found, there was no evidence that club competition without comparable services threatened to drive TRU services out of the market or to harm customers. Manufacturers paid each retailer directly for the services they wanted the retailer to furnish.

[13] Based on this record, the Commission drew three central conclusions of law: (1) the TRU-led manufacturer boycott of the warehouse clubs was illegal per se under the rule enunciated in *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.*, 472 U.S. 284 (1985); (2) the boycott was illegal under a full rule of reason analysis because its anticompetitive effects "clearly outweighed any possible business justification"; and (3) the vertical agreements between TRU and the individual toy manufacturers, "entered into seriatim with clear anticompetitive effect, violate section 1 of the Sherman Act." These antitrust violations in turn were enough to prove a violation of FTC Act § 5, which for present purposes tracks the prohibitions of the Sherman and Clayton Acts. [. . .]

[14] As TRU correctly points out, the critical question here is whether substantial evidence supported the Commission's finding that there was a horizontal agreement among the toy manufacturers, with TRU in the center as the ringmaster, to boycott . . . warehouse clubs [which competed with TRU in selling toys]. It acknowledges that such an agreement may be proved by either direct or circumstantial evidence . . . . When circumstantial evidence is used, there must be some evidence that tends to exclude the possibility that the alleged conspirators acted independently. This does not mean, however, that the Commission had to exclude all possibility that the manufacturers acted independently. . . . [T]hat would amount to an absurd and legally unfounded burden to prove with 100% certainty that an antitrust violation occurred. The test states only that there must be some evidence which, if believed, would support a finding of concerted behavior. In the context of an appeal from the Commission, the question is whether substantial evidence supports its conclusion that it is more likely than not that the manufacturers acted collusively.

[15] In TRU's opinion, this record shows nothing more than a series of separate, similar vertical agreements between itself and various toy manufacturers. It believes that each manufacturer in its independent self-interest had an incentive to limit sales to the clubs, because TRU's policy provided strong unilateral incentives for the manufacturer to reduce its sales to the clubs. Why gain a few sales at the clubs, it asks, when it would have much more to gain by maintaining a good relationship with the 100-pound gorilla of the industry, TRU, and make far more sales?

[16] We do not disagree that there was some evidence in the record that would bear TRU's interpretation. But that is not the standard we apply when we review decisions of the Federal Trade Commission. Instead, we apply the substantial evidence test . . . .

[17] The Commission's theory, stripped to its essentials, is that this case is a modern equivalent of the old *Interstate Circuit* decision [*i.e.*, Interstate Circuit, Inc. v. United States, 306 US 208 (1939)]. {*Eds.: As noted above, this case is summarized in Chapter IV.*} That case too involved actors at two levels of the distribution chain, distributors of motion pictures and exhibitors. Interstate Circuit was one of the exhibitors; it had a stranglehold on the

exhibition of movies in a number of Texas cities. The antitrust violation occurred when Interstate's manager, O'Donnell, sent an identical letter to the eight branch managers of the distributor companies, with each letter naming all eight as addressees, in which he asked them to comply with two demands: a minimum price for first-run theaters, and a policy against double features at night. The trial court there drew an inference of agreement from the nature of the proposals, from the manner in which they were made, from the substantial unanimity of action taken, and from the lack of evidence of a benign motive; the Supreme Court affirmed. The new policies represented a radical shift from the industry's prior business practices, and the Court rejected as beyond the range of probability that such unanimity of action was explainable only by chance.

[18] The Commission is right. Indeed, as it argues in its brief, the TRU case if anything presents a more compelling case for inferring horizontal agreement than did *Interstate Circuit*, because not only was the manufacturers' decision to stop dealing with the warehouse clubs an abrupt shift from the past, and not only is it suspicious for a manufacturer to deprive itself of a profitable sales outlet, but the record here included the direct evidence of communications that was missing in *Interstate Circuit*. Just as in *Interstate Circuit*, TRU tries to avoid this result by hypothesizing independent motives. If there were no evidence in the record tending to support concerted behavior, then we agree that *Matsushita* would require a ruling in TRU's favor. But there is. The evidence showed that the companies wanted to diversify from TRU, not to become more dependent upon it; it showed that each manufacturer was afraid to curb its sales to the warehouse clubs alone, because it was afraid its rivals would cheat and gain a special advantage in that popular new market niche. The Commission was not required to disbelieve the testimony of the different toy company executives and TRU itself to the effect that the only condition on which each toy manufacturer would agree to TRU's demands was if it could be sure its competitors were doing the same thing.

[19] That is a horizontal agreement. . . . [I]t has nothing to do with enhancing efficiencies of distribution from the manufacturer's point of view. The typical story of a legitimate vertical transaction would have the manufacturer going to TRU and asking it to be the exclusive carrier of the manufacturer's goods; in exchange for that exclusivity, the manufacturer would hope to receive more effective promotion of its goods, and TRU would have a large enough profit margin to do the job well. But not all manufacturers think that exclusive dealing arrangements will maximize their profits. Some think, and are entitled to think, that using the greatest number of retailers possible is a better strategy. These manufacturers were in effect being asked by TRU to reduce their output (especially of the popular toys), and as is classically true in such cartels, they were willing to do so only if TRU could protect them against cheaters.

[20] *Northwest Stationers* also demonstrates why the facts the Commission found support its conclusion that the essence of the agreement network TRU supervised was horizontal. There the Court described the cases that had condemned boycotts as "per se" illegal as those involving joint efforts by a firm or firms to disadvantage competitors by either directly denying or persuading or coercing suppliers or customers to deny relationships the competitors need in the competitive struggle. The boycotters had to have some market power, though the Court did not suggest that the level had to be as high as it would require in a case under Sherman Act § 2. Here, TRU was trying to disadvantage the warehouse clubs, its competitors, by coercing suppliers to deny the clubs the products they needed. It accomplished this goal by inducing the suppliers to collude, rather than to compete independently for shelf space in the different toy retail stores.

United States v. Apple, Inc.

791 F.3d 290 (2d Cir. 2015)

Judge Livingston.

{*Eds.: Amazon, which operated an e-commerce website, sold e-books for use on its Kindle e-reader that were published by (among others) the "Big Six" book publishers: Hachette, HarperCollins, Penguin, RandomHouse, Macmillan, and Simon & Schuster. These e-books were sold through a "wholesale" model: the publisher set a "wholesale price" that Amazon paid to the publisher for each e-book sold to a consumer. Publishers charged higher wholesale prices for new releases and New York Times bestsellers, reflecting their higher print book prices for those desirable titles. But Amazon refused to charge a premium to its customers for these books: it set*

the retail price at the low point of $9.99—near, or even below, the wholesale price of those e-books. This strategy caused the publishers concern, as the court explains.}

[1] [T]op executives in the Big Six [book publishers: *i.e.*, Hachette, HarperCollins, Penguin, RandomHouse, Macmillan, and Simon & Schuster] saw Amazon's $9.99 pricing strategy as a threat to their established way of doing business. . . . In the short term, these members of the Big Six thought that Amazon's lower-priced ebooks would make it more difficult for them to sell hardcover copies of new releases, which were often priced, as the district court noted, at thirty dollars or more, as well as New York Times bestsellers. Further down the road, the publishers feared that consumers would become accustomed to the uniform $9.99 price point for these ebooks, permanently driving down the price they could charge for print versions of the books. Moreover, if Amazon became powerful enough, it could demand lower wholesale prices from the Big Six or allow authors to publish directly with Amazon, cutting out the publishers entirely. As Hachette's [CEO] put it, the idea of the "wretched $9.99 price point becoming a de facto standard" for ebooks "sickened" him. [. . .]

[2] [Apple, which was planning to enter the market for ebook retail by introducing the iBookstore,] learned that the publishers feared that Amazon's pricing model could change their industry, that several publishers had engaged in simultaneous windowing efforts to thwart Amazon, and that the industry as a whole was in a state of turmoil. "Apple understood," as the district court put it, "that the Publishers wanted to pressure Amazon to raise the $9.99 price point for e-books, that the Publishers were searching for ways to do that, and that they were willing to coordinate their efforts to achieve that goal." [. . .]

[3] [Apple felt that it would be unable to negotiate wholesale prices that were low enough to allow it to compete with Amazon. Accordingly, Apple proposed the "agency" model to publishers, pursuant to which] the publisher sets the price that consumers will pay for each ebook. Then, rather than the retailer paying the publisher for each ebook that it sells, the publisher pays the retailer a fixed percentage of each sale. In essence, the retailer receives a commission for distributing the publisher's ebooks. Under the system Apple devised, publishers would have the freedom to set ebook prices in the iBookstore, and would keep 70% of each sale. The remaining 30% would go to Apple as a commission.

[4] This switch to an agency model obviated Apple's concerns about negotiating wholesale prices with the Big Six while ensuring that Apple profited on every sale. It did not, however, solve all of the company's problems. Because the agency model handed the publishers control over pricing, it created the risk that the Big Six would sell ebooks in the iBookstore at far higher prices than Kindle's $9.99 offering. If the prices were too high, Apple could be left with a brand new marketplace brimming with titles, but devoid of customers.

[5] To solve this pricing problem, [Apple] initially devised two strategies. First, they realized that they could maintain "realistic prices" by establishing price caps for different types of books. Of course, these caps would need to be higher than Amazon's $9.99 price point, or Apple would face the same difficult price negotiations that it sought to avoid by switching away from the wholesale model. But at this point Apple was not content to open its iBookstore offering prices higher than the competition. For as the district court found, if the Publisher Defendants wanted to end Amazon's $9.99 pricing, Apple similarly desired that there be no price competition at the retail level.

[6] Apple next concluded, then, as the district court found, that to ensure that the iBookstore would be competitive at higher prices, Apple needed to eliminate all retail price competition. Thus, rather than simply agreeing to price caps above Amazon's $9.99 price point, Apple created a second requirement: publishers must switch all of their other ebook retailers—including Amazon—to an agency pricing model. The result would be that Apple would not need to compete with Amazon on price, and publishers would be able to eliminate Amazon's $9.99 pricing. Or, as Cue would later describe the plan to executives at Simon & Schuster, Macmillan, and Random House, the plan solved the Amazon issue by allowing the publishers to wrest control over pricing from Amazon.

[7] On January 4 and 5, Apple sent essentially identical emails to each member of the Big Six to explain its agency model proposal. Each email described the commission split between Apple and the publishers and recommended three price caps: $14.99 for hardcover books with list prices above $35; $12.99 for hardcover

books with list prices below $35; and $9.99 for all other trade books. The emails also explained that, to sell ebooks at realistic prices all other resellers of new titles need to be in [the] agency model" as well. Or, as [Apple] told [the CEO of Simon & Schuster], "all publishers" would need to move "all retailers" to an agency model. [. . .]

[8] [Rather than explicitly insert contractual clauses that obliged publishers to change their contractual relationships with other retailers such as Amazon, Apple] devised an alternative to explicitly requiring publishers to switch other retailers to agency. This alternative involved the use of a "most-favored nation" clause ("MFN Clause" or "MFN"). In general, an MFN Clause is a contractual provision that requires one party to give the other the best terms that it makes available to any competitor. In the context of Apple's negotiations, the MFN Clause mandated that, "if, for any particular New Release in hardcover format, the Customer Price in the iBookstore at any time is or becomes higher than a customer price offered by any other reseller, then the Publisher shall designate a new, lower Customer Price in the iBookstore to meet such lower customer price." Put differently, the MFN would require the publisher to offer any ebook in Apple's iBookstore for no more than what the same ebook was offered elsewhere, such as from Amazon.

[9] On January 11, Apple sent each of the Big Six a proposed eBook Agency Distribution Agreement (the "Contracts"). As described in the January 4 and 5 emails, these Contracts would split the proceeds from each ebook sale between the publisher and Apple, with the publisher receiving 70%, and would set price caps on ebooks at $14.99, $12.99, and $9.99 depending on the book's hardcover price. But unlike the initial emails, the Contracts contained MFN Clauses in place of the requirement that publishers move all other retailers to an agency model. Apple then assured each member of the Big Six that it was being offered the same terms as the others.

[10] The Big Six understood the economic incentives that the MFN Clause created. Suppose a new hardcover release sells at a list price of $25, and a wholesale price of $12.50. With Amazon, the publishers had been receiving the wholesale price (or a slightly lower digital wholesale price) for every ebook copy of the volume sold on Kindle, even if Amazon ultimately sold the ebook for less than that wholesale price. Under Apple's initial agency model—with price caps but no MFN Clause—the publishers already stood to make less money per ebook with Apple. Because Apple capped the ebook price of a $25 hardcover at $12.99 and took 30% of that price, publishers could only expect to make $8.75 per sale. But what the publishers sacrificed in short-term revenue, they hoped to gain in long-term stability by acquiring more control over pricing and, accordingly, the ability to protect their hardcover sales.

[11] The MFN Clause changed the situation by making it imperative, not merely desirable, that the publishers wrest control over pricing from ebook retailers generally. Under the MFN, if Amazon stayed at a wholesale model and continued to sell ebooks at $9.99, the publishers would be forced to sell in the iBookstore, too, at that same $9.99 price point. The result would be the worst of both worlds: lower short-term revenue and no control over pricing. The publishers recognized that, as a practical matter, this meant that the MFN Clause would force them to move Amazon to an agency relationship. As [the CEO of Simon & Schuster] put it, her company would need to move all its other ebook retailers to agency unless we wanted to make even less money in this growing market. This situation also gave each of the publishers a stake in Apple's quest to have a critical mass of publishers join the iBookstore because, "while no one Publisher could effect an industry-wide shift in prices or change the public's perception of a book's value, if they moved together they could."

[12] Apple understood this dynamic as well. As the district court found, Apple did not change its thinking when it replaced the explicit requirement that the publishers move other retailers to an agency model with the MFN. Indeed, in the following weeks, Apple assiduously worked to make sure that the shift to agency occurred. But Apple also understood that . . . "any decent MFN forces the model" away from wholesale and to agency. Or as the district court found, the MFN protected Apple from retail price competition as it punished a Publisher if it failed to impose agency terms on other e-tailers.

[13] Thus, the terms of the negotiation between Apple and the publishers became clear: Apple wanted quick and successful entry into the ebook market and to eliminate retail price competition with Amazon. In exchange, it offered the publishers an opportunity to confront Amazon as one of an organized group united in an effort to

eradicate the $9.99 price point. Both sides needed a critical mass of publishers to achieve their goals. The MFN played a pivotal role in this quid pro quo by stiffening the spines of the publishers to ensure that they would demand new terms from Amazon, and protecting Apple from retail price competition. [. . .]

[14] By the January 27 iPad launch, five of the Big Six—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster—had agreed to participate in the iBookstore. The lone holdout, Random House, did not join because its executives believed it would fare better under a wholesale pricing model and were unwilling to make a complete switch to agency pricing. [. . .]

[15] Apple portrays its Contracts with the Publisher Defendants as, at worst, "unwittingly facilitat[ing]" their joint conduct. All Apple did, it claims, was attempt to enter the market on profitable terms by offering contractual provisions—an agency model, the MFN Clause, and tiered price caps—which ensured the company a small profit on each ebook sale and insulated it from retail price competition. This had the effect of raising prices because it created an incentive for the Publisher Defendants to demand that Amazon adopt an agency model and to seize control over consumer-facing ebook prices industry-wide. But although Apple knew that its contractual terms would entice the Publisher Defendants (who wanted to do away with Amazon's $9.99 pricing) to seek control over prices from Amazon and other ebook retailers, Apple's success in capitalizing on the Publisher Defendants' preexisting incentives, it contends, does not suggest that it joined a conspiracy among the Publisher Defendants to raise prices. In sum, Apple's basic argument is that because its Contracts with the Publisher Defendants were fully consistent with its independent business interests, those agreements provide only "ambiguous" evidence of a § 1 conspiracy, and the district court therefore erred under Matsushita and Monsanto in inferring such a conspiracy.

[16] We disagree. At the start, Apple's benign portrayal of its Contracts with the Publisher Defendants is not persuasive—not because those Contracts themselves were independently unlawful, but because, in context, they provide strong evidence that Apple consciously orchestrated a conspiracy among the Publisher Defendants. As explained below, and as the district court concluded, Apple understood that its proposed Contracts were attractive to the Publisher Defendants only if they collectively shifted their relationships with Amazon to an agency model—which Apple knew would result in higher consumer-facing ebook prices. In addition to these Contracts, moreover, ample additional evidence identified by the district court established both that the Publisher Defendants' shifting to an agency model with Amazon was the result of express collusion among them and that Apple consciously played a key role in organizing that collusion. The district court did not err in concluding that Apple was more than an innocent bystander.

[17] Apple offered each Big Six publisher a proposed Contract that would be attractive only if the publishers acted collectively. Under Apple's proposed agency model, the publishers stood to make less money per sale than under their wholesale agreements with Amazon, but the Publisher Defendants were willing to stomach this loss because the model allowed them to sell new releases and bestsellers for more than $9.99. Because of the MFN Clause, however, each new release and bestseller sold in the iBookstore would cost only $9.99 as long as Amazon continued to sell ebooks at that price. So in order to receive the perceived benefit of Apple's proposed Contracts, the Publisher Defendants had to switch Amazon to an agency model as well—something no individual publisher had sufficient leverage to do on its own. Thus, each Publisher Defendant would be able to accomplish the shift to agency—and therefore have an incentive to sign Apple's proposed Contracts—only if it acted in tandem with its competitors. By the very act of signing a Contract with Apple containing an MFN Clause, then, each of the Publisher Defendants signaled a clear commitment to move against Amazon, thereby facilitating their collective action. As the district court explained, the MFNs "stiffened the spines" of the Publisher Defendants.

[18] As a sophisticated negotiator, Apple was fully aware that its proposed Contracts would entice a critical mass of publishers only if these publishers perceived an opportunity collectively to shift Amazon to agency. In fact, this was the very purpose of the MFN, which Apple's [employee] devised as an elegant alternative to a provision that would have explicitly required the publishers to adopt an agency model with other retailers. As [another Apple employee] put it, the MFN "force[d] the model" from wholesale to agency. Indeed, the MFN's capacity for forcing collective action by the publishers was precisely what enabled [CEO Steve] Jobs to predict with confidence that "the price will be the same" on the iBookstore and the Kindle when he announced the launch of the iPad—the same, Jobs said, because the publishers would make Amazon "sign agency contract[s]" by

threatening to withhold their ebooks. Apple was also fully aware that once the Publisher Defendants seized control over consumer-facing ebook prices, those prices would rise. It knew from the outset that the publishers hated Amazon's $9.99 price point, and it put price caps in its agreements because it specifically anticipated that once the publishers gained control over prices, they would push them higher than $9.99, higher than Apple itself deemed "realistic."

[19] On appeal, Apple nonetheless defends the Contracts that it proposed to the publishers as an "aikido move" that shrewdly leveraged market conditions to its own advantage. "Aikido move" or not, the attractiveness of Apple's offer to the Publisher Defendants hinged on whether it could successfully help organize them to force Amazon to an agency model and then to use their newfound collective control to raise ebook prices. The Supreme Court has defined an agreement for Sherman Act § 1 purposes as a conscious commitment to a common scheme designed to achieve an unlawful objective. Plainly, this use of the promise of higher prices as a bargaining chip to induce the Publisher Defendants to participate in the iBookstore constituted a conscious commitment to the goal of raising ebook prices. "Antitrust law has never required identical motives among conspirators" when their independent reasons for joining together lead to collusive action. Put differently, "independent reasons" can also be "interdependent," and the fact that Apple's conduct was in its own economic interest in no way undermines the inference that it entered an agreement to raise ebook prices.

[20] Nor was the Publisher Defendants' joint action against Amazon a result of parallel decisionmaking. As we have explained, conduct resulting solely from competitors' independent business decisions—and not from any "agreement"—is not unlawful under § 1 of the Sherman Act, even if it is anticompetitive. But to generate a permissible inference of agreement, a plaintiff need only present sufficient evidence that such agreement conclude that it was not equally likely that the near-simultaneous signing of Apple's Contracts by multiple publishers—which led to all of the Publisher Defendants moving against Amazon—resulted from the parties' independent decisions, as opposed to a meeting of the minds. That the Publisher Defendants were in constant communication regarding their negotiations with both Apple and Amazon can hardly be disputed. Indeed, Apple never seriously argues that the Publisher Defendants were not acting in concert.

[21] Even so, Apple claims, it cannot have organized the conspiracy among the Publisher Defendants if it merely unwittingly facilitated their joint conduct. But this argument founders—and dramatically so—on the factual findings of the district court. As the district court explained, Apple's Contracts with the publishers must be considered in the context of the entire record. Even if Apple was unaware of the extent of the Publisher Defendants' coordination when it first approached them, its subsequent communications with them as negotiations progressed show that Apple consciously played a key role in organizing their express collusion. From the outset, [Apple] told the publishers that Apple would launch its iBookstore only if a sufficient number of them agreed to participate and that each publisher would receive identical terms, assuring them that a critical mass of major publishers would be prepared to move against Amazon. Later on, [Apple] kept the publishers updated about how many of their peers signed Apple's Contracts, and reminded them that it was offering "the best chance for publishers to challenge the 9.99 price point" before it became "cemented" in "consumer expectations." When time ran short, Apple coordinated phone calls between the publishers who had agreed and those who remained on the fence. As Cue said at trial, Apple endeavored to "assure the publishers that they weren't going to be alone, so that Apple would take the fear away of the Amazon retribution that they were all afraid of." [. . .]

[22] In short, we have no difficulty on this record rejecting Apple's argument that the district court erred in concluding that Apple conspired with the Publisher Defendants to eliminate retail price competition and to raise e-book prices. . . . .

[23] By agreeing to orchestrate a horizontal price-fixing conspiracy, Apple committed itself to achieving that unlawful objective: namely, collusion with and among the Publisher Defendants to set ebook prices. This type of agreement, moreover, is a restraint that would always or almost always tend to restrict competition and decrease output.

[24] The response, raised by Apple . . . that Apple engaged in "vertical conduct" that is unfit for per se condemnation therefore misconstrues the Sherman Act analysis. It is the type of restraint Apple agreed to

impose that determines whether the per se rule or the rule of reason is appropriate. These rules are means of evaluating whether a restraint is unreasonable, not the reasonableness of a particular defendant's role in the scheme.

[25] Consistent with this principle, the Supreme Court and our Sister Circuits have held all participants in "hub-and-spoke" conspiracies liable when the objective of the conspiracy was a per se unreasonable restraint of trade. In *Klor's, Inc. v. Broadway–Hale Stores, Inc.*, for example, the Supreme Court considered whether a prominent retailer of electronic appliances could be held liable under § 1 of the Sherman Act for fostering an agreement with and among its distributors to have those companies boycott a competing retailer. The Court characterized this arrangement as a "group boycott" supported by a wide combination consisting of manufacturers, distributors and a retailer. It then decided that, if the combination were proved at trial, holding the retailer liable would be appropriate because group boycotts, or concerted refusals by traders to deal with other traders, are per se unreasonable restraints of trade. [. . .]

[26] Because the reasonableness of a restraint turns on its anticompetitive effects, and not the identity of each actor who participates in imposing it, Apple and the dissent's observation that the Supreme Court has refused to apply the *per se* rule to certain vertical agreements is inapposite. The rule of reason is unquestionably appropriate to analyze an agreement between a manufacturer and its distributors to, for instance, limit the price at which the distributors sell the manufacturer's goods or the locations at which they sell them. These vertical restrictions are widely used in our free market economy, can enhance interbrand competition, and do not inevitably have a pernicious effect on competition. But the relevant agreement in restraint of trade in this case is not Apple's vertical Contracts with the Publisher Defendants (which might well, if challenged, have to be evaluated under the rule of reason); it is the horizontal agreement that Apple organized among the Publisher Defendants to raise ebook prices. As explained below, horizontal agreements with the purpose and effect of raising prices are per se unreasonable because they pose a threat to the central nervous system of the economy; that threat is just as significant when a vertical market participant organizes the conspiracy. Indeed, as the dissent notes, the Publisher Defendants' coordination to fix prices is uncontested on appeal. The competitive effects of that same restraint are no different merely because a different conspirator is the defendant. [. . .]

[27] In short, the relevant "agreement in restraint of trade" in this case is the price-fixing conspiracy identified by the district court, not Apple's vertical contracts with the Publisher Defendants. How the law might treat Apple's vertical agreements in the absence of a finding that Apple agreed to create the horizontal restraint is irrelevant. Instead, the question is whether the vertical organizer of a horizontal conspiracy designed to raise prices has agreed to a restraint that is any less anticompetitive than its co-conspirators, and can therefore escape per se liability. We think not.

NOTES

1) Could Toys R Us have unilaterally announced that it would not deal with any manufacturer that was selling to warehouse clubs? If so, why was the conduct described above challenged and punished?
2) Do you agree with the Second Circuit that Apple organized a horizontal conspiracy? Or did Apple, understanding each publisher's incentives, simply act in ways designed to facilitate each publisher's unilateral decisionmaking in ways that benefited Apple? What rule or principle are you using to differentiate between those two characterizations: and what evidence in the case is critical to your view?
3) Think back to the discussion in Chapter IV on the definition of agreement. Is it fair to say that the horizontal competitors in *Toys R Us* and *Apple* satisfied that definition while participants in tacit collusion do not?
4) Was there a procompetitive justification for the conduct in either of these hub-and-spoke cases?

C. What Is Naked Collusion? The *Per Se* / Rule of Reason Boundary

When is "literal" price fixing not "antitrust" price fixing? This is one of the recurrent riddles in the string of Supreme Court cases that attempt to define the border between *per se* illegal conduct and practices that merit rule of reason analysis.

Of course, some forms of literal "price fixing" do not even get onto the radar of antitrust analysis. Some are not regarded as joint conduct at all: for example, as we saw in Chapter IV, employees and subsidiaries wholly within the bounds of the firm coordinate on price and output all the time without any suggestion of antitrust scrutiny.[359] Other forms of price fixing are specially protected by antitrust exemptions, as we shall see in Chapter X, including collective wage bargaining by unions.

But other practices that come under antitrust scrutiny may raise serious questions about whether it is appropriate to treat the behavior in question as naked collusion and apply *per se* condemnation. In this section we will meet several of these "edge cases." The unifying theme in these cases is that there is a serious question about whether what is going on should be characterized as naked collusion among competitors—that is, conduct equivalent to a price-fixing cartel—or alternatively as a collaborative effort among competitors to do something that could be procompetitive, even if it involves reducing or eliminating competition between the participants.

1. Joint Ventures and Joint Products

The antitrust analysis of cooperative ventures among rivals to find new ways to meet demand has changed significantly over the last 60 years. We begin with *Sealy* and *Topco*, two somewhat infamous older decisions that condemn as *per se* illegal practices that would almost certainly be analyzed under the rule of reason today. In *Sealy* the court held that a group of mattress manufacturers violated the Sherman Act when they jointly developed and offered "Sealy" label mattresses, because the participants had divided territories amongst themselves for the purposes of the jointly-offered Sealy mattresses only. In *Topco*, the Court condemned as *per se* illegal a cooperative enterprise between smaller supermarkets that aimed to facilitate more vigorous competition with larger rivals, involving restrictions on their dealings with the jointly-branded private label goods.

CASENOTE: United States v. Sealy, Inc.

388 U.S. 350 (1967)

In *Sealy* DOJ challenged an arrangement between manufacturers of mattresses and other bedding products that permitted smaller, regional manufacturers to build national brand recognition. The arrangement involved Sealy granting licenses to make "Sealy" products to a series of manufacturer-licensees, each of which had the exclusive right to make and sell products under the Sealy name and trademark in a particular territory. The prices of the Sealy mattresses were set collectively. The arrangement did *not* involve any limitation or agreement on each manufacturer-licensee's ability to make, sell, or price products that were not branded with the Sealy name.

Writing for the Court, Justice Fortas called this venture "flagrant and pervasive price-fixing, in obvious violation of the law." Arguments that the venture actually promoted competition were irrelevant, given the coordination on price: "It is argued . . . that a number of small grocers might allocate territory among themselves on an exclusive basis as incident to the use of a common name and common advertisements, and that this sort of venture should be welcomed in the interests of competition, and should not be condemned as per se unlawful. But condemnation of appellee's territorial arrangements certainly does not require us to go so far as to condemn that quite different situation, whatever might be the result if it were presented to us for decision. For here, the arrangements for territorial limitations are part of 'an aggregation of trade restraints' including unlawful price-

[359] Sanjukta Paul has called this the "firm exception" to a general rule against coordination. Sanjukta Paul, *Fissuring and the Firm Exception*, 82 L. & Contemp. Probs. 65 (2019); Sanjukta Paul, *On Firms*, 90 U. Chi. L. Rev. 579 (2023).

fixing and policing. Within settled doctrine, they are unlawful under s 1 of the Sherman Act without the necessity for an inquiry in each particular case as to their business or economic justification, their impact in the marketplace, or their reasonableness."

Justice Harlan dissented, but he did not argue that Sealy's project was a horizontal collaboration for which rule of reason treatment was appropriate. Instead, he argued that the arrangement was fundamentally vertical, as it was grounded in the relationships between Sealy (the licensor) and the individual manufacturer-licensees. This, he argued, was crucial: "[V]ertical restraints—that is, limitations imposed by a manufacturer on its own dealers . . . or by a licensor on his licensees—may have independent and valid business justifications. The person imposing the restraint cannot necessarily be said to be acting for anticompetitive purposes. Quite to the contrary, he can be expected to be acting to enhance the competitive position of his product vis-a-vis other brands." And vertical restraints may represent "the only practicable means a small company has for breaking into or staying in business." As such, they should be "tested by the rule of reason."

United States v. Topco Associates

405 U.S. 596 (1972)

Justice Marshall.

[1] The United States brought this action for injunctive relief against alleged violation by Topco Associates, Inc. (Topco), of § 1 of the Sherman Act . . . . Following a trial on the merits, the United States District Court for the Northern District of Illinois entered judgment for Topco, and the United States appealed directly to this Court pursuant to § 2 of the Expediting Act. We noted probable jurisdiction, and we now reverse the judgment of the District Court.

[2] Topco is a cooperative association of approximately 25 small and medium-sized regional supermarket chains that operate stores in some 33 States. Each of the member chains operates independently; there is no pooling of earnings, profits, capital, management, or advertising resources. No grocery business is conducted under the Topco name. Its basic function is to serve as a purchasing agent for its members. In this capacity, it procures and distributes to the members more than 1,000 different food and related nonfood items, most of which are distributed under brand names owned by Topco. The association does not itself own any manufacturing, processing, or warehousing facilities, and the items that it procures for members are usually shipped directly from the packer or manufacturer to the members. Payment is made either to Topco or directly to the manufacturer at a cost that is virtually the same for the members as for Topco itself.

[3] All of the stock in Topco is owned by the members, with the common stock, the only stock having voting rights, being equally distributed. The board of directors, which controls the operation of the association, is drawn from the members and is normally composed of high-ranking executive officers of member chains. It is the board that elects the association's officers and appoints committee members, and it is from the board that the principal executive officers of Topco must be drawn. Restrictions on the alienation of stock and the procedure for selecting all important officials of the association from within the ranks of its members give the members complete and unfettered control over the operations of the association.

[4] Topco was founded in the 1940's by a group of small, local grocery chains, independently owned and operated, that desired to cooperate to obtain high quality merchandise under private labels in order to compete more effectively with larger national and regional chains. . . . By 1964, Topco's members had combined retail sales of more than $2 billion; by 1967, their sales totaled more than $2.3 billion, a figure exceeded by only three national grocery chains.

[5] Members of the association vary in the degree of market share that they possess in their respective areas. The range is from 1.5% to 16%, with the average being approximately 6%. While it is difficult to compare these figures with the market shares of larger regional and national chains because of the absence in the record of accurate statistics for these chains, there is much evidence in the record that Topco members are frequently in as strong a competitive position in their respective areas as any other chain. The strength of this competitive position is due, in some measure, to the success of Topco-brand products. Although only 10% of the total goods

sold by Topco members bear the association's brand names, the profit on these goods is substantial and their very existence has improved the competitive potential of Topco members with respect to other large and powerful chains.

[6] It is apparent that from meager beginnings approximately a quarter of a century ago, Topco has developed into a purchasing association wholly owned and operated by member chains, which possess much economic muscle, individually as well as cooperatively. [. . .]

[7] The United States charged that, beginning at least as early as 1960 and continuing up to the time that the complaint was filed, Topco had combined and conspired with its members to violate § 1 in two respects. First, the Government alleged that there existed:

> a continuing agreement, understanding and concert of action among the co-conspirator member firms acting through Topco, the substantial terms of which have been and are that each co-conspirator member firm will sell Topco-controlled brands only within the marketing territory allocated to it, and will refrain from selling Topco-controlled brands outside such marketing territory.

[8] The division of marketing territories to which the complaint refers consists of a number of practices by the association.

[9] Article IX, § 2, of the Topco bylaws establishes three categories of territorial licenses that members may secure from the association:

(a) *Exclusive* — An exclusive territory is one in which the member is licensed to sell all products bearing specified trademarks of the Association, to the exclusion of all other persons.

(b) *Non-exclusive* — A non-exclusive territory is one in which a member is licensed to sell all products bearing specified trademarks of the Association, but not to the exclusion of others who may also be licensed to sell products bearing the same trademarks of the Association in the same territory.

(c) *Coextensive* — A coextensive territory is one in which two (2) or more members are licensed to sell all products bearing specified trademarks of the Association to the exclusion of all other persons. . . .

[10] When applying for membership, a chain must designate the type of license that it desires. Membership must first be approved by the board of directors, and thereafter by an affirmative vote of 75% of the association's members. If, however, the member whose operations are closest to those of the applicant, or any member whose operations are located within 100 miles of the applicant, votes against approval, an affirmative vote of 85% of the members is required for approval. Because, as indicated by the record, members cooperate in accommodating each other's wishes, the procedure for approval provides, in essence, that members have a veto of sorts over actual or potential competition in the territorial areas in which they are concerned.

[11] Following approval, each new member signs an agreement with Topco designating the territory in which that member may sell Topco-brand products. No member may sell these products outside the territory in which it is licensed. Most licenses are exclusive, and even those denominated "coextensive" or "non-exclusive" prove to be *de facto* exclusive. Exclusive territorial areas are often allocated to members who do no actual business in those areas on the theory that they may wish to expand at some indefinite future time and that expansion would likely be in the direction of the allocated territory. When combined with each member's veto power over new members, provisions for exclusivity work effectively to insulate members from competition in Topco-brand goods. Should a member violate its license agreement and sell in areas other than those in which it is licensed, its membership can be terminated under Art. IV, §§ 2(a) and 2(b) of the bylaws. Once a territory is classified as exclusive, either formally or *de facto*, it is extremely unlikely that the classification will ever be changed.

[12] The Government maintains that this scheme of dividing markets violates the Sherman Act because it operates to prohibit competition in Topco-brand products among grocery chains engaged in retail operations. The Government also makes a subsidiary challenge to Topco's practices regarding licensing members to sell at wholesale. Under the bylaws, members are not permitted to sell any products supplied by the association at wholesale, whether trademarked or not, without first applying for and receiving special permission from the

association to do so. Before permission is granted, other licenses (usually retailers), whose interests may potentially be affected by wholesale operations, are consulted as to their wishes in the matter. If permission is obtained, the member must agree to restrict the sale of Topco products to a specific geographic area and to sell under any conditions imposed by the association. Permission to wholesale has often been sought by members, only to be denied by the association. The Government contends that this amounts not only to a territorial restriction violative of the Sherman Act, but also to a restriction on customers that in itself is violative of the Act.

[13] From the inception of this lawsuit, Topco accepted as true most of the Government's allegations regarding territorial divisions and restrictions on wholesaling, although it differed greatly with the Government on the conclusions, both factual and legal, to be drawn from these facts.

[14] Topco's answer to the complaint is illustrative of its posture in the District Court and before this Court:

> Private label merchandising is a way of economic life in the food retailing industry, and exclusivity is the essence of a private label program; without exclusivity, a private label would not be private. Each national and large regional chain has its own exclusive private label products in addition to the nationally advertised brands which all chains sell. Each such chain relies upon the exclusivity of its own private label line to differentiate its private label products from those of its competitors and to attract and retain the repeat business and loyalty of consumers. Smaller retail grocery stores and chains are unable to compete effectively with the national and large regional chains without also offering their own exclusive private label products. [. . .]
>
> The only feasible method by which Topco can procure private label products and assure the exclusivity thereof is through trademark licenses specifying the territory in which each member may sell such trademarked products.

[15] Topco essentially maintains that it needs territorial divisions to compete with larger chains; that the association could not exist if the territorial divisions were anything but exclusive; and that by restricting competition in the sale of Topco-brand goods, the association actually increases competition by enabling its members to compete successfully with larger regional and national chains.

[16] The District Court, considering all these things relevant to its decision, agreed with Topco. It recognized that the panoply of restraints that Topco imposed on its members worked to prevent competition in Topco-brand products, but concluded that

> whatever anti-competitive effect these practices may have on competition in the sale of Topco private label brands is far outweighed by the increased ability of Topco members to compete both with the national chains and other supermarkets operating in their respective territories.

[17] The court held that Topco's practices were procompetitive and, therefore, consistent with the purposes of the antitrust laws. But we conclude that the District Court used an improper analysis in reaching its result. [. . .]

[18] We think that it is clear that the restraint in this case is a horizontal one, and, therefore, a *per se* violation of § 1. The District Court failed to make any determination as to whether there were *per se* horizontal territorial restraints in this case and simply applied a rule of reason in reaching its conclusions that the restraints were not illegal. In so doing, the District Court erred. *United States* v. *Sealy, Inc.*, [388 U.S. 350 (1967)] is, in fact, on all fours with this case. Sealy licensed manufacturers of mattresses and bedding to make and sell products using the Sealy trademark. Like Topco, Sealy was a corporation owned almost entirely by its licensees, who elected the Board of Directors and controlled the business. Just as in this case, Sealy agreed with the licensees not to license other manufacturers or sellers to sell Sealy-brand products in a designated territory in exchange for the promise of the licensee who sold in that territory not to expand its sales beyond the area demarcated by Sealy. The Court held that this was a horizontal territorial restraint, which was *per se* violative of the Sherman Act.[9]

[9] It is true that in *Sealy* the Court dealt with price fixing as well as territorial restrictions. To the extent that *Sealy* casts doubt on whether horizontal territorial limitations, unaccompanied by price fixing, are *per se* violations of the Sherman Act, we remove that doubt today.

[19] Whether or not we would decide this case the same way under the rule of reason used by the District Court is irrelevant to the issue before us. The fact is that courts are of limited utility in examining difficult economic problems.[10] Our inability to weigh, in any meaningful sense, destruction of competition in one sector of the economy against promotion of competition in another sector is one important reason we have formulated *per se* rules.

[20] In applying these rigid rules, the Court has consistently rejected the notion that naked restraints of trade are to be tolerated because they are well intended or because they are allegedly developed to increase competition.

[21] Antitrust laws in general, and the Sherman Act in particular, are the Magna Carta of free enterprise. They are as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms. And the freedom guaranteed each and every business, no matter how small, is the freedom to compete—to assert with vigor, imagination, devotion, and ingenuity whatever economic muscle it can muster. Implicit in such freedom is the notion that it cannot be foreclosed with respect to one sector of the economy because certain private citizens or groups believe that such foreclosure might promote greater competition in a more important sector of the economy.

[22] The District Court determined that by limiting the freedom of its individual members to compete with each other, Topco was doing a greater good by fostering competition between members and other large supermarket chains. But, the fallacy in this is that Topco has no authority under the Sherman Act to determine the respective values of competition in various sectors of the economy. On the contrary, the Sherman Act gives to each Topco member and to each prospective member the right to ascertain for itself whether or not competition with other supermarket chains is more desirable than competition in the sale of Topco-brand products. Without territorial restrictions, Topco members may indeed "cut each other's throats." But, we have never found this possibility sufficient to warrant condoning horizontal restraints of trade. [. . .]

[23] There have been tremendous departures from the notion of a free-enterprise system as it was originally conceived in this country. These departures have been the product of congressional action and the will of the people. If a decision is to be made to sacrifice competition in one portion of the economy for greater competition in another portion, this too is a decision that must be made by Congress and not by private forces or by the courts. Private forces are too keenly aware of their own interests in making such decisions and courts are ill-equipped and ill-situated for such decisionmaking. To analyze, interpret, and evaluate the myriad of competing interests and the endless data that would surely be brought to bear on such decisions, and to make the delicate judgment on the relative values to society of competitive areas of the economy, the judgment of the elected representatives of the people is required.

[24] Just as the territorial restrictions on retailing Topco-brand products must fall, so must the territorial restrictions on wholesaling. The considerations are the same, and the Sherman Act requires identical results.

[25] We also strike down Topco's other restrictions on the right of its members to wholesale goods. These restrictions amount to regulation of the customers to whom members of Topco may sell Topco-brand goods. Like territorial restrictions, limitations on customers are intended to limit intra-brand competition and to promote inter-brand competition. For the reasons previously discussed, the arena in which Topco members compete must be left to their unfettered choice absent a contrary congressional determination.

[26] We reverse the judgment of the District Court and remand the case for entry of an appropriate decree.

Justice Blackmun, concurring in the result.

[10] There has been much recent commentary on the wisdom of *per se* rules. Without the *per se* rules, businessmen would be left with little to aid them in predicting in any particular case what courts will find to be legal and illegal under the Sherman Act. Should Congress ultimately determine that predictability is unimportant in this area of the law, it can, of course, make *per se* rules inapplicable in some or all cases, and leave courts free to ramble through the wilds of economic theory in order to maintain a flexible approach.

[27] The conclusion the Court reaches has its anomalous aspects, for surely, as the District Court's findings make clear, today's decision in the Government's favor will tend to stultify Topco members' competition with the great and larger chains. The bigs, therefore, should find it easier to get bigger and, as a consequence, reality seems at odds with the public interest. The per se rule, however, now appears to be so firmly established by the Court that, at this late date, I could not oppose it. Relief, if any is to be forthcoming, apparently must be by way of legislation.

Chief Justice Burger, dissenting.

[28] This case does not involve restraints on interbrand competition or an allocation of markets by an association with monopoly or near-monopoly control of the sources of supply of one or more varieties of staple goods. Rather, we have here an agreement among several small grocery chains to join in a cooperative endeavor that, in my view, has an unquestionably lawful principal purpose; in pursuit of that purpose they have mutually agreed to certain minimal ancillary restraints that are fully reasonable in view of the principal purpose and that have never before today been held by this Court to be *per se* violations of the Sherman Act.

[29] In joining in this cooperative endeavor, these small chains did not agree to the restraints here at issue in order to make it possible for them to exploit an already established line of products through noncompetitive pricing. There was no such thing as a Topco line of products until this cooperative was formed. The restraints to which the cooperative's members have agreed deal only with the marketing of the products in the Topco line, and the only function of those restraints is to permit each member chain to establish, within its own geographical area and through its own local advertising and marketing efforts, a local consumer awareness of the trademarked family of products as that member's "private label" line. The goal sought was the enhancement of the individual members' abilities to compete, albeit to a modest degree, with the large national chains which had been successfully marketing private-label lines for several years. The sole reason for a cooperative endeavor was to make economically feasible such things as quality control, large quantity purchases at bulk prices, the development of attractively printed labels, and the ability to offer a number of different lines of trademarked products. All these things, of course, are feasible for the large national chains operating individually, but they are beyond the reach of the small operators proceeding alone.

[30] After a careful review of the economic considerations bearing upon this case, the District Court determined that "the relief which the government here seeks would not increase competition in Topco private label brands"; on the contrary, such relief "would substantially diminish competition in the supermarket field." This Court has not today determined, on the basis of an examination of the underlying economic realities, that the District Court's conclusions are incorrect. Rather, the majority holds that the District Court had no business examining Topco's practices under the "rule of reason"; it should not have sought to determine whether Topco's practices did in fact restrain trade or commerce within the meaning of § 1 of the Sherman Act; it should have found no more than that those practices involve a "horizontal division of markets" and are, by that very fact, *per se* violations of the Act.

[31] I do not believe that our prior decisions justify the result reached by the majority. Nor do I believe that a new *per se* rule should be established in disposing of this case, for the judicial convenience and ready predictability that are made possible by *per se* rules are not such overriding considerations in antitrust law as to justify their promulgation without careful prior consideration of the relevant economic realities in the light of the basic policy and goals of the Sherman Act. [. . .]

[32] I cannot agree with the Court's description of *Sealy* as being "on all fours with this case." *Sealy* does support the proposition that the restraints on the Topco licensees are horizontally imposed. Beyond that, however, *Sealy* is hardly controlling here. The territorial restrictions in *Sealy* were found by this Court to be so intimately a part of an unlawful price-fixing and policing scheme that the two arrangements fell together:

> [T]his unlawful resale price-fixing activity refutes appellee's claim that the territorial restraints were mere incidents of a lawful program of trademark licensing. The territorial restraints were a part of the unlawful price-fixing and policing.

[33] [. . .] The foregoing analysis . . . indicates to me that the Court is not merely following prior holdings; on the contrary, it is establishing a new *per se* rule. In the face of the District Court's well supported findings that the effects of such a rule in this case will be adverse to the public welfare, the Court lays down that rule without regard to the impact that the condemned practices may have on competition. In doing so, the Court virtually invites Congress to undertake to determine that impact. I question whether the Court is fulfilling the role assigned to it under the statute when it declines to make this determination; in any event, if the Court is unwilling on this record to assess the economic impact, it surely should not proceed to make a new rule to govern the economic activity. [. . .]

[34] In formulating a new *per se* rule today, the Court does not tell us what "pernicious effect on competition" the practices here outlawed are perceived to have; nor does it attempt to show that those practices "lack . . . any redeeming virtue." Rather, it emphasizes only the importance of predictability, asserting that "courts are of limited utility in examining difficult economic problems" and have not yet been left free by Congress to "ramble through the wilds of economic theory in order to maintain a flexible approach."

[35] With all respect, I believe that there are two basic fallacies in the Court's approach here. First, while I would not characterize our role under the Sherman Act as one of "rambling through the wilds," it is indeed one that requires our "examination of difficult economic problems." We can undoubtedly ease our task, but we should not abdicate that role by formulation of *per se* rules with no justification other than the enhancement of predictability and the reduction of judicial investigation. Second, from the general proposition that *per se* rules play a necessary role in antitrust law, it does not follow that the particular *per se* rule promulgated today is an appropriate one. Although it might well be desirable in a proper case for this Court to formulate a *per se* rule dealing with horizontal territorial limitations, it would not necessarily be appropriate for such a rule to amount to a blanket prohibition against all such limitations. More specifically, it is far from clear to me why such a rule should cover those division-of-market agreements that involve no price fixing and which are concerned only with trademarked products that are not in a monopoly or near-monopoly position with respect to competing brands. The instant case presents such an agreement; I would not decide it upon the basis of a *per se* rule.

[36] The District Court specifically found that the horizontal restraints involved here tend positively to promote competition in the supermarket field and to produce lower costs for the consumer. The Court seems implicitly to accept this determination, but says that the Sherman Act does not give Topco the authority to determine for itself "whether or not competition with other supermarket chains is more desirable than competition in the sale of Topco-brand products." But the majority overlooks a further specific determination of the District Court, namely, that the invalidation of the restraints here at issue "would not increase competition in Topco private label brands." Indeed, the District Court seemed to believe that it would, on the contrary, lead to the likely demise of those brands in time. And the evidence before the District Court would appear to justify that conclusion.

[37] There is no national demand for Topco brands, nor has there ever been any national advertising of those brands. It would be impracticable for Topco, with its limited financial resources, to convert itself into a national brand distributor in competition with distributors of existing national brands. Furthermore, without the right to grant exclusive licenses, it could not attract and hold new members as replacements for those of its present members who, following the pattern of the past, eventually grow sufficiently in size to be able to leave the cooperative organization and develop their own individual private-label brands. Moreover, Topco's present members, once today's decision has had its full impact over the course of time, will have no more reason to promote Topco products through local advertising and merchandising efforts than they will have such reason to promote any other generally available brands.

[38] The issues presented by the antitrust cases reaching this Court are rarely simple to resolve under the rule of reason; they do indeed frequently require us to make difficult economic determinations. We should not for that reason alone, however, be overly zealous in formulating new *per se* rules, for an excess of zeal in that regard is both contrary to the policy of the Sherman Act and detrimental to the welfare of consumers generally. Indeed, the economic effect of the new rule laid down by the Court today seems clear: unless Congress intervenes, grocery staples marketed under private-label brands with their lower consumer prices will soon be available only to those who patronize the large national chains.

* * *

We now turn to two more modern landmarks on the boundary between the *per se* rule and the rule of reason: *Broadcast Music Inc.* (often just "*BMI*") and *Maricopa County*. *BMI* was a watershed case, and arguably it marked the repudiation of the formalism on display in *Sealy* and *Topco.* In *BMI*, the Court declined to condemn as *per se* illegal an activity that, it recognized, involved "literal" price fixing. *BMI* established that coordination among competitors to create a new product or service that would not otherwise be available, without restricting the participants' freedom to compete individually, should be judged under the rule of reason, not the *per se* rule. In *Maricopa County*, by contrast, the Court went the other way, condemning as *per se* illegal joint activity among competitors that one might have thought plausibly related to a procompetitive activity.[360] Subsequent cases (including *Board of Regents*, which we encountered in Chapter IV, and the *Indiana Federation of Dentists* and *California Dental Association* decisions we will meet later in this Chapter) have tended to take an approach that more closely resembles the one in *BMI* than the one in *Maricopa County*. That is: when a horizontal collaboration is plausibly related to significant procompetitive benefits, the Court has tended to avoid *per se* condemnation.[361]

Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.

441 U.S. 1 (1979)

Justice White.

[1] This case involves an action under the antitrust and copyright laws brought by respondent Columbia Broadcasting System, Inc. (CBS), against petitioners, American Society of Composers, Authors and Publishers (ASCAP) and Broadcast Music, Inc. (BMI), and their members and affiliates. The basic question presented is whether the issuance by ASCAP and BMI to CBS of blanket licenses to copyrighted musical compositions at fees negotiated by them is price fixing *per se* unlawful under the antitrust laws. [. . .]

[2] CBS operates one of three national commercial television networks, supplying programs to approximately 200 affiliated stations and telecasting approximately 7,500 network programs per year. Many, but not all, of these programs make use of copyrighted music recorded on the soundtrack. CBS also owns television and radio stations in various cities. [. . .]

[3] Since 1897, the copyright laws have vested in the owner of a copyrighted musical composition the exclusive right to perform the work publicly for profit, but the legal right is not self-enforcing. In 1914, Victor Herbert and a handful of other composers organized ASCAP because those who performed copyrighted music for profit were so numerous and widespread, and most performances so fleeting, that as a practical matter it was impossible for the many individual copyright owners to negotiate with and license the users and to detect unauthorized uses. ASCAP was organized as a clearing-house for copyright owners and users to solve these problems associated with the licensing of music. As ASCAP operates today, its 22,000 members grant it nonexclusive rights to license nondramatic performances of their works, and ASCAP issues licenses and distributes royalties to copyright owners in accordance with a schedule reflecting the nature and amount of the use of their music and other factors.

[4] BMI, a nonprofit corporation owned by members of the broadcasting industry, was organized in 1939, is affiliated with or represents some 10,000 publishing companies and 20,000 authors and composers, and operates in much the same manner as ASCAP. Almost every domestic copyrighted composition is in the repertory either of ASCAP, with a total of three million compositions, or of BMI, with one million.

[5] Both organizations operate primarily through blanket licenses, which give the licensees the right to perform any and all of the compositions owned by the members or affiliates as often as the licensees desire for a stated term. Fees for blanket licenses are ordinarily a percentage of total revenues or a flat dollar amount, and do not

---

[360] *See*, *e.g.*, Rocco J. De Grasse, Maricopa County *and the Problem of Per Se Characterization in Horizontal Price Fixing Cases*, 18 Val. U. L. Rev. 1007 (1984); *but see*, *e.g.*, Keith B. Leffler, Arizona v. Maricopa County Medical Society: *Maximum-Price Agreements in Markets with Insured Buyers*, 2 Sup. Ct. Econ. Rev. 187 (1983) (supporting per se condemnation).

[361] *But see*, *e.g.*, NCAA v. Alston, 141 S.Ct. 2141, 2167 (2021) (Kavanaugh, J., concurring) ("Price-fixing labor is price-fixing labor.").

directly depend on the amount or type of music used. Radio and television broadcasters are the largest users of music, and almost all of them hold blanket licenses from both ASCAP and BMI. Until this litigation, CBS held blanket licenses from both organizations for its television network on a continuous basis since the late 1940's and had never attempted to secure any other form of license from either ASCAP[5] or any of its members.

[6] The complaint filed by CBS charged various violations of the Sherman Act and the copyright laws. CBS argued that ASCAP and BMI are unlawful monopolies and that the blanket license is illegal price fixing, an unlawful tying arrangement, a concerted refusal to deal, and a misuse of copyrights. The District Court, though denying summary judgment to certain defendants, ruled that the practice did not fall within the *per se* rule. After an 8-week trial, limited to the issue of liability, the court dismissed the complaint, rejecting again the claim that the blanket license was price fixing and a *per se* violation of § 1 of the Sherman Act, and holding that since direct negotiation with individual copyright owners is available and feasible there is no undue restraint of trade, illegal tying, misuse of copyrights, or monopolization.

[7] Though agreeing with the District Court's factfinding and not disturbing its legal conclusions on the other antitrust theories of liability, the Court of Appeals held that the blanket license issued to television networks was a form of price fixing illegal *per se* under the Sherman Act. This conclusion, without more, settled the issue of liability under the Sherman Act, established copyright misuse, and required reversal of the District Court's judgment, as well as a remand to consider the appropriate remedy.

[8] [. . .] Because we disagree with the Court of Appeals' conclusions with respect to the *per se* illegality of the blanket license, we reverse its judgment and remand the cause for further appropriate proceedings.

[9] In construing and applying the Sherman Act's ban against contracts, conspiracies, and combinations in restraint of trade, the Court has held that certain agreements or practices are so plainly anticompetitive and so often lack . . . any redeeming virtue, that they are conclusively presumed illegal without further examination under the rule of reason generally applied in Sherman Act cases. This *per se* rule is a valid and useful tool of antitrust policy and enforcement. And agreements among competitors to fix prices on their individual goods or services are among those concerted activities that the Court has held to be within the *per se* category. But easy labels do not always supply ready answers.

[10] To the Court of Appeals and CBS, the blanket license involves "price fixing" in the literal sense: the composers and publishing houses have joined together into an organization that sets its price for the blanket license it sells. But this is not a question simply of determining whether two or more potential competitors have literally "fixed" a "price." As generally used in the antitrust field, "price fixing" is a shorthand way of describing certain categories of business behavior to which the *per se* rule has been held applicable. The Court of Appeals' literal approach does not alone establish that this particular practice is one of those types or that it is "plainly anticompetitive" and very likely without "redeeming virtue." Literalness is overly simplistic and often overbroad. When two partners set the price of their goods or services they are literally "price fixing," but they are not *per se* in violation of the Sherman Act. Thus, it is necessary to characterize the challenged conduct as falling within or without that category of behavior to which we apply the label "*per se* price fixing." That will often, but not always, be a simple matter.

[11] Consequently, as we recognized in *United States v. Topco Associates, Inc.,* 405 U.S. 596, 607–608 (1972), "[i]t is only after considerable experience with certain business relationships that courts classify them as *per se* violations . . . ." We have never examined a practice like this one before; indeed, the Court of Appeals recognized that in dealing with performing rights in the music industry we confront conditions both in copyright law and in antitrust law which are *sui generis*. And though there has been rather intensive antitrust scrutiny of ASCAP and its blanket licenses, that experience hardly counsels that we should outlaw the blanket license as a *per se* restraint of trade. [. . .]

[5] Unless the context indicates otherwise, references to ASCAP alone in this opinion usually apply to BMI as well. . . .

[12] [The Department of Justice sued ASCAP in 1941, alleging that the blanket license was anticompetitive. That litigation resulted in settlement and a consent decree, which was modified in 1950.] Under the amended decree . . .members may grant ASCAP only nonexclusive rights to license their works for public performance. Members, therefore, retain the rights individually to license public performances, along with the rights to license the use of their compositions for other purposes. ASCAP itself is forbidden to grant any license to perform one or more specified compositions in the ASCAP repertory unless both the user and the owner have requested it in writing to do so. ASCAP is required to grant to any user making written application a nonexclusive license to perform all ASCAP compositions either for a period of time or on a per-program basis. ASCAP may not insist on the blanket license, and the fee for the per-program license, which is to be based on the revenues for the program on which ASCAP music is played, must offer the applicant a genuine economic choice between the per-program license and the more common blanket license. If ASCAP and a putative licensee are unable to agree on a fee within 60 days, the applicant may apply to the District Court for a determination of a reasonable fee, with ASCAP having the burden of proving reasonableness.

[13] The 1950 decree, as amended from time to time, continues in effect, and the blanket license continues to be the primary instrument through which ASCAP conducts its business under the decree. The courts have twice construed the decree not to require ASCAP to issue licenses for selected portions of its repertory. It also remains true that the decree guarantees the legal availability of direct licensing of performance rights by ASCAP members; and the District Court found, and in this respect the Court of Appeals agreed, that there are no practical impediments preventing direct dealing by the television networks if they so desire. Historically, they have not done so. Since 1946, CBS and other television networks have taken blanket licenses from ASCAP and BMI. It was not until this suit arose that the CBS network demanded any other kind of license.

[14] Of course, a consent judgment, even one entered at the behest of the Antitrust Division, does not immunize the defendant from liability for actions, including those contemplated by the decree, that violate the rights of nonparties. But it cannot be ignored that the Federal Executive and Judiciary have carefully scrutinized ASCAP and the challenged conduct, have imposed restrictions on various of ASCAP's practices, and, by the terms of the decree, stand ready to provide further consideration, supervision, and perhaps invalidation of asserted anticompetitive practices. In these circumstances, we have a unique indicator that the challenged practice may have redeeming competitive virtues and that the search for those values is not almost sure to be in vain. Thus, although CBS is not bound by the Antitrust Division's actions, the decree is a fact of economic and legal life in this industry, and the Court of Appeals should not have ignored it completely in analyzing the practice. That fact alone might not remove a naked price-fixing scheme from the ambit of the *per se* rule, but . . . here we are uncertain whether the practice on its face has the effect, or could have been spurred by the purpose, of restraining competition among the individual composers. [. . .]

[15] Finally, we note that Congress itself, in the new Copyright Act, has chosen to employ the blanket license and similar practices. Congress created a compulsory blanket license for secondary transmissions by cable television systems and provided that "[n]otwithstanding any provisions of the antitrust laws, . . . any claimants may agree among themselves as to the proportionate division of compulsory licensing fees among them, may lump their claims together and file them jointly or as a single claim, or may designate a common agent to receive payment on their behalf." 17 U.S.C. § 111(d)(5)(A). And the newly created compulsory license for the use of copyrighted compositions in jukeboxes is also a blanket license, which is payable to the performing-rights societies such as ASCAP unless an individual copyright holder can prove his entitlement to a share. § 116(c)(4). Moreover, in requiring noncommercial broadcasters to pay for their use of copyrighted music, Congress again provided that "[n]otwithstanding any provision of the antitrust laws" copyright owners "may designate common agents to negotiate, agree to, pay, or receive payments." § 118(b). Though these provisions are not directly controlling, they do reflect an opinion that the blanket license, and ASCAP, are economically beneficial in at least some circumstances. [. . .]

[16] As a preliminary matter, we are mindful that the Court of Appeals' holding would appear to be quite difficult to contain. If, as the court held, there is a *per se* antitrust violation whenever ASCAP issues a blanket license to a television network for a single fee, why would it not also be automatically illegal for ASCAP to negotiate and issue blanket licenses to individual radio or television stations or to other users who perform

copyrighted music for profit? Likewise, if the present network licenses issued through ASCAP on behalf of its members are *per se* violations, why would it not be equally illegal for the members to authorize ASCAP to issue licenses establishing various categories of uses that a network might have for copyrighted music and setting a standard fee for each described use?

[17] Although the Court of Appeals apparently thought the blanket license could be saved in some or even many applications, it seems to us that the *per se* rule does not accommodate itself to such flexibility and that the observations of the Court of Appeals with respect to remedy tend to impeach the *per se* basis for the holding of liability.[27]

[18] CBS would prefer that ASCAP be authorized, indeed directed, to make all its compositions available at standard per-use rates within negotiated categories of use. But if this in itself or in conjunction with blanket licensing constitutes illegal price fixing by copyright owners, CBS urges that an injunction issue forbidding ASCAP to issue any blanket license or to negotiate any fee except on behalf of an individual member for the use of his own copyrighted work or works. Thus, we are called upon to determine that blanket licensing is unlawful across the board. We are quite sure, however, that the *per se* rule does not require any such holding. [. . .]

[19] In the first place, the line of commerce allegedly being restrained, the performing rights to copyrighted music, exists at all only because of the copyright laws. Those who would use copyrighted music in public performances must secure consent from the copyright owner or be liable at least for the statutory damages for each infringement and, if the conduct is willful and for the purpose of financial gain, to criminal penalties. Furthermore, nothing in the Copyright Act of 1976 indicates in the slightest that Congress intended to weaken the rights of copyright owners to control the public performance of musical compositions. Quite the contrary is true. Although the copyright laws confer no rights on copyright owners to fix prices among themselves or otherwise to violate the antitrust laws, we would not expect that any market arrangements reasonably necessary to effectuate the rights that are granted would be deemed a *per se* violation of the Sherman Act. Otherwise, the commerce anticipated by the Copyright Act and protected against restraint by the Sherman Act would not exist at all or would exist only as a pale reminder of what Congress envisioned.[32]

[20] More generally, in characterizing this conduct under the *per se* rule,[33] our inquiry must focus on whether the effect and, here because it tends to show effect, the purpose of the practice are to threaten the proper operation of our predominantly free-market economy—that is, whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output, and in what portion of the market, or instead one designed to increase economic efficiency and render markets more, rather than less, competitive.

[21] The blanket license, as we see it, is not a naked restraint of trade with no purpose except stifling of competition, but rather accompanies the integration of sales, monitoring, and enforcement against unauthorized copyright use. As we have already indicated, ASCAP and the blanket license developed together out of the

---

[27] The Court of Appeals would apparently not outlaw the blanket license across the board but would permit it in various circumstances where it is deemed necessary or sufficiently desirable. It did not even enjoin blanket licensing with the television networks, the relief it realized would normally follow a finding of *per se* illegality of the license in that context. Instead, as requested by CBS, it remanded to the District Court to require ASCAP to offer in addition to blanket licensing some competitive form of per-use licensing. But per-use licensing by ASCAP, as recognized in the consent decrees, might be even more susceptible to the *per se* rule than blanket licensing.

The rationale for this unusual relief in a *per se* case was that "[t]he blanket license is not simply a 'naked restraint' ineluctably doomed to extinction." To the contrary, the Court of Appeals found that the blanket license might well "serve a market need" for some. This, it seems to us, is not the *per se* approach, which does not yield so readily to circumstances, but in effect is a rather bobtailed application of the rule of reason, bobtailed in the sense that it is unaccompanied by the necessary analysis demonstrating why the particular licensing system is an undue competitive restraint.

[32] Because a musical composition can be "consumed" by many different people at the same time and without the creator's knowledge, the "owner" has no real way to demand reimbursement for the use of his property except through the copyright laws *and* an effective way to enforce those legal rights. It takes an organization of rather large size to monitor most or all uses and to deal with users on behalf of the composers. Moreover, it is inefficient to have too many such organizations duplicating each other's monitoring of use.

[33] The scrutiny occasionally required must not merely subsume the burdensome analysis required under the rule of reason, or else we should apply the rule of reason from the start. That is why the *per se* rule is not employed until after considerable experience with the type of challenged restraint.

practical situation in the marketplace: thousands of users, thousands of copyright owners, and millions of compositions. Most users want unplanned, rapid, and indemnified access to any and all of the repertory of compositions, and the owners want a reliable method of collecting for the use of their copyrights. Individual sales transactions in this industry are quite expensive, as would be individual monitoring and enforcement, especially in light of the resources of single composers. Indeed, as both the Court of Appeals and CBS recognize, the costs are prohibitive for licenses with individual radio stations, nightclubs, and restaurants, and it was in that milieu that the blanket license arose.

[22] A middleman with a blanket license was an obvious necessity if the thousands of individual negotiations, a virtual impossibility, were to be avoided. Also, individual fees for the use of individual compositions would presuppose an intricate schedule of fees and uses, as well as a difficult and expensive reporting problem for the user and policing task for the copyright owner. Historically, the market for public-performance rights organized itself largely around the single-fee blanket license, which gave unlimited access to the repertory and reliable protection against infringement. When ASCAP's major and user-created competitor, BMI, came on the scene, it also turned to the blanket license.

[23] With the advent of radio and television networks, market conditions changed, and the necessity for and advantages of a blanket license for those users may be far less obvious than is the case when the potential users are individual television or radio stations, or the thousands of other individuals and organizations performing copyrighted compositions in public. But even for television network licenses, ASCAP reduces costs absolutely by creating a blanket license that is sold only a few, instead of thousands, of times, and that obviates the need for closely monitoring the networks to see that they do not use more than they pay for. ASCAP also provides the necessary resources for blanket sales and enforcement, resources unavailable to the vast majority of composers and publishing houses. Moreover, a bulk license of some type is a necessary consequence of the integration necessary to achieve these efficiencies, and a necessary consequence of an aggregate license is that its price must be established.

[24] This substantial lowering of costs, which is of course potentially beneficial to both sellers and buyers, differentiates the blanket license from individual use licenses. The blanket license is composed of the individual compositions plus the aggregating service. Here, the whole is truly greater than the sum of its parts; it is, to some extent, a different product. The blanket license has certain unique characteristics: It allows the licensee immediate use of covered compositions, without the delay of prior individual negotiations and great flexibility in the choice of musical material. Many consumers clearly prefer the characteristics and cost advantages of this marketable package, and even small-performing rights societies that have occasionally arisen to compete with ASCAP and BMI have offered blanket licenses. Thus, to the extent the blanket license is a different product, ASCAP is not really a joint sales agency offering the individual goods of many sellers, but is a separate seller offering its blanket license, of which the individual compositions are raw material.[40] ASCAP, in short, made a market in which individual composers are inherently unable to compete fully effectively.

[25] Finally, we have some doubt—enough to counsel against application of the *per se* rule—about the extent to which this practice threatens the "central nervous system of the economy," *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 226 n.59 (1940), that is, competitive pricing as the free market's means of allocating resources. Not all arrangements among actual or potential competitors that have an impact on price are *per se* violations of the Sherman Act or even unreasonable restraints. Mergers among competitors eliminate competition, including price competition, but they are not *per se* illegal, and many of them withstand attack under any existing antitrust standard. Joint ventures and other cooperative arrangements are also not usually unlawful, at least not as price-fixing schemes, where the agreement on price is necessary to market the product at all.

[26] Here, the blanket-license fee is not set by competition among individual copyright owners, and it is a fee for the use of any of the compositions covered by the license. But the blanket license cannot be wholly equated with a simple horizontal arrangement among competitors. ASCAP does set the price for its blanket license, but that license is quite different from anything any individual owner could issue. The individual composers and authors have neither agreed not to sell individually in any other market nor use the blanket license to mask price fixing in such other markets. Moreover, the substantial restraints placed on ASCAP and its members by the consent

decree must not be ignored. The District Court found that there was no legal, practical, or conspiratorial impediment to CBS's obtaining individual licenses; CBS, in short, had a real choice.

[27] With this background in mind, which plainly enough indicates that over the years, and in the face of available alternatives, the blanket license has provided an acceptable mechanism for at least a large part of the market for the performing rights to copyrighted musical compositions, we cannot agree that it should automatically be declared illegal in all of its many manifestations. Rather, when attacked, it should be subjected to a more discriminating examination under the rule of reason. It may not ultimately survive that attack, but that is not the issue before us today.

[28] [T]he general import of [the judgment of the Court of Appeals below was] that the licensing practices of ASCAP and BMI under the consent decree are *per se* violations of the Sherman Act. We reverse that judgment . . . and remand for further proceedings to consider any unresolved issues that CBS may have properly brought to the Court of Appeals. [. . .]

Justice Stevens, dissenting.

[29] The Court holds that ASCAP's blanket license is not a species of price fixing categorically forbidden by the Sherman Act. I agree with that holding. The Court remands the cases to the Court of Appeals, leaving open the question whether the blanket license as employed by ASCAP and BMI is unlawful under a rule-of-reason inquiry. I think that question is properly before us now and should be answered affirmatively.

[30] There is ample precedent for affirmance of the judgment of the Court of Appeals on a ground that differs from its rationale, provided of course that we do not modify its judgment. In this litigation, the judgment of the Court of Appeals was not that blanket licenses may never be offered by ASCAP and BMI. Rather, its judgment directed the District Court to fashion relief requiring them to offer additional forms of license as well. Even though that judgment may not be consistent with its stated conclusion that the blanket license is "illegal *per se*" as a kind of price fixing, it is entirely consistent with a conclusion that petitioners' exclusive all-or-nothing blanket-license policy violates the rule of reason.

[31] The Court of Appeals may well so decide on remand. In my judgment, however, a remand is not necessary. The record before this Court is a full one, reflecting extensive discovery and eight weeks of trial. The District Court's findings of fact are thorough and well supported. They clearly reveal that the challenged policy does have a significant adverse impact on competition. I would therefore affirm the judgment of the Court of Appeals. [. . .]

[32] The market for music at issue here is wholly dominated by ASCAP-issued blanket licenses. Virtually every domestic copyrighted composition is in the repertoire of either ASCAP or BMI. And again, virtually without exception, the only means that has been used to secure authority to perform such compositions is the blanket license.

[33] The blanket all-or-nothing license is patently discriminatory. The user purchases full access to ASCAP's entire repertoire, even though his needs could be satisfied by a far more limited selection. The price he pays for this access is unrelated either to the quantity or the quality of the music he actually uses, or, indeed, to what he would probably use in a competitive system. Rather, in this unique all-or-nothing system, the price is based on a percentage of the user's advertising revenues, a measure that reflects the customer's ability to pay but is totally unrelated to factors—such as the cost, quality, or quantity of the product—that normally affect price in a competitive market. The ASCAP system requires users to buy more music than they want at a price which, while not beyond their ability to pay and perhaps not even beyond what is "reasonable" for the access they are getting, may well be far higher than what they would choose to spend for music in a competitive system. It is a classic example of economic discrimination.

[34] The record plainly establishes that there is no price competition between separate musical compositions. Under a blanket license, it is no more expensive for a network to play the most popular current hit in prime time than it is to use an unknown composition as background music in a soap opera. Because the cost to the user is unaffected by the amount used on any program or on all programs, the user has no incentive to economize by,

for example, substituting what would otherwise be less expensive songs for established favorites or by reducing the quantity of music used on a program. The blanket license thereby tends to encourage the use of more music, and also of a larger share of what is really more valuable music, than would be expected in a competitive system characterized by separate licenses. And since revenues are passed on to composers on a basis reflecting the character and frequency of the use of their music, the tendency is to increase the rewards of the established composers at the expense of those less well known. Perhaps the prospect is in any event unlikely, but the blanket license does not present a new songwriter with any opportunity to try to break into the market by offering his product for sale at an unusually low price. The absence of that opportunity, however unlikely it may be, is characteristic of a cartelized rather than a competitive market.

[35] The current state of the market cannot be explained on the ground that it could not operate competitively, or that issuance of more limited—and thus less restrictive—licenses by ASCAP is not feasible. The District Court's findings disclose no reason why music-performing rights could not be negotiated on a per-composition or per-use basis, either with the composer or publisher directly or with an agent such as ASCAP. In fact, ASCAP now compensates composers and publishers on precisely those bases. If distributions of royalties can be calculated on a per-use and per-composition basis, it is difficult to see why royalties could not also be collected in the same way. Moreover, the record also shows that where ASCAP's blanket-license scheme does not govern, competitive markets do. A competitive market for "synch" rights exists, and after the use of blanket licenses in the motion picture industry was discontinued, such a market promptly developed in that industry. In sum, the record demonstrates that the market at issue here is one that could be highly competitive, but is not competitive at all. [. . .]

[36] More basically, ASCAP's underlying argument that CBS must be viewed as having acted with complete freedom in choosing the blanket license is not supported by the District Court's findings. The District Court did not find that CBS could cancel its blanket license "tomorrow" and continue to use music in its programming and compete with the other networks. Nor did the District Court find that such a course was without any risk or expense. Rather, the District Court's finding was that within a year, during which it would continue to pay some millions of dollars for its annual blanket license, CBS would be able to develop the needed machinery and enter into the necessary contracts. In other words, although the barriers to direct dealing by CBS as an alternative to paying for a blanket license are real and significant, they are not insurmountable.

[37] Far from establishing ASCAP's immunity from liability, these District Court findings, in my judgment, confirm the illegality of its conduct. Neither CBS nor any other user has been willing to assume the costs and risks associated with an attempt to purchase music on a competitive basis. The fact that an attempt by CBS to break down the ASCAP monopoly might well succeed does not preclude the conclusion that smaller and less powerful buyers are totally foreclosed from a competitive market. [. . .]

[38] Antitrust policy requires that great aggregations of economic power be closely scrutinized. That duty is especially important when the aggregation is composed of statutory monopoly privileges. Our cases have repeatedly stressed the need to limit the privileges conferred by patent and copyright strictly to the scope of the statutory grant. The record in this case plainly discloses that the limits have been exceeded and that ASCAP and BMI exercise monopoly powers that far exceed the sum of the privileges of the individual copyright holders. Indeed, ASCAP itself argues that its blanket license constitutes a product that is significantly different from the sum of its component parts. I agree with that premise, but I conclude that the aggregate is a monopolistic restraint of trade proscribed by the Sherman Act.

CASENOTE: Arizona v. Maricopa County Medical Society

457 U.S. 332 (1982)

BMI marked a profound inflection point in the history of antitrust's approach to horizontal restraints: a shift away from the formal severity of *Sealy* and *Topco*'s reaction to coordination among rivals, toward a more cautious, more granular, effects-based approach. But *BMI* did not spell the end of the *per se* rule, or even its application to conduct that was clearly more complicated than simple price fixing or market division. *Maricopa*

County—decided in 1982, just three years after *BMI* came down—stands as a reminder that, even post-*BMI*, the *per se* rule may be applied to conduct of some complexity.

The case concerned the activities of the Maricopa Foundation for Medical Care and the Pima Foundation for Medical Care ("Foundations"), two nonprofits that had been created in order to provide an alternative to existing healthcare models. Under the traditional models, a patient either: (1) obtains insurance coverage from an insurer for customary and reasonable medical expenses, and then obtains treatment from a provider, with the reasonable costs borne by the insurer and any excess being borne by the insured patient themselves (the traditional fee-for-service model); or (2) pays a fixed regular amount to a group of healthcare providers, in exchange for the provision of medical care, with the provider group bearing the risk that costs of care will exceed the insured's payments (the health maintenance organization or "HMO" model).

The Foundations were designed to provide a new model of payment for healthcare by offering something distinctive to doctors, insurers, and patients:

- Doctors were offered the opportunity to participate in the model, and thus receive the business of covered patients and the benefits of swift payment, in exchange for committing to accept a schedule of maximum fees (set by a vote of the member physicians) as full payment for their services, subject to the Foundations' determination that the care was necessary and appropriate. Participating doctors were free to charge anything they liked to patients not covered by the model, and were also free to charge *less* than the maximum fee to covered patients.
- Insurers were offered the opportunity to participate in the model, and thus receive the business of covered patients, the benefit of guaranteed low prices from doctors, and the benefits of the Foundations' technical assessment of the necessity and appropriateness of care, in exchange for allowing the Foundations to write checks that drew directly on their accounts to pay doctors swiftly for providing necessary and appropriate care.
- Patients were offered the opportunity to participate in the model, and thus receive efficient care—as well as freedom from the threat that they will be made to bear the burden of excess medical expenses—in exchange for their premiums. Patients were free to go to nonparticipating doctors to obtain care: if they did so, they would be covered up to the scheduled amount for the service received, but would be personally on the hook for any excess.

The Foundations were a success. About 70% of the medical practitioners in Maricopa County, Arizona, joined the Maricopa Foundation, and about 400 doctors joined the Pima Foundation. And the maximum-fee schedules seemed to compare favorably to market rates for service: around 90% of the physicians in Maricopa County billed at or above the fee rates set by the Maricopa Foundation.

But then things hit a snag: Arizona sued the Foundations (and the Maricopa County Medical Society) under Section 1 for price-fixing. Arizona moved for summary judgment on the issue of liability, which the district court and court of appeals both declined to grant. But the Supreme Court granted cert and, in an opinion by Justice Stevens for a four-Justice majority (with two recusals), granted Arizona's motion.

The Court began by acknowledging that the evidence on the competitive effects of the Foundations' new model—and particularly the fee schedules—was mixed. Arizona argued that the schedules tended to stabilize and increase prices, while the Foundations argued that they tended to limit and reduce prices. As Arizona was the summary judgment movant, the Court acknowledged accepted the Foundations' interpretation.

But this benefit of the doubt did not save the Foundations! The Court sternly reiterated the *per se* illegality of all agreements to fix prices, even agreements to fix maximum prices. And here, the Court continued, that rule "is violated by a price restraint that tends to provide the same economic rewards to all practitioners regardless of their skill, their experience, their training, or their willingness to employ innovative and difficult procedures in individual cases. Such a restraint also may discourage entry into the market and may deter experimentation and new developments by individual entrepreneurs. It may be a masquerade for an agreement to fix uniform prices, or it may in the future take on that character." The fact that the Court had "little antitrust experience in the health care industry" would not change that conclusion. Indeed, the whole point of the rule was to avoid "an

incredibly complicated and prolonged economic investigation into the entire history of the industry involved . . . an inquiry so often wholly fruitless when undertaken."

The Foundations had argued that *per se* condemnation was inappropriate because the collaboration here had procompetitive benefits, and specifically that it made it possible to "provide consumers of health care with a uniquely desirable form of insurance coverage that could not otherwise exist." The Foundations specifically emphasized the value of offering patients "a choice of doctors, complete insurance coverage, and lower premiums," compared to existing models of healthcare coverage. But the Court was not impressed. The first two items could be obtained in other ways. And while a maximum fee schedule was probably necessary in order to secure (the potential for) lower prices and an assurance of complete coverage, "it is not necessary that the doctors do the price fixing": after all, insurers could set their own maximum-price schedules rather than having competing doctors do so jointly. "[N]othing in the record," the Court concluded, "even arguably supports the conclusion that this type of insurance program could not function if the fee schedules were set in a different way."

Despite the summary-judgment posture, the Court seemed to credit Arizona's interpretation of the evidence of the interaction of the model's positive and negative effects. "[T]here is no reason to believe that any savings that might accrue from this arrangement would be sufficiently great to affect the competitiveness of these kinds of insurance plans. It is *entirely possible* that the potential or actual power of the foundations to dictate the terms of such insurance plans may more than offset the theoretical efficiencies upon which the respondents' defense ultimately rests." (Emphasis added.)

Nor did the Court's recent *BMI* decision save the day for the Foundations. *BMI*, the Court explained, involved the joint creation of a product that would not otherwise have been available. By contrast, the doctors' cooperation here "does not permit them to sell any different product. Their combination has merely permitted them to sell their services to certain customers at fixed prices and arguably to affect the prevailing market price of medical care."

In closing, the Court nodded at possible alternative models that might have earned more favorable treatment. "The foundations are not analogous to partnerships or other joint arrangements in which persons who would otherwise be competitors pool their capital and share the risks of loss as well as the opportunities for profit. . . . The agreement under attack is an agreement among hundreds of competing doctors concerning the price at which each will offer his own services to a substantial number of consumers. . . . If a clinic offered complete medical coverage for a flat fee, the cooperating doctors would have the type of partnership arrangement in which a price-fixing agreement among the doctors would be perfectly proper. But the fee agreements disclosed by the record in this case are among independent competing entrepreneurs. They fit squarely into the horizontal price-fixing mold." Liability followed.

Justice Powell, joined by two other members of the Court, dissented. The Foundations, he argued, offered a "comparatively new method of providing insured medical services at predetermined maximum costs. . . . [T]he plan seems to be in the public interest." Moreover, given the summary-judgment posture, the Foundations were entitled to the benefit of all reasonable inferences from the record. And here, that compelled the assumption that the Foundations' model had limited doctors' fees, helped insurers to assess risk more accurately, and saved patients and payers money.

He pointed out that the Foundations did not prohibit or deter what would amount to cheating on the supposed cartel: physicians and insurers retained freedom to deal on whatever terms they liked outside of the scope of the collaboration. Even more telling was the fact that seven insurers—the payers for care, with every incentive to keep costs down rather than drive them up—had voluntarily chosen to invite the doctors to jointly establish appropriate maximum prices. This suggested that the collaboration's true effect was indeed to keep prices down rather than drive them up.

The blanket license in *BMI* was a close parallel to the enterprise here. "Each involved competitors and resulted in co-operative pricing. Each arrangement also was prompted by the need for better service to the consumers. And each arrangement apparently makes possible a new product by reaping otherwise unattainable efficiencies."

In condemning the collaboration, Justice Powell concluded, the Court had "[lost] sight of the basic purposes of the Sherman Act. . . . [T]he antitrust laws are a consumer welfare prescription. In its rush to condemn a novel plan about which it knows very little, the Court suggests that this end is achieved only by invalidating activities that may have some potential for harm. But the little that the record does show about the effect of the plan suggests that it is a means of providing medical services that in fact benefits rather than injures persons who need them." To label this enterprise "price fixing" and condemn it out of hand was to ignore the reality that a complex economy often produces complex arrangements that merited a closer look. "It is unwise for the Court, in a case as novel and important as this one, to make a final judgment in the absence of a complete record and where mandatory inferences create critical issues of fact."

CASENOTE: Deslandes v. McDonald's USA, LLC

81 F.4th 699 (7th Cir. 2023)

When franchisees agree on prices, territories, wages, or other dimensions of competition, is that a *per se* violation of the antitrust laws, or an ancillary restraint that must be assessed under the rule of reason? A recent decision of the Seventh Circuit suggests that, depending on the context, it might be either.

The plaintiffs in *Deslandes* were employees of franchisees of McDonald's, and they sued to challenge an "anti-poach" clause in the standard McDonald's franchise agreement. Pursuant to that clause, each franchise operator agreed not to hire any person employed by McDonald's or by another McDonald's franchisee until six months after such employment had ended. This, they alleged, harmed competition for labor. But the district court below had dismissed the complaint on two grounds: (1) because *per se* condemnation was inappropriate as the restraint here was not naked, but was rather ancillary to a procompetitive franchise agreement; and (2) for failure to allege that McDonald's and its franchisees held market power in a market for restaurant workers' labor, as without such power no showing of anticompetitive effect at step one of the rule of reason could be made.

The Seventh Circuit reversed. Judge Easterbrook, writing for the panel, held that the district court had wrongly dismissed the prospect of *per se* liability. For one thing, he suggested, any benefit that might make the restraint non-naked would have to accrue in the market for labor, not in the downstream market for fast food service to consumers. It was "not right," he indicated, to treat benefits to consumers as justifying detriments to workers. For another thing, the fact that that anti-poach agreement was created at the same time as the broader franchise relationship did not mean that it was in fact reasonably related to that procompetitive end. "[What was the no-poach clause doing?" he asked. "Was it protecting [franchisees'] investments in training, or was it allowing them to appropriate the value of workers' own investments?" Answering this question would require "careful economic analysis" of a kind that could not be done on the face of the complaint. Moreover, the claim that the restraint was ancillary, rather than naked, was a defense, and "complaints need not anticipate and plead around defenses." The dismissal of the *per se* claim was reversed, and the case remanded for further proceedings.

NOTES

1) Did *Broadcast Music* repudiate *Sealy* and *Topco*? And did *Maricopa County* in turn cut back on *Broadcast Music*? Or is there a consistent principle that explains all four cases?
2) Can you explain why the Court in *Broadcast Music* applied the rule of reason rather than the *per se* rule? Do you agree with the Court that the system of blanket licensing of musical compositions is procompetitive? What about Justice Stevens' point that the same competitive benefits can be obtained without an "all-or-nothing" system of blanket licensing?
3) ASCAP and BMI remain under antitrust consent decrees to this day; in fact, in 2021, after considering the issue, the Antitrust Division decided to leave the consent decrees in place without modification. But the apparent stability may be deceiving. During the most recent DOJ review of the consent decrees, the Division learned that ASCAP and BMI (as well as smaller "performance rights organization" competitors

SESAC and GMR) are engaging in so-called "fractional licensing"—i.e., instead of licensing the full rights to each composition in their portfolio, for compositions with more than one owner the PROs license only the *share* of copyright ownership that belongs to the copyright owner or owners that license through that PRO. The result is that for many popular musical compositions, a licensee must license from multiple PROs in order to clear rights for the composition. And this means that, at least for these compositions, the PROs are not competitors, but rather, complements. As one of us has recently written:

> The music publishing industry is dominated by three major publishers, but there is a competitive fringe featuring a very large number of smaller publishers. Significantly, ownership of musical compositions is often fragmented among two or more authors, who may be represented by multiple publishers (representation which changes with some frequency as publishers are acquired, or pieces of a publisher's catalog are sold off), and the data that is available to licensees regarding who owns what is very poor. Now imagine that the streaming services, instead of licensing public performance of musical compositions from a few PROs (two of which are subject to non-discrimination requirements), must license directly from literally hundreds of music publishing companies. The opportunities for licensor collusion, holdout and strategic behavior would multiply. And the streaming services would almost inevitably face a wave of copyright infringement lawsuits claiming that the services' direct licenses do not cover all of the copyright ownership shares in some large number of compositions. Perhaps not surprisingly, the streaming services, well aware of the difficulties direct licensing would create for their businesses, expressed relief when the DOJ rebuffed the request to permit partial withdrawal.
>
> Nor would I bet that a Division guided by neo-Brandeisians will move in the coming years to terminate or sunset the consent decrees in favor of an unregulated licensing market. It's more likely that neo-Brandeisians among the Division leadership would conclude that the PROs practice of fractional licensing suggests that the existing consent decrees aren't strong enough. And I think that it's possible that the neo-Brandeisians may go even further. They may conclude that the decrees should be dissolved and new price fixing litigation instituted against the PROs; not just ASCAP and BMI, but the up-and-coming rival PROs SESAC and Global Music Rights (GMR) as well. After all, if ASCAP and BMI are price-fixing vehicles, then SESAC and GMR, which work according to the same basic structure, are too.
>
> If I'm right, then the neo-Brandeisians' end-game might be to use the enormous leverage from the prospect of a new price-fixing lawsuit to negotiate new decrees that apply to all of the PROs. Decrees that strengthen the anti-discrimination provisions of the current decrees, that specifically bar partial withdrawal, that mandate 100% licensing. And that subject all of the PROs to rate court determinations.[362]

4) Were the doctors in *Maricopa County* cooperating to offer a lower-cost healthcare solution in competition with existing options? If so, why was their conduct unlawful? If not, why is that characterization inapt?
5) In both *Topco* and *Maricopa County*, the majority and dissenting opinions disagree on whether the restraints incident to the competitor collaborations in those cases were socially beneficial. Does that disagreement suggest anything about the wisdom of *per se* rules in the context of competitor collaborations?
6) The DOJ/FTC Competitor Collaboration Guidelines state that "[i]f . . . participants in an efficiency-enhancing integration of economic activity enter into an agreement that is reasonably related to the integration and reasonably necessary to achieve its procompetitive benefits, the Agencies analyze the agreement under the rule of reason, even if it is of a type that might otherwise be considered per se illegal." In light of the cases you have just read—or whichever of them you think is still good law—what does it mean for a restraint to be "reasonably necessary" to the collaboration? Does this mean that the collaboration would be profitable only with the restraint? Does it mean that the collaboration would be *significantly more* profitable with the restraint? Something else?
7) Does *Deslandes* imply that an agreement that harms competition in one market while benefiting competition in a separate market is nakedly anticompetitive, and therefore *per se* illegal? Suppose that two suppliers (such

---

[362] Christopher Jon Sprigman, *What Does Antitrust's Revival Mean for Copyright?: The 50th Annual Brace Memorial Lecture of the Copyright Society of the USA*, 68 J. of the Copyright Soc'y 401, 422-23 (2021) (internal citations and notes removed).

as professional service providers) in Market A formed a partnership to enter Market B instead, and ceased to be active in Market A as a result. Does *Deslandes* imply that that is *per se* illegal? Should it be?[363]

2. Joint Facilitating Practices and Information Exchange

As we noted at the beginning of this chapter, competitors across the economy engage in a wide variety of joint practices, from the very benign to the extremely suspicious, leaving agencies and courts to try to separate the harmful ones from the beneficial ones. One long, and sometimes tangled, strand of cases under Section 1 deals with so-called "facilitating practices": that is, practices that may not constitute outright collusion but might have the effect of making collusive-like outcomes much more likely. Such practices may be themselves concerted or unilateral. Unilateral facilitating practices—that is, practices adopted independently by market participants in an effort to make tacit collusion easier—fall outside Section 1, for want of an agreement. In Chapter XI we will see that efforts to tackle them using Section 5 of the FTC Act (which contains a broader prohibition on "unfair methods of competition") have also not generally been successful.[364] But an agreement, express or implied, to do something that may soften competition invites scrutiny under Section 1.

A particularly prominent genre of joint facilitating practice that is clearly subject to evaluation under Section 1 involves the concerted exchange of information among rivals. Information-sharing practices can range from barely disguised cartels to deeply ambiguous activities with genuine procompetitive benefits.

Cases of this kind usually raise either (or both) of two distinct questions under Section 1. The first is whether such practices furnish a basis for inferring an implicit agreement to fix prices or divide markets among competitors: that is, whether they constitute "plus factors" in addition to parallelism from which agreement can be inferred.[365] The second is whether a particular agreement to exchange information is, itself, anticompetitive and a violation of Section 1.

In approaching the second question, courts and agencies recognize that rivals may agree to exchange information with one another for a variety of purposes, and with a variety of effects. On the procompetitive side, information-sharing may promote participants' ability to accurately and efficiently assess current and future market conditions. For example, businesses may be better able to meet demand—now or in future—if they know that a new distribution channel has opened up, or that a supply shortage is coming for a key input, or that demand is likely to spike in a few months' time, or that a new technology will soon become available in a complementary market. In some circumstances, likewise, having accurate information about what my rivals are up to might help facilitate more aggressive competition: perhaps by helping me spot opportunities to satisfy demand more efficiently, borrow strategies to lower my own costs, or win a key customer.

On the anticompetitive side, though, the sharing of information among rivals may also tend to soften, restrict, and even eliminate competition. If I have up-to-date and accurate information about my rivals' current and/or anticipated future prices, this may significantly help me to sustain tacit collusion with them. (As noted above, if my rivals and I are agreeing to exchange such information, that exchange might well be part of an implicit underlying agreement to actually fix prices.) But competitive harm can result from the exchange of information short of current or future price information. More insight into my rivals' costs, margins, customers, capacity, stock-on-hand, strategy, etc., may make me better able to anticipate their reactions in ways that make tacit collusion possible, or more successful.

The Supreme Court's Information-Exchange Jurisprudence

On a number of occasions, the Court has applied Section 1 to information exchanges among rivals, and its approach has changed over time. In its earlier jurisprudence, and particularly a trio of cases in the 1920s, the

[363] We owe this example to Louis Kaplow.

[364] *See infra* § XI.B.2.(a).

[365] *See generally supra* § IV.2. (inference of conspiracy from parallelism and the role of "plus factors").

Court mingled *per se* style language with rule-of-reason-like attention to evidence; it was not until the 1970s that the Court finally clarified that the rule of reason applies to most information-sharing agreements.

In a well-known early case, *American Column* (1921), the Court considered the "Open Competition Plan" operated by the American Hardwood Manufacturers Association.[366] The Plan involved 365 hardwood mill owners, together representing about a third of the national hardwood production of the United States. Under the Plan, each member was required (among other things) to: (1) make a daily report to the Association of all sales and shipments and their terms, including the identity of each customer; (2) make monthly reports of all production and stock on hand; and (3) to file price lists at the beginning of each month and update them immediately with any changes. The Court noted that that the participants had entered into no "definite agreement" to fix or limit production or prices, but noted that "it would be very difficult to devise a more minute disclosure of everything connected with one's business than . . . this Plan."

The *American Column* Court had little difficulty in holding that the Plan violated Section 1. Noting that the Plan's reports to its members, and the discussions at the Association's meetings, were suffused with repeated warnings about "overproduction" and heavy hints about "the proper course [for market participants] to pursue"—and given the testimonials of delighted members about how the Plan had helped to increase prices—the Court found it clear that "the united action of the large and influential membership of dealers contributed greatly to [an] extraordinary price increase." "Genuine competitors," the Court pointed out, "do not make daily, weekly, and monthly reports of the minutest details of their business of their rivals[.]" The Plan was "an old evil in a new dress and with a new name." In condemning the Plan, the Court did not quite make clear whether it was applying a *per se* rule of illegality or a rule-of-reason-style approach: some of the language reaches very broadly, but the court's attention to effects evidence suggests a granular analysis. Justice Holmes wrote a dissenting opinion, finding antitrust condemnation of information exchange "surprising in a country of free speech that affects to regard education and knowledge as desirable." Justice Brandeis also dissented, protesting that the Plan involved neither coercion nor actual uniformity in prices, but rather was an effort to "permit a multitude of small rivals to co-operate . . . in order to protect themselves and the public from the chaos and havoc wrought in their trade by ignorance."

The Court's follow-up decision in *American Linseed* (1923) concerned the operation of the "Armstrong Bureau of Related Industries."[367] The Bureau provided a contract service to 12 linseed "crushers"—manufacturers of linseed oil, together accounting for a "very large part" of national linseed oil consumption—pursuant to which each crusher would commit to report all sales, quotations, and deliveries of linseed (on pain of forfeiting a significant bond deposited with the Bureau) and attend monthly in-person meetings to discuss market conditions. The Court had little difficulty in concluding that "[t]he obvious policy—indeed, the declared purpose—of the arrangement was to submerge the competition . . . among the subscribers." The "necessary tendency" and "manifest purpose" of participation in the scheme was the suppression of competition, and it was clearly unlawful. The Court drew a sharp distinction between unilateral information-sharing, on the one hand, and joint activities like the work of the Bureau on the other: "In the absence of a purpose to monopolize, *or the compulsion that results from contract or agreement*, the individual certainly may exercise great freedom; but concerted action . . . presents a wholly different problem, and is forbidden when the necessary tendency is to destroy . . . competition[.]" (Emphasis added.)

Maple Flooring (1925) presented a closer call.[368] In that case, 22 sellers and shippers of maple, beech, and birch flooring, mostly based in Michigan, Minnesota, and Wisconsin, had formed the Maple Flooring Manufacturers' Association. The Association's activities included the computation and distribution to members of: (1) average cost information for all "dimensions and grades" of flooring, (2) freight rates from Cadillac, MI, to many destinations throughout the United States; and (3) sales, price, and stock-on-hand information *in anonymized form only* (*i.e.*, revealing no specific information about any identifiable member). No agreement on production or prices was alleged or proved, nor was there any "direct proof" that the association's activities had increased

[366] American Column & Lumber Co. v. United States, 257 U.S. 377 (1921).
[367] United States v. American Linseed Oil Co., 262 U.S. 371 (1923).
[368] Maple Flooring Mfrs. Ass'n v. United States, 268 U.S. 563 (1925).

prices. In fact, there was "undisputed evidence that the prices of members were fair and reasonable and that they were usually lower than the prices of nonmembers[.]" The Section 1 challenge was aimed at "the plan of the association itself," on the theory that it was unlawful "regardless of its actual operation and effect so far as price maintenance is concerned." DOJ argued that the joint activity, by its nature, necessarily would tend to keep prices near the reported cost levels.

The *Maple Flooring* Court agreed in principle with DOJ that the exchange of cost information among members, when combined with a calculated freight rate, *could* be the basis for inferring an actual underlying agreement to fix prices. But here the evidence did not support such an inference. The mere transmission of information alone was not invariably harmful: "Competition does not become less free merely because the conduct of commercial operations becomes more intelligent through the free distribution of knowledge," noted the Court: "[i]t was not the purpose or intent of the [Sherman Act] to inhibit the intelligent conduct of business operations[.]" The sharing of market information did not become unlawful "merely because the ultimate result of their efforts may be to stabilize prices or limit production *merely through a better understanding of economic laws and a more general ability to conform to them.*" (Emphasis added.) The costs of production and transportation were "legitimate subjects of inquiry and knowledge." Thus, while in some cases, information exchange "may be the basis of agreement or concerted action to lessen production arbitrarily or to raise prices," as it was in *American Column* and *American Linseed*, here—"in the absence of proof of such agreement or concerted action having been actually reached or actually attempted"—there was no basis to infer illegality or any harm to competition.

In *Container Corp.* (1969), by contrast, the Court needed barely a thousand words to condemn an agreement among manufacturers of corrugated containers—collectively representing 90% of all shipments from the Southeastern United States—to inform one another of the most recent price each had charged or quoted.[369] The effect of that practice appeared, unsurprisingly, to have had the effect "of keeping prices within a fairly narrow ambit." With capacity exceeding demand, and with market entry "easy," prices had been falling and, as a result of the challenged practice, appeared to have been "stabilized[,] though at a downward level." Condemning the practice as a violation of Section 1, the Court pointed out that the practice had had an "anticompetitive effect": it had resulted in the "limitation or reduction" of price competition, by stabilizing prices that were generally declining: and the Sherman Act prohibited "[stabilizing prices as well as raising them[.]" The Court (somewhat pointedly, given Justice Fortas's concurring opinion) did not make clear whether it was applying *per se* or rule-of-reason scrutiny.

In a concurring opinion, Justice Fortas expressly argued that the *per se* rule should not be applied to an agreement to exchange information. Proof of anticompetitive effect, under the rule of reason, was necessary: the mere "[t]heoretical probability" of competitive harm was not in his view enough to make the exchange of price information "so akin to price-fixing. . . as to deserve the per se classification. But, here, he concluded that such proof was available: the record indicated that the practice "did in fact substantially limit the amount of price competition." Justice Marshall's dissenting opinion (joined by two other members of the Court) also took the view that this was a rule-of-reason case: but denied that there was evidence of harm in the record! "On the contrary," he argued, "the evidence establishes that the information . . . was actually employed for the purpose of engaging in active price competition."

Finally, two cases in the 1970s made clear that when the target of Section 1 analysis is the information-sharing agreement, rather than an inferred underlying conspiracy to fix prices, the rule of reason generally applies. In *Citizens and Southern*—citing among other things to Justice Fortas' concurrence in *Container Corp.*—the Supreme Court directly stated that "the dissemination of price information is not itself a *per se* violation of the Sherman Act."[370] And in a footnote in *U.S. Gypsum*, the Court set up the frame for modern antitrust analysis of information sharing among rivals: "The exchange of price data and other information among competitors does not invariably have anticompetitive effects; indeed such practices can in certain circumstances increase economic efficiency and render markets more, rather than less, competitive. . . . [S]uch exchanges of

[369] United States v. Container Corp. of America, 393 U.S. 333 (1969).

[370] United States v. Citizens and Southern Nat. Bank, 422 U.S. 86, 113 (1975).

> information do not constitute a per se violation of the Sherman Act. A number of factors including most prominently the structure of the industry involved and the nature of the information exchanged are generally considered in divining the procompetitive or anticompetitive effects of this type of interseller communication. Exchanges of current price information, of course, have the greatest potential for generating anticompetitive effects and although not per se unlawful have consistently been held to violate the Sherman Act."[371]

So what do courts actually do today in the shadow of these decisions, when confronted with a complaint alleging that information sharing has harmed competition? Modern analysis is exemplified by then-Judge Sotomayor's 2001 opinion for the Second Circuit in *Todd*. Confronted with a detailed allegation that several major oil companies had agreed to exchange information in a manner that tended to suppress their wages for certain employees, and mindful of the *Gypsum* footnote described above, the court of appeals set out a crisp framework for the rule-of-reason analysis of information sharing.

Todd v. Exxon Corp.

275 F.3d 191 (2d Cir. 2001)

Judge Sotomayor.

[1] Plaintiff brought this action against fourteen major companies in the integrated oil and petrochemical industry, collectively accounting for 80–90% of the industry's revenues and employing approximately the same percentage of the industry's workforce. On behalf of herself and all other similarly situated current and former Exxon employees (the putative class), plaintiff alleges that defendants violated § 1 of the Sherman Act by regularly sharing detailed information regarding compensation paid to nonunion managerial, professional, and technical ("MPT") employees and using this information in setting the salaries of these employees at artificially low levels. Plaintiff seeks money damages and equitable relief pursuant to § 1 of the Sherman Act.

[2] Accepting the allegations in the complaint as true, as we must on this motion to dismiss, the facts of this case are as follows. Defendants instituted a system whereby they periodically conducted surveys comparing past and current MPT salary information and participated in regular meetings at which current and future salary budgets were discussed. The data exchanges were also accompanied by assurances that the information would be used in setting the salaries of MPT employees. Defendants' "Job Match Survey" created a common denominator to facilitate the comparison of MPT salaries. The survey used certain jobs at defendant Chevron as benchmarks. The other defendants would submit detailed information regarding the jobs at their companies that were most comparable to the Chevron benchmark jobs so that they could be matched. The survey compared the responsibilities and compensation packages offered by defendants for certain jobs and job types against those of the benchmark positions at Chevron. This survey was coordinated by defendants Unocal and Chevron. Chevron and Unocal each would meet with half of the other companies involved to develop matches to the benchmarks, and then would gather the information before submitting it to a third-party consultant, Towers Perrin. Towers Perrin compiled the information, then analyzed, refined, and distributed it to the defendants on diskettes and in the form of hard copies.

[3] Defendants' "Job Family Survey" provided the most current account of the compensation being paid in the industry. Each company submitted information on salaries actually paid in thirty different categories of jobs, or "job families," classified according to the nature of the work. . . .

[4] . . . [E]ach company was entitled to receive subsets of Job Family Survey data, consisting of salary information from as few as three companies at a time. Plaintiff alleges that Exxon used these subsets to compare its own salaries with those of six particular competitors, referred to as the "Six Majors." [. . .]

[5] Plaintiff contends that defendants' arrangement violated § 1 of the Sherman Act. According to the complaint, these violations had the purpose and effect of depressing MPT salaries paid by defendants. [. . .]

---

[371] United States v. U.S. Gypsum Co., 438 U.S. 422, 441 n.16 (1978).

[6] Section 1 of the Sherman Act prohibits "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations." Traditional "hard-core" price fixing remains per se unlawful . . . . If the plaintiff in this case could allege that defendants actually formed an agreement to fix MPT salaries, this per se rule would likely apply. Furthermore, even in the absence of direct "smoking gun" evidence, a horizontal price-fixing agreement may be inferred on the basis of conscious parallelism, when such interdependent conduct is accompanied by circumstantial evidence and plus factors such as defendants' use of facilitating practices. Information exchange is an example of a facilitating practice that can help support an inference of a price-fixing agreement.

[7] There is a closely related but analytically distinct type of claim, also based on § 1 of the Sherman Act, where the violation lies in the information exchange itself—as opposed to merely using the information exchange as evidence upon which to infer a price-fixing agreement. This exchange of information is not illegal per se, but can be found unlawful under a rule of reason analysis. [. . .]

[8] As plaintiff does not allege an actual agreement among defendants to fix salaries, we analyze plaintiff's complaint solely as to whether it alleges unlawful information exchange pursuant to this rule of reason. [. . .]

[9] The traditional horizontal conspiracy case involves an agreement among sellers with the purpose of raising prices to supracompetitive levels. The Sherman Act, however, also applies to abuse of market power on the buyer side—often taking the form of monopsony or oligopsony. Plaintiff is correct to point out that a horizontal conspiracy among buyers to stifle competition is as unlawful as one among sellers. [. . .]

[10] Plaintiff claims that MPT employees accumulate industry-specific knowledge that renders them more valuable to employers in the oil and petrochemical industry than to employers in other industries. . . . It is consistent with common sense and empirical research that employees' industry-specific experience may cause them to suffer a pay cut if forced to switch industries. [. . .]

[11] [P]laintiff is simply alleging that a slight decrease in salary by a hypothetical oligopsonist cartel in the oil/petrochemical industry would not cause MPT employees to leave the industry because they would have difficulty finding compensation fully reflecting the value of their experience elsewhere. At trial, plaintiff would have to prove this theory with economic evidence regarding the cross-industrial elasticity of MPT employees. [. . .]

[12] In sum, plaintiff's complaint alleges a plausible product market. [. . .]

[13] Market power defined as a percentage market share . . . is not the only way to demonstrate defendants' ability to depress salaries. . . .

[14] In this Circuit, a threshold showing of market share is not a prerequisite for bringing a § 1 claim. If a plaintiff can show an actual adverse effect on competition, such as reduced output, we do not require a further showing of market power. If, for example, the plaintiff in this case could prove that (1) defendants engaged in information exchanges that would be deemed anticompetitive . . . and (2) such activities did in fact have an anticompetitive effect on the market for MPT labor in the oil and petrochemical industry, we would not deny relief on the basis of market share figures. [. . .]

[15] The Supreme Court [has] explained that one of the two most prominent factors in the rule of reason analysis of a data exchange is the structure of the industry involved. Therefore, once the relevant market is defined, a court must analyze the structure of that market to determine whether it is susceptible to the exercise of market power through tacit coordination. As the district court explained, susceptible markets tend to be highly concentrated—that is, oligopolistic—and to have fungible products subject to inelastic demand. [. . .]

[16] The Supreme Court has found that data exchange can be unlawful despite a relatively large number of sellers. In [United States v. Container Corp. of America, 393 U.S. 333 (1969)], the Court used the oft-cited language that the industry was dominated by relatively few sellers. But in fact, the defendants in *Container Corp.* were eighteen firms controlling 90% of the market, defined as the sale of cardboard cartons in the Southeast. The Court nonetheless found the market sufficiently concentrated to support the finding of a violation. It is fairly clear that the reason the Court reached its holding despite the multiplicity of sellers was the specific

anticompetitive characteristics of the information exchange. Given that the market concentration in this case is not radically different from that in *Container Corp.*, and given that concentration is part of a rule of reason inquiry that also emphasizes the nature of the information exchanged, we do not think that fourteen companies sharing an 80–90% market share is so unconcentrated as to warrant a Rule 12(b)(6) dismissal where the nature of the exchanges appears anticompetitive. We also find it unsurprising that data exchange cases may involve a number of participants that begins to push the boundaries of oligopoly. These players are *most* in need of such data exchange arrangements in order to facilitate price coordination; a very small handful of firms in a more highly concentrated market may be less likely to require the kind of sophisticated data dissemination alleged in this case. [. . .]

[17] The inquiry [into fungibility] is one part of the question of whether the market is susceptible to the exercise of market power though tacit coordination. Fungibility is relevant on this point because it is less realistic for a cartel to establish and police a price conspiracy where it is difficult to compare the products being sold. . . .

[18] The question in this case is whether jobs at the various oil and petrochemical companies were comparable, or fungible enough so that the defendants could have used the exchanged information as part of a tacit conspiracy to depress salaries. [. . .]

[19] Plaintiff's complaint alleges in detail the sophisticated techniques defendants used to achieve a common denominator with respect to the compensation paid to their MPT employees. Defendants developed the Job Match Survey because they realized it was not functionally efficient simply to know what each others' employees were being paid unless they were able to horizontally match the various job classifications. . . .

[20] Plaintiff is thus on solid ground when she argues that defendants made their own employees' positions "fungible" for comparison purposes with those of their competitors. [. . .]

[21] Alongside the structure of the industry involved, the other major factor for courts to consider in a data exchange case is the nature of the information exchanged. There are certain well-established criteria used to help ascertain the anticompetitive potential of information exchanges. As part of the analysis, a court should consider, broadly speaking, whether it was of the sort in *American Column & Lumber Co. v. United States* or of that in *Maple Flooring Manufacturers Ass'n v. United States*. Applying the relevant criteria reveals anticompetitive potential in this case.

[22] The first factor to consider is the time frame of the data. The Supreme Court has made clear that exchanges of current price information, of course, have the greatest potential for generating anti-competitive effects and although not per se unlawful have consistently been held to violate the Sherman Act. The exchange of past price data is greatly preferred because current data have greater potential to affect future prices and facilitate price conspiracies. By the same reasoning, exchanges of future price information are considered especially anticompetitive.

[23] Plaintiff's complaint alleges that defendants exchanged past and current salary information, as well as future salary budget information. . . .

[24] In addition to the time frame, another factor courts look to is the specificity of the information. Price exchanges that identify particular parties, transactions, and prices are seen as potentially anticompetitive because they may be used to police a secret or tacit conspiracy to stabilize prices. Courts prefer that information be aggregated in the form of industry averages, thus avoiding transactional specificity.

[25] Two aspects of the information exchange at issue are problematic in this regard. First, although the salary information was aggregated and distributed by a third-party consulting firm, companies participating in the Job Family Survey received compensation data broken down to subsets consisting of as few as three competitors. . . . Second, at their meetings defendants discussed current and future salary budgets, including company-specific information, such that all participants learn[ed] where each other participant [was] going with its salary budget for the upcoming year or, if a participant's salary year had only recently begun, for that new year.

[26] Another important factor to consider in evaluating an information exchange is whether the data are made publicly available. Public dissemination is a primary way for data exchange to realize its procompetitive potential. . . .

[27] In the instant case, dissemination of the information to the employees could have helped mitigate any anticompetitive effects of the exchange and possibly enhanced market efficiency by making employees more sensitive to salary increases. No such dissemination occurred, however. The information was not disclosed to the public nor to the employees whose salaries were the subject of the exchange. [. . .]

[28] In sum, the "nature of the information exchanged" weighs against the motion to dismiss. The characteristics of the data exchange in this case are precisely those that arouse suspicion of anticompetitive activity under the rule of reason.

[29] An antitrust plaintiff must allege not only cognizable harm to herself, but an adverse effect on competition market-wide. . . [I]nformation exchange is not always anticompetitive and can enhance competition by making competitors more sensitive to each other's price changes, enhancing rivalry among them.

[30] The complaint in this case, however, points to anticompetitive effects the exchanges have had on MPT salaries market-wide, most particularly with respect to Exxon. Plaintiff specifically alleges that salary levels across the integrated oil and petrochemical industry have been artificially depressed because the information exchange has reduced competitive incentives. Moreover, Exxon has supposedly used the information . . . to reduce its salaries 4.1% between 1987 and 1994 in comparison to the Six Majors and to reduce its [relative salary index] in relation to the competition [by an amount quantified in the complaint]. . . . In her claim for relief, plaintiff again alleges that she received compensation materially below what she would have received in an uncontaminated marketplace.

[31] . . . [Although the defendants' salaries had been increasing year-on-year,] [t]he fact that Exxon increased its salaries each year would not defeat an allegation that those increases were lower than they would have been but for a conspiracy to stabilize prices. We understand the complaint as alleging a market where Exxon's salaries and those of the Six Majors continue to increase, but where the difference grows gradually smaller—a portrait of market stabilization. [. . .]

[32] For the reasons stated, we vacate the district court's grant of defendants' Rule 12(b)(6) motion to dismiss and remand for proceedings consistent with this opinion.

NOTES

1) In practice, information exchange among competitors—through trade and professional associations, trade publications, or informal contacts—is very common. Why do you think this is?
2) Justice Holmes, dissenting in *American Column*, objected that "I should have supposed that the Sherman Act did not set itself against knowledge—did not aim at a transitory cheapness unprofitable to the community as a whole because not corresponding to the actual conditions of the country." Does he have a point? Should the exchange of true factual information about current or past events be *per se* legal?
3) What do you make of the following proposition? "It should be *per se* illegal for competitors to privately exchange information about anything to do with their businesses. They don't need to do it, and a *per se* rule would make things clearer for businesses and more competitive for everyone. If they really must talk about 'market conditions,' nothing is lost and much is gained by making them do it in public."
4) Imagine you were asked to give one paragraph of advice to non-lawyer sales employees attending their first trade association meeting. They know nothing about the Sherman Act, antitrust, or microeconomics, and they ask you for clear, straightforward advice so they know what is off-limits. What do you tell them?

D. What Is "Inherently Suspect"? The Quick Look / Rule of Reason Boundary

As we saw in Chapter IV, courts have recognized that some restraints may be presumed to have an anticompetitive effect by reason of their nature. In *Board of Regents*, as you have already seen, the Court expressed the core principle in terms like the following:

> As a matter of law, the absence of proof of market power does not justify a naked restriction on price or output. To the contrary, when there is an agreement not to compete in terms of price or output, no elaborate industry analysis is required to demonstrate the anticompetitive character of such an agreement. Petitioner does not quarrel with the District Court's finding that price and output are not responsive to demand. Thus the plan is inconsistent with the Sherman Act's command that price and supply be responsive to consumer preference. We have never required proof of market power in such a case. This naked restraint on price and output requires some competitive justification even in the absence of a detailed market analysis. [. . .]
>
> [T]he NCAA television plan [at issue in *Board of Regents*] on its face constitutes a restraint upon the operation of a free market, and the findings of the District Court establish that it has operated to raise prices and reduce output. Under the Rule of Reason, these hallmarks of anticompetitive behavior place upon petitioner a heavy burden of establishing an affirmative defense which competitively justifies this apparent deviation from the operations of a free market.[372]

But the existence of this standard raises an obvious question: when, exactly, does joint conduct warrant this kind of treatment? The question is critical, given the high proportion of rule-of-reason cases that fail at step one. Quick look treatment—or equivalent standards like the FTC's "inherently suspect" classification—allows a plaintiff to satisfy this obligation by reference to the nature of the conduct, with the burden then shifting immediately to the defendant to produce procompetitive benefits.

Board of Regents was decided in 1984. Two years later, the concept of quick-look review was developed and reinforced in *Indiana Federation of Dentists*.

FTC v. Indiana Federation of Dentists

476 U.S. 447 (1986)

{*Eds.: In the following extract, some paragraphs have been broken up to make them easier to read.*}

Justice White.

[1] Since the 1970's, dental health insurers . . . have attempted to contain the cost of dental treatment by, among other devices, limiting payment of benefits to the cost of the "least expensive yet adequate treatment" suitable to the needs of individual patients. Implementation of such cost-containment measures, known as "alternative benefits" plans, requires evaluation by the insurer of the diagnosis and recommendation of the treating dentist, either in advance of or following the provision of care. In order to carry out such evaluation, insurers frequently request dentists to submit, along with insurance claim forms requesting payment of benefits, any dental x rays that have been used by the dentist in examining the patient as well as other information concerning their diagnoses and treatment recommendations. . . . On the basis of the materials available, supplemented where appropriate by further diagnostic aids, [a] dental consultant may recommend that the insurer approve a claim, deny it, or pay only for a less expensive course of treatment.

[2] Such review of diagnostic and treatment decisions has been viewed by some dentists as a threat to their professional independence and economic well-being. In the early 1970's, the Indiana Dental Association, a professional organization comprising some 85% of practicing dentists in the State of Indiana, initiated an

---

[372] NCAA v. Board of Regents of the University of Oklahoma, 468 U.S. 85 (1984).

aggressive effort to hinder insurers' efforts to implement alternative benefits plans by enlisting member dentists to pledge not to submit x rays in conjunction with claim forms. The Association's efforts met considerable success: large numbers of dentists signed the pledge, and insurers operating in Indiana found it difficult to obtain compliance with their requests for x rays and accordingly had to choose either to employ more expensive means of making alternative benefits determinations (for example, visiting the office of the treating dentist or conducting an independent oral examination) or to abandon such efforts altogether.

[3] By the mid-1970's, fears of possible antitrust liability had dampened the Association's enthusiasm for opposing the submission of x rays to insurers. In 1979, the Association and a number of its constituent societies consented to a Federal Trade Commission order requiring them to cease and desist from further efforts to prevent member dentists from submitting x rays. Not all Indiana dentists were content to leave the matter of submitting x rays to the individual dentist. In 1976, a group of such dentists formed the Indiana Federation of Dentists, respondent in this case, in order to continue to pursue the Association's policy of resisting insurers' requests for x rays. The Federation, which styled itself a "union" in the belief that this label would stave off antitrust liability, immediately promulgated a "work rule" forbidding its members to submit x rays to dental insurers in conjunction with claim forms. Although the Federation's membership was small, numbering less than 100, its members were highly concentrated in and around three Indiana communities: Anderson, Lafayette, and Fort Wayne. The Federation succeeded in enlisting nearly 100% of the dental specialists in the Anderson area, and approximately 67% of the dentists in and around Lafayette. In the areas of its strength, the Federation was successful in continuing to enforce the Association's prior policy of refusal to submit x rays to dental insurers.

[4] In 1978, the Federal Trade Commission issued a complaint against the Federation [alleging that the practice violated the antitrust laws.] . . . The Commission found that the Federation had conspired both with the Indiana Dental Association and with its own members to withhold cooperation with dental insurers' requests for x rays; that absent such a restraint, competition among dentists for patients would have tended to lead dentists to compete with respect to their policies in dealing with patients' insurers; and that in those areas where the Federation's membership was strong, the Federation's policy had had the actual effect of eliminating such competition among dentists and preventing insurers from obtaining access to x rays in the desired manner. These findings of anticompetitive effect, the Commission concluded, were sufficient to establish that the restraint was unreasonable even absent proof that the Federation's policy had resulted in higher costs to the insurers and patients than would have occurred had the x rays been provided. Further, the Commission rejected the Federation's argument that its policy of withholding x rays was reasonable because the provision of x rays might lead the insurers to make inaccurate determinations of the proper level of care and thus injure the health of the insured patients: the Commission found no evidence that use of x rays by insurance companies in evaluating claims would result in inadequate dental care. . . .

[5] The Federation sought judicial review of the Commission's order in the United States Court of Appeals for the Seventh Circuit, which vacated the order on the ground that it was not supported by substantial evidence. [. . .]

[6] . . . [T]he sole basis of the FTC's finding of an unfair method of competition was the Commission's conclusion that the Federation's collective decision to withhold x rays from insurers was an unreasonable and conspiratorial restraint of trade in violation of § 1 of the Sherman Act. Accordingly, the legal question before us is whether the Commission's factual findings, if supported by evidence, make out a violation of Sherman Act § 1. [. . .]

[7] Under our precedents, a restraint may be adjudged unreasonable either because it fits within a class of restraints that has been held to be "per se " unreasonable, or because it violates what has come to be known as the "Rule of Reason," under which the test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition.

[8] The policy of the Federation with respect to its members' dealings with third-party insurers resembles practices that have been labeled "group boycotts": the policy constitutes a concerted refusal to deal on particular terms with patients covered by group dental insurance. Although this Court has in the past stated that group

boycotts are unlawful per se, we decline to resolve this case by forcing the Federation's policy into the "boycott" pigeonhole and invoking the per se rule. As we observed last Term in Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co., 472 U.S. 284 (1985), the category of restraints classed as group boycotts is not to be expanded indiscriminately, and the per se approach has generally been limited to cases in which firms with market power boycott suppliers or customers in order to discourage them from doing business with a competitor—a situation obviously not present here. Moreover, we have been slow to condemn rules adopted by professional associations as unreasonable per se, and, in general, to extend per se analysis to restraints imposed in the context of business relationships where the economic impact of certain practices is not immediately obvious. Thus, as did the FTC, we evaluate the restraint at issue in this case under the Rule of Reason rather than a rule of per se illegality.

[9] Application of the Rule of Reason to these facts is not a matter of any great difficulty. The Federation's policy takes the form of a horizontal agreement among the participating dentists to withhold from their customers a particular service that they desire—the forwarding of x rays to insurance companies along with claim forms. While this is not price fixing as such, no elaborate industry analysis is required to demonstrate the anticompetitive character of such an agreement. A refusal to compete with respect to the package of services offered to customers, no less than a refusal to compete with respect to the price term of an agreement, impairs the ability of the market to advance social welfare by ensuring the provision of desired goods and services to consumers at a price approximating the marginal cost of providing them. Absent some countervailing procompetitive virtue—such as, for example, the creation of efficiencies in the operation of a market or the provision of goods and services—such an agreement limiting consumer choice by impeding the ordinary give and take of the market place, cannot be sustained under the Rule of Reason. No credible argument has been advanced for the proposition that making it more costly for the insurers and patients who are the dentists' customers to obtain information needed for evaluating the dentists' diagnoses has any such procompetitive effect.

[10] The Federation advances three principal arguments for the proposition that, notwithstanding its lack of competitive virtue, the Federation's policy of withholding x rays should not be deemed an unreasonable restraint of trade. First, . . . the Federation suggests that in the absence of specific findings by the Commission concerning the definition of the market in which the Federation allegedly restrained trade and the power of the Federation's members in that market, the conclusion that the Federation unreasonably restrained trade is erroneous as a matter of law, regardless of whether the challenged practices might be impermissibly anticompetitive if engaged in by persons who together possessed power in a specifically defined market.

[11] This contention, however, runs counter to the Court's holding in *National Collegiate Athletic Assn. v. Board of Regents of Univ. of Okla.* [468 U.S. 85 (1984)], that as a matter of law, the absence of proof of market power does not justify a naked restriction on price or output, and that such a restriction requires some competitive justification even in the absence of a detailed market analysis. Moreover, even if the restriction imposed by the Federation is not sufficiently naked to call this principle into play, the Commission's failure to engage in detailed market analysis is not fatal to its finding of a violation of the Rule of Reason. The Commission found that in two localities in the State of Indiana (the Anderson and Lafayette areas), Federation dentists constituted heavy majorities of the practicing dentists and that as a result of the efforts of the Federation, insurers in those areas were, over a period of years, actually unable to obtain compliance with their requests for submission of x rays. Since the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, proof of actual detrimental effects, such as a reduction of output, can obviate the need for an inquiry into market power, which is but a surrogate for detrimental effects. In this case, we conclude that the finding of actual, sustained adverse effects on competition in those areas where IFD dentists predominated, viewed in light of the reality that markets for dental services tend to be relatively localized, is legally sufficient to support a finding that the challenged restraint was unreasonable even in the absence of elaborate market analysis.

[12] Second, the Federation . . . argues that a holding that its policy of withholding x rays constituted an unreasonable restraint of trade is precluded by the Commission's failure to make any finding that the policy resulted in the provision of dental services that were more costly than those that the patients and their insurers

would have chosen were they able to evaluate x rays in conjunction with claim forms. This argument, too, is unpersuasive. Although it is true that the goal of the insurers in seeking submission of x rays for use in their review of benefits claims was to minimize costs by choosing the least expensive adequate course of dental treatment, a showing that this goal was actually achieved through the means chosen is not an essential step in establishing that the dentists' attempt to thwart its achievement by collectively refusing to supply the requested information was an unreasonable restraint of trade. A concerted and effective effort to withhold (or make more costly) information desired by consumers for the purpose of determining whether a particular purchase is cost justified is likely enough to disrupt the proper functioning of the price-setting mechanism of the market that it may be condemned even absent proof that it resulted in higher prices or, as here, the purchase of higher priced services, than would occur in its absence. Moreover, even if the desired information were in fact completely useless to the insurers and their patients in making an informed choice regarding the least costly adequate course of treatment—or, to put it another way, if the costs of evaluating the information were far greater than the cost savings resulting from its use—the Federation would still not be justified in deciding on behalf of its members' customers that they did not need the information: presumably, if that were the case, the discipline of the market would itself soon result in the insurers' abandoning their requests for x rays. The Federation is not entitled to pre-empt the working of the market by deciding for itself that its customers do not need that which they demand.

[13] Third, the Federation complains that the Commission erred in failing to consider, as relevant to its Rule of Reason analysis, noncompetitive "quality of care" justifications for the prohibition on provision of x rays to insurers in conjunction with claim forms. . . . The gist of the claim is that x rays, standing alone, are not adequate bases for diagnosis of dental problems or for the formulation of an acceptable course of treatment. Accordingly, if insurance companies are permitted to determine whether they will pay a claim for dental treatment on the basis of x rays as opposed to a full examination of all the diagnostic aids available to the examining dentist, there is a danger that they will erroneously decline to pay for treatment that is in fact in the interest of the patient, and that the patient will as a result be deprived of fully adequate care.

[14] The Federation's argument is flawed both legally and factually. The premise of the argument is that, far from having no effect on the cost of dental services chosen by patients and their insurers, the provision of x rays will have too great an impact: it will lead to the reduction of costs through the selection of inadequate treatment. Precisely such a justification for withholding information from customers was rejected as illegitimate in the *National Society of Professional Engineers* case. The argument is, in essence, that an unrestrained market in which consumers are given access to the information they believe to be relevant to their choices will lead them to make unwise and even dangerous choices. Such an argument amounts to nothing less than a frontal assault on the basic policy of the Sherman Act. Moreover, there is no particular reason to believe that the provision of information will be more harmful to consumers in the market for dental services than in other markets. Insurers deciding what level of care to pay for are not themselves the recipients of those services, but it is by no means clear that they lack incentives to consider the welfare of the patient as well as the minimization of costs. They are themselves in competition for the patronage of the patients—or, in most cases, the unions or businesses that contract on their behalf for group insurance coverage—and must satisfy their potential customers not only that they will provide coverage at a reasonable cost, but also that that coverage will be adequate to meet their customers' dental needs. There is thus no more reason to expect dental insurance companies to sacrifice quality in return for cost savings than to believe this of consumers in, say, the market for engineering services. Accordingly, if noncompetitive quality-of-service justifications are inadmissible to justify the denial of information to consumers in the latter market, there is little reason to credit such justifications here.

[15] In any event, the Commission did not, as the Federation suggests, refuse even to consider the quality-of-care justification for the withholding of x rays. Rather, the Commission held that the Federation had failed to introduce sufficient evidence to establish such a justification[.] [. . .]

[16] The factual findings of the Commission regarding the effect of the Federation's policy of withholding x rays are supported by substantial evidence, and those findings are sufficient as a matter of law to establish a violation of § 1 of the Sherman Act . . . .

* * *

In *California Dental*, the Supreme Court held that the Ninth Circuit and the FTC had been wrong to conclude that advertising restraints adopted by dental practitioners in California were sufficiently suspicious to warrant quick-look scrutiny. Do you agree?

California Dental Association v. FTC

526 U.S. 756 (1999)

Justice Souter.

[1] There are two issues in this case: whether the jurisdiction of the Federal Trade Commission extends to the California Dental Association (CDA), a nonprofit professional association {*Eds: we have excised this portion of the decision: it is enough to know that the FTC's power to enforce the antitrust laws through Section 5 of the FTC does not extend to nonprofit entities.*[373]}, and whether a "quick look" sufficed to justify finding that certain advertising restrictions adopted by the CDA violated the antitrust laws. We hold that the Commission's jurisdiction under the Federal Trade Commission Act (FTC Act) extends to an association that, like the CDA, provides substantial economic benefit to its for-profit members, but that where, as here, any anticompetitive effects of given restraints are far from intuitively obvious, the rule of reason demands a more thorough enquiry into the consequences of those restraints than the Court of Appeals performed.

[2] The CDA is a voluntary nonprofit association of local dental societies to which some 19,000 dentists belong, including about three-quarters of those practicing in the State. . . .

[3] The dentists who belong to the CDA through these associations agree to abide by a Code of Ethics (Code) including the following . . . :

> Although any dentist may advertise, no dentist shall advertise or solicit patients in any form of communication in a manner that is false or misleading in any material respect. In order to properly serve the public, dentists should represent themselves in a manner that contributes to the esteem of the public. Dentists should not misrepresent their training and competence in any way that would be false or misleading in any material respect.

[4] The CDA has issued a number of advisory opinions interpreting this section, and through separate advertising guidelines intended to help members comply with the Code and with state law the CDA has advised its dentists of disclosures they must make under state law when engaging in discount advertising. [. . .]

{*Eds: The CDA's advertising guidelines directed that any advertisement offering a discount must specify the dollar amount of the non-discounted fee, the amount and duration of the discount, and any conditions or restrictions. CDA advisory opinions stated that any price advertising "shall be exact, without omissions, and shall make each service clearly identifiable, without the use of such phrases as 'as low as.'" CDA advisory opinions also disfavored quality claims, stating that such claims "are not susceptible to measurement or verification" and hence "are likely to be false or misleading." Local dental societies enforced the Code, including CDA guidelines and advisory opinions interpreting the Code. Applicants for CDA membership who violated the advertising restrictions could be denied membership. CDA members who violated the advertising restrictions faced suspension or expulsion from CDA.*}

[5] The Commission brought a complaint against the CDA, alleging that it applied its guidelines so as to restrict truthful, nondeceptive advertising, and so violated § 5 of the FTC Act The complaint alleged that the CDA had unreasonably restricted two types of advertising: price advertising, particularly discounted fees, and advertising relating to the quality of dental services. An Administrative Law Judge (ALJ) held the Commission to have jurisdiction over the CDA. . . . He found that, although there had been no proof that the CDA exerted market power, no such proof was required to establish an antitrust violation . . . since the CDA had unreasonably prevented members and potential members from using truthful, nondeceptive advertising, all to the detriment of both dentists and consumers of dental services. He accordingly found a violation of § 5 of the FTC Act.

[6] The Commission adopted the factual findings of the ALJ except for his conclusion that the CDA lacked market power, with which the Commission disagreed. The Commission treated the CDA's restrictions on

[373] *See infra* § XI.B.

discount advertising as illegal *per se.* In the alternative, the Commission held the price advertising (as well as the nonprice) restrictions to be violations of the Sherman and FTC Acts under an abbreviated rule-of-reason analysis. . . .

[7] The Court of Appeals for the Ninth Circuit affirmed, sustaining the Commission's assertion of jurisdiction over the CDA and its ultimate conclusion on the merits. The court thought it error for the Commission to have applied *per se* analysis to the price advertising restrictions, finding analysis under the rule of reason required for all the restrictions. But the Court of Appeals went on to explain that the Commission had properly applied an abbreviated, or "quick look," rule of reason analysis designed for restraints that are not per se unlawful but are sufficiently anticompetitive on their face that they do not require a full-blown rule of reason inquiry. [. . .]

[8] The Court of Appeals treated as distinct questions the sufficiency of the analysis of anticompetitive effects and the substantiality of the evidence supporting the Commission's conclusions. Because we decide that the Court of Appeals erred when it held as a matter of law that quick-look analysis was appropriate . . . we do not reach the question of the substantiality of the evidence supporting the Commission's conclusion.

[9] In *National Collegiate Athletic Assn. v. Board of Regents of Univ. of Okla.,* 468 U.S. 85 (1984), we held that a "naked restraint on price and output requires some competitive justification even in the absence of a detailed market analysis." Elsewhere, we held that no elaborate industry analysis is required to demonstrate the anticompetitive character of horizontal agreements among competitors to refuse to discuss prices, *National Soc. of Professional Engineers v. United States,* 435 U.S. 679, 692 (1978), or to withhold a particular desired service, *FTC v. Indiana Federation of Dentists,* 476 U.S. 447, 459 (1986). In each of these cases, which have formed the basis for what has come to be called abbreviated or "quick-look" analysis under the rule of reason, an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets. In *National Collegiate Athletic Assn.,* the league's television plan expressly limited output (the number of games that could be televised) and fixed a minimum price. In *National Soc. of Professional Engineers,* the restraint was an absolute ban on competitive bidding. In *Indiana Federation of Dentists,* the restraint was a horizontal agreement among the participating dentists to withhold from their customers a particular service that they desire. As in such cases, quick-look analysis carries the day when the great likelihood of anticompetitive effects can easily be ascertained.

[10] The case before us, however, fails to present a situation in which the likelihood of anticompetitive effects is comparably obvious. Even on Justice Breyer's view that bars on truthful and verifiable price and quality advertising are *prima facie* anticompetitive, and place the burden of procompetitive justification on those who agree to adopt them, the very issue at the threshold of this case is whether professional price and quality advertising is sufficiently verifiable in theory and in fact to fall within such a general rule. Ultimately our disagreement with Justice Breyer turns on our different responses to this issue. Whereas he accepts . . . that the restrictions here were like restrictions on advertisement of price and quality generally, it seems to us that the CDA's advertising restrictions might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition. The restrictions on both discount and nondiscount advertising are, at least on their face, designed to avoid false or deceptive advertising in a market characterized by striking disparities between the information available to the professional and the patient. In a market for professional services, in which advertising is relatively rare and the comparability of service packages not easily established, the difficulty for customers or potential competitors to get and verify information about the price and availability of services magnifies the dangers to competition associated with misleading advertising. What is more, the quality of professional services tends to resist either calibration or monitoring by individual patients or clients, partly because of the specialized knowledge required to evaluate the services, and partly because of the difficulty in determining whether, and the degree to which, an outcome is attributable to the quality of services (like a poor job of tooth filling) or to something else (like a very tough walnut). Patients' attachments to particular professionals, the rationality of which is difficult to assess, complicate the picture even further. The existence of such significant challenges to informed decisionmaking by the customer for professional services immediately suggests that advertising restrictions arguably protecting patients from misleading or irrelevant advertising call for more than cursory treatment as obviously comparable to classic horizontal agreements to limit output or price competition.

[11] The explanation proffered by the Court of Appeals for the likely anticompetitive effect of the CDA's restrictions on discount advertising began with the unexceptionable statements that "price advertising is fundamental to price competition," and that "[r]estrictions on the ability to advertise prices normally make it more difficult for consumers to find a lower price and for dentists to compete on the basis of price." The court then acknowledged that, according to the CDA, the restrictions nonetheless furthered the "legitimate, indeed procompetitive, goal of preventing false and misleading price advertising." The Court of Appeals might, at this juncture, have recognized that the restrictions at issue here are very far from a total ban on price or discount advertising, and might have considered the possibility that the particular restrictions on professional advertising could have different effects from those "normally" found in the commercial world, even to the point of promoting competition by reducing the occurrence of unverifiable and misleading across-the-board discount advertising. Instead, the Court of Appeals confined itself to the brief assertion that the "CDA's disclosure requirements appear to prohibit across-the-board discounts because it is simply infeasible to disclose all of the information that is required," followed by the observation that "the record provides no evidence that the rule has in fact led to increased disclosure and transparency of dental pricing."

[12] But these observations brush over the professional context and describe no anticompetitive effects. Assuming that the record in fact supports the conclusion that the CDA disclosure rules essentially bar advertisement of across-the-board discounts, it does not obviously follow that such a ban would have a net anticompetitive effect here. Whether advertisements that announced discounts for, say, first-time customers, would be less effective at conveying information relevant to competition if they listed the original and discounted prices for checkups, X-rays, and fillings, than they would be if they simply specified a percentage discount across the board, seems to us a question susceptible to empirical but not *a priori* analysis. In a suspicious world, the discipline of specific example may well be a necessary condition of plausibility for professional claims that for all practical purposes defy comparison shopping. It is also possible in principle that, even if across-the-board discount advertisements were more effective in drawing customers in the short run, the recurrence of some measure of intentional or accidental misstatement due to the breadth of their claims might leak out over time to make potential patients skeptical of any such across-the-board advertising, so undercutting the method's effectiveness. It might be, too, that across-the-board discount advertisements would continue to attract business indefinitely, but might work precisely because they were misleading customers, and thus just because their effect would be anticompetitive, not procompetitive. Put another way, the CDA's rule appears to reflect the prediction that any costs to competition associated with the elimination of across-the-board advertising will be outweighed by gains to consumer information (and hence competition) created by discount advertising that is exact, accurate, and more easily verifiable (at least by regulators). As a matter of economics this view may or may not be correct, but it is not implausible, and neither a court nor the Commission may initially dismiss it as presumptively wrong.

[13] In theory, it is true, the Court of Appeals neither ruled out the plausibility of some procompetitive support for the CDA's requirements nor foreclosed the utility of an evidentiary discussion on the point. The court indirectly acknowledged the plausibility of procompetitive justifications for the CDA's position when it stated that "the record provides no evidence that the rule has in fact led to increased disclosure and transparency of dental pricing[.]" But because petitioner alone would have had the incentive to introduce such evidence, the statement sounds as though the Court of Appeals may have thought it was justified without further analysis to shift a burden to the CDA to adduce hard evidence of the procompetitive nature of its policy; the court's adversion to empirical evidence at the moment of this implicit burden shifting underscores the leniency of its enquiry into evidence of the restrictions' anticompetitive effects.

[14] The Court of Appeals was comparably tolerant in accepting the sufficiency of abbreviated rule-of-reason analysis as to the nonprice advertising restrictions. The court began with the argument that "[t]hese restrictions are in effect a form of output limitation, as they restrict the supply of information about individual dentists' services." Although this sentence does indeed appear as cited, it is puzzling, given that the relevant output for antitrust purposes here is presumably not information or advertising, but dental services themselves. The question is not whether the universe of possible advertisements has been limited (as assuredly it has), but whether the limitation on advertisements obviously tends to limit the total delivery of dental services. The court came closest to addressing this latter question when it went on to assert that limiting advertisements regarding quality

and safety "prevents dentists from fully describing the package of services they offer," adding that "[t]he restrictions may also affect output more directly, as quality and comfort advertising may induce some customers to obtain nonemergency care when they might not otherwise do so." This suggestion about output is also puzzling. If quality advertising actually induces some patients to obtain more care than they would in its absence, then restricting such advertising would reduce the demand for dental services, not the supply; and it is of course the producers' supply of a good in relation to demand that is normally relevant in determining whether a producer-imposed output limitation has the anticompetitive effect of artificially raising prices.

[15] Although the Court of Appeals acknowledged the CDA's view that "claims about quality are inherently unverifiable and therefore misleading," it responded that this concern "does not justify banning all quality claims without regard to whether they are, in fact, false or misleading." As a result, the court said, "the restriction is a sufficiently naked restraint on output to justify quick look analysis." The court assumed, in these words, that some dental quality claims may escape justifiable censure, because they are both verifiable and true. But its implicit assumption fails to explain why it gave no weight to the countervailing, and at least equally plausible, suggestion that restricting difficult-to-verify claims about quality or patient comfort would have a procompetitive effect by preventing misleading or false claims that distort the market. It is, indeed, entirely possible to understand the CDA's restrictions on unverifiable quality and comfort advertising as nothing more than a procompetitive ban on puffery.

[16] The point is not that the CDA's restrictions necessarily have the procompetitive effect claimed by the CDA; it is possible that banning quality claims might have no effect at all on competitiveness if, for example, many dentists made very much the same sort of claims. And it is also of course possible that the restrictions might in the final analysis be anticompetitive. The point, rather, is that the plausibility of competing claims about the effects of the professional advertising restrictions rules out the indulgently abbreviated review to which the Commission's order was treated. The obvious anticompetitive effect that triggers abbreviated analysis has not been shown. [. . .]

[17] Saying here that the Court of Appeals's conclusion at least required a more extended examination of the possible factual underpinnings than it received is not, of course, necessarily to call for the fullest market analysis. Although we have said that a challenge to a naked restraint on price and output need not be supported by a detailed market analysis in order to require some competitive justification, it does not follow that every case attacking a less obviously anticompetitive restraint (like this one) is a candidate for plenary market examination. The truth is that our categories of analysis of anticompetitive effect are less fixed than terms like "*per se*," "quick look," and "rule of reason" tend to make them appear. We have recognized, for example, that there is often no bright line separating *per se* from Rule of Reason analysis, since considerable inquiry into market conditions may be required before the application of any so-called "*per se*" condemnation is justified. . . . What is required . . . is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint. The object is to see whether the experience of the market has been so clear, or necessarily will be, that a confident conclusion about the principal tendency of a restriction will follow from a quick (or at least quicker) look, in place of a more sedulous one. And of course what we see may vary over time, if rule-of-reason analyses in case after case reach identical conclusions. For now, at least, a less quick look was required for the initial assessment of the tendency of these professional advertising restrictions. Because the Court of Appeals did not scrutinize the assumption of relative anticompetitive tendencies, we vacate the judgment and remand the case for a fuller consideration of the issue.

Justice Breyer, with whom Justice Stevens, Justice Kennedy, and Justice Ginsburg join, concurring in part and dissenting in part.

[18] . . . [I]n a rule of reason antitrust case the quality of proof required should vary with the circumstances, . . . what is required is an enquiry meet for the case, and that the object is a confident conclusion about the principal tendency of a restriction. But I do not agree that the Court has properly applied those unobjectionable principles here. In my view, a traditional application of the rule of reason to the facts as found by the Commission requires affirming the Commission-just as the Court of Appeals did below.

[19] The Commission's conclusion is lawful if its factual findings, insofar as they are supported by substantial evidence, make out a violation of Sherman Act § 1. To determine whether that is so, I would not simply ask whether the restraints at issue are anticompetitive overall. Rather, like the Court of Appeals (and the Commission), I would break that question down into four classical, subsidiary antitrust questions: (1) What is the specific restraint at issue? (2) What are its likely anticompetitive effects? (3) Are there offsetting procompetitive justifications? (4) Do the parties have sufficient market power to make a difference?

[20] The most important question is the first: What are the specific restraints at issue? [. . .]

[21] The Court of Appeals referred explicitly to some of the evidence that it found adequate to support the Commission's conclusions. It pointed out, for example, that the Dental Association's advisory opinions and guidelines indicate that descriptions of prices as "reasonable" or "low" do not comply with the Association's rule; that in "numerous cases" the Association advised members of objections to special offers, senior citizen discounts, and new patient discounts, apparently without regard to their truth; and that one advisory opinion expressly states that claims as to the quality of services are inherently likely to be false or misleading, all without any particular consideration of whether such statements were true or false.

[22] The Commission itself had before it far more evidence. It referred to instances in which the Association, without regard for the truthfulness of the statements at issue, recommended denial of membership to dentists wishing to advertise, for example, "reasonable fees quoted in advance," "major savings," or "making teeth cleaning inexpensive." It referred to testimony that "across-the-board discount advertising in literal compliance with the requirements 'would probably take two pages in the telephone book' and '[n]obody is going to really advertise in that fashion.'" And it pointed to many instances in which the Dental Association suppressed such advertising claims as "we guarantee all dental work for 1 year," "latest in cosmetic dentistry," and "gentle dentistry in a caring environment."

[23] Do each of the three restrictions mentioned have the potential for genuine adverse effects on competition? I should have thought that the anticompetitive tendencies of the three restrictions were obvious. An agreement not to advertise that a fee is reasonable, that service is inexpensive, or that a customer will receive a discount makes it more difficult for a dentist to inform customers that he charges a lower price. If the customer does not know about a lower price, he will find it more difficult to buy lower price service. That fact, in turn, makes it less likely that a dentist will obtain more customers by offering lower prices. And that likelihood means that dentists will prove less likely to offer lower prices. But why should I have to spell out the obvious? To restrain truthful advertising about lower prices is likely to restrict competition in respect to price-the central nervous system of the economy. The Commission thought this fact sufficient to hold (in the alternative) that the price advertising restrictions were unlawful *per se.* [C]f. *Socony-Vacuum* (finding agreement among competitors to buy "spot-market oil" unlawful *per se* because of its tendency to restrict price competition). For present purposes, I need not decide whether the Commission was right in applying a *per se* rule. I need only assume a rule of reason applies, and note the serious anticompetitive tendencies of the price advertising restraints.

[24] The restrictions on the advertising of service quality also have serious anticompetitive tendencies. This is not a case of "mere puffing," as the FTC recognized . . . [S]ome parents may . . . want to know that a particular dentist makes a point of "gentle care." Others may want to know about 1-year dental work guarantees. To restrict that kind of service quality advertisement is to restrict competition over the quality of service itself, for, unless consumers know, they may not purchase, and dentists may not compete to supply that which will make little difference to the demand for their services. That, at any rate, is the theory of the Sherman Act. And it is rather late in the day for anyone to deny the significant anticompetitive tendencies of an agreement that restricts competition in any legitimate respect, let alone one that inhibits customers from learning about the quality of a dentist's service. [. . .]

[25] The FTC found that the price advertising restrictions amounted to a naked attempt to eliminate price competition. It found that the service quality advertising restrictions deprive consumers of information they value and of healthy competition for their patronage. It added that the anticompetitive nature of these restrictions was plain. The Court of Appeals agreed. I do not believe it possible to deny the anticompetitive tendencies I have mentioned.

[26] We must also ask whether, despite their anticompetitive tendencies, these restrictions might be justified by other procompetitive tendencies or redeeming virtues. This is a closer question—at least in theory. The Dental Association argues that the three relevant restrictions are inextricably tied to a legitimate Association effort to restrict false or misleading advertising. The Association, the argument goes, had to prevent dentists from engaging in the kind of truthful, nondeceptive advertising that it banned in order effectively to stop dentists from making unverifiable claims about price or service quality, which claims would mislead the consumer.

[27] The problem with this or any similar argument is an empirical one. Notwithstanding its theoretical plausibility, the record does not bear out such a claim. The Commission, which is expert in the area of false and misleading advertising, was uncertain whether petitioner had even *made* the claim. It characterized petitioner's efficiencies argument as rooted in the (unproved) factual assertion that its ethical rule "challenges *only* advertising that is false or misleading." Regardless, the Court of Appeals wrote, in respect to the price restrictions, that "the record provides no evidence that the rule has in fact led to increased disclosure and transparency of dental pricing." With respect to quality advertising, the Commission stressed that the Association "offered no convincing argument, let alone evidence, that consumers of dental services have been, or are likely to be, harmed by the broad categories of advertising it restricts." Nor did the Court of Appeals think that the Association's unsubstantiated contention that claims about quality are inherently unverifiable and therefore misleading could justify banning all quality claims without regard to whether they are, in fact, false or misleading. [. . .]

[28] The upshot, in my view, is that the Court of Appeals, applying ordinary antitrust principles, reached an unexceptional conclusion. It is the same legal conclusion that this Court itself reached in *Indiana Federation*—a much closer case than this one. There the Court found that an agreement by dentists not to submit dental X rays to insurers violated the rule of reason. The anticompetitive tendency of that agreement was to reduce competition among dentists in respect to their willingness to submit X rays to insurers—a matter in respect to which consumers are relatively indifferent, as compared to advertising of price discounts and service quality, the matters at issue here. The redeeming virtue in *Indiana Federation* was the alleged undesirability of having insurers consider a range of matters when deciding whether treatment was justified—a virtue no less plausible, and no less proved, than the virtue offered here. The "power" of the dentists to enforce their agreement was no greater than that at issue here (control of 75% to 90% of the relevant markets). It is difficult to see how the two cases can be reconciled.

CASENOTE: The *1-800 Contacts* Litigation

In the Matter of 1-800 Contacts, Inc., 2018 WL 6078349 (F.T.C. 2018); 1-800 Contacts, Inc. v. FTC, 1 F.4th 102 (2d Cir. 2021)

In a more recent effort to apply quick-look analysis, the FTC was again knocked back. *1-800 Contacts* was an e-commerce case, in which the defendant contact lens retailer, 1-800 Contacts, discovered that its competitors were buying search advertising—that is, ad space alongside search engine results—that would be displayed when a user typed in "1-800 contacts" into the search bar. 1-800 Contacts sued these competitors on the theory that buying search advertising for this keyword was a form of trademark infringement. 1-800 Contacts then settled those infringement claims in agreements that included a commitment by each party to refrain from bidding on keywords including one another's trademarks and internet URLs in future.

The Commission, in an opinion by Chairman Simons, held that the restraints were inherently suspect and unlawful. Quoting *PolyGram* (discussed in Chapter IV), the Commission noted that "[i]nherently suspect conduct ordinarily encompasses behavior that past judicial experience and current economic learning have shown to warrant summary condemnation." And the settlements here met that standard: they "are, in essence, agreements between horizontal competitors to restrict the information provided by advertising to consumers when they search for 1-800 Contacts' trademark terms and URLs; consumers could have used that withheld information to compare and evaluate the prices and other features of competing online sellers. Ultimately, the effect of the advertising restrictions is to make information enabling consumer comparisons more difficult and costly to obtain." The Commission emphasized the importance of online search, and online search advertising,

as a forum for competition, as "the advertising is presented to a consumer at a time when the consumer is more likely to be looking to buy." It followed from this that "[b]ecause the Challenged Agreements restrict the ability of lower cost online sellers to show their ads to consumers, it is easy to see how an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets."

Commissioner Phillips dissented, emphasizing that "[t]he per se and inherently suspect standards are exceptional and their application is reserved for the most patently anticompetitive restraints." Unlike previous cases dealing with broad bans or limits on advertising, he argued, the trademark settlements in this case were of narrow application ("[t]hey do not restrict the content of advertisements that 1-800 Contacts or the counterparties can run in innumerable contexts, including in response to search queries.") and were related to a procompetitive justification (the protection of trademarks, a "competing federal policy"). He identified the Second Circuit's *Clorox* decision—Clorox Co. v. Sterling Winthrop, Inc., 117 F.3d 50 (2d Cir. 1997)—as support for the proposition that trademark settlements that limited competition should be analyzed under the full-blown rule of reason, not under an abbreviated approach.

On appeal, the Second Circuit agreed with Commissioner Phillips. "[I]f an arrangement might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition," the court explained, "more than a quick look is required." And the presence of a trademark interest here was decisive. "[T]he restraints at issue here could plausibly be thought to have a net procompetitive effect because they are derived from trademark settlement agreements. . . . As the [settlements] restrict the parties from running advertisements on [1-800-Contacts'] trademarked terms, they directly implicate trademark policy." Full rule of reason scrutiny was appropriate, and the Commission's record could not support liability on such a theory.

NOTES

1) Now that you have read *Board of Regents* (Chapter IV), *IFD,* and *California Dental*, what is the best way to understand the circumstances under which courts will apply a "quick look" analysis? Does the Second Circuit's opinion in *1-800-Contacts* add anything to that understanding, or does it merely apply it?
2) Given that quick-look review is really a way of discharging the plaintiff's burden at step one of a rule of reason analysis, to what extent are they really different rules at all?