I. Basic Concepts

A. Problems in Markets - Monopolies/Cartels - the American economic system is built on a free market. However, where businesses make cartels or hold monopolies they have the ability to disturb the market balance, the goal of antitrust protections is to prevent disruption to the market.

1. Interests in Antitrust Protection - The following are all concerns addressed by antitrust provisions:
   a) Consumer Welfare - more than just protecting the consumer from high prices, the goal of antitrust protections is to preserve consumer choice. Only by protecting choice is the market system actually working.
   b) Protect Small Business - occasionally the court has cited a desire to protect the mom & pop businesses from the Walmarts of the world through antitrust law – note that most economists would not view this as a valid goal.
   c) Fear of Big Business - fear that big business is inherently predatory and will attempt to divide up markets and form monopolies and oligopolies.

2. Schools of Thought - the law of antitrust is governed in part by economic theory, since the adoption of the Sherman Act in the 1910s, the world of economic theory has changed somewhat:
   a) Structural Analysis - popular in the 1930s – this theory looked at the size and shape of firms in particular markets.
   b) Neo-Classical Price Theory - or the “CHICAGO SCHOOL” economics now dominates the world of antitrust theory. This theory focuses on the relationship between price and cost and places strong faith in market and business freedom.

3. Types of Restraints - of concern are contracts made to restrain trade, through price or other means – there are essentially 3 types of restraints:
   a) Vertical Restraints - these are restraints between buyers and seller of goods at different levels – these are of concern because of the potential exclusion of other buyers or sellers. (exclusive deal contracts)
   b) Horizontal Restraints - these are restraints between buyers or between sellers at the same level – these are of concern because of the potential exclusion of other buyers or sellers. (concerted refusal to deal – boycott)
   c) Mergers - these will involve the integration of markets and may be vertical or horizontal. Such mergers are of concern where if allowed, they may create monopoly power or facilitate oligopoly power.

B. Common Law Prohibitions - the prohibition against monopolies, price fixing and other trade restraints had its origin in the common law, long before modern statutory protections.

1. Monopolies Illegal - (Case of Monopolies) – a state granted monopoly in playing cards was found illegal. This was based on a presumption that monopolies encourage higher prices & lower quality.
2. **Price Fixing Illegal** – (King v. Norris) - agreements to fix price (here on salt) were illegal regardless if the price is high or low – this is a *per se* prohibition. Such agreements cause unnatural forces in the market which cause evil.

3. **Ancillary Trade Restraints Allowed** – (Mitchel v. Renolds) – covenant not to compete upheld – where a trade restraint is made ancillary to a valid contract will be permitted where the *restraint is reasonable*.

C. **Modern Statutory Solutions**

1. **Sherman Act** - the goal of the act was to *codify common prohibitions on restraints of trade* and to give *access to federal courts* to those who make claims under such protections.

   a) **Section One – Agreements in Restraint of Trade** - “every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce... [is] illegal”

   b) **Section Two – Monopolies** – “every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce...shall be deemed guilty of a felony.”

   c) **Private Cause of Action** - the Act also creates a private cause of action for persons who can prove the were damaged by *antitrust actions*.

   d) **Remedies** - there are a broad variety of remedies available under the Act:

      1) **Injunctions** - the court may enjoin a party from performing some actions. This is referred to as a *conduct remedy* and is the most popular form where the government is the plaintiff.

      2) **Treble Damages** - the court may award treble damages under the statute (3x) – additionally the court may also award attorneys’ fees.

      3) **Divestiture** - the court may even order the equitable remedy of divestiture.

      4) **Criminal Penalties** - the act also has criminal provisions that may create personal liability for individuals in corporations.
2. **Clayton Act**- this act was later enacted to supplement the Sherman Act, this course will concern two sections of the act:

a) §3 – Foreclosing restraints

b) §7 - Mergers

3. **Robinson-Patman Act**- this act was passed to protect small business and limits the amount and nature of price discrimination that can be used by suppliers

4. **Exempted Businesses** – the statutes contain several exceptions of where the rules will not be applied to specific industries:

a) Baseball

b) Insurance Companies

c) Collective Bargaining – Labor Unions

**D. Defining “in Restraint of Trade”** - the Sherman Act by its plain language prohibits any contract in restraint of trade, a broad reading of this provision would invalidate essentially every business contract. As a result, the court has interpreted the Act more narrowly:

1. **Sherman Act Bars “Unreasonable Restraints”**- (US v. Trans-MO Freight – RR assoc. establishing rates found unreasonable) The court noted the Act should be read to invalidate only unreasonable restraints of trade. However, the court found the fixing of price is per se unreasonable.

2. **Restraint Upheld where Reasonable & ‘Merely Ancillary’**- (US v. Addyston Pipe & Steel) – the use of covenants-not-to-compete were upheld, so long as they were reasonable and ancillary to the contract. A contract for the main purpose of restraining trade is invalid, such restriction must be reasonable and ancillary to the agreement.

3. **‘Rule of Reason’ Applied to Restraint** – (Standard Oil – oil trust divested) – for the first time the court adopts a rule of reason to look at restraint of trade. Will look to see if the measure has business justification or not. Even with justification, may find unreasonable or unduly restrictive.

   a) Unification of Market = Prima Facie Unreasonable- where the restraint unifies power and control over the industry/market – there is a presumption of intent to monopolize or restrain trade.

   b) Divestment Remedy Used- this case is also the first where the court used the equitable power of divestment to order the company to break up into 5 separate parts.

**E. Economic Concepts**- the following are brief summaries of economic concept necessary to understand the market forces considered in antitrust cases:

1. **Ruinous Competition**- this is where competition is made to fierce – that every one is competing so vigorously that a profit cannot be made, in the long term this will bankrupt the industry. Courts are often unwilling to accept this as a defense,
note that the likely industries where this may occurs are ones with high fixed costs & extremely low variable costs. (e.g. airlines).

2. **Producers Produce Where MC = MR** – common to all economic models is that a producer will seek to maximize production at a profitable level – today this is a common assumption that producer attempt to maximize market share. This level is determined where Marginal Cost = Marginal Revenue – that is to say the cost of producing the next good is the same as the revenue received from it.

3. **Perfect Competition** - an economic pipe dream – this is the goal of the free market system, antitrust provisions are utilized to push the market towards this end:
   a) *Large Numbers of Buyers & Sellers* – key to this concept is a large number of participants in transactions such that no one actor can influence price. The seller is a price taker
   b) *Producer Has Flat Demand Curve* – since the producer cannot influence price, he faces a flat demand and produces where MC = MR = Demand.

4. **Problems of Monopoly Power** - where a monopoly exists, the free market forces normally present are ineffective, leading to bad consequences:
   a) *Small Number/One Producer*- a monopoly market is characterized by have a sole or small number of producers. As a result, producers are price setters, not price takers.
   b) *Producer Has Downward Sloped Demand Curve*- because the producer is the industry, he faces the aggregate curve is which is downward sloping. Because of the point of production, MC = MR Doesn’t = Demand.
   c) *Consequences to Monopoly Power*- because the demand line = MR where it meets w/MC, the monopolist does not produce at the most efficient point resulting in-
      1) **Higher Prices** - at the MR = MC point, price will be higher than it would be in a perfectly competitive market.
      2) **Lower Quality/Quantity** - also the quantity sold is less that would be in perfect market conditions, additionally, the monopolist has no incentive to try and keep up quality to assure continued demand.
      3) **Wealth Transfer to Producers** - artificially high prices cause by the “shortage” created by the monopoly creates monopoly profits – these profits are wealth transferred to producers.
      4) **‘Dead Weight’ Loss** - in an economic utility sense there is also loss – persons who would have bought the product at the competitive price, but were forced to settle for a substitute because of monopoly pricing.

II. **Monopolies – Sherman Act §2** - the Sherman Act broadly prohibits monopolies, however, having monopoly power itself is insufficient to constitute a violation. However, where a firm acts in an attempts to monopolize or has monopoly
power and maintains it through exclusionary or anti-competitive acts, then they will violate the Act.

A. Early Interpretations – U.S. v. Alcoa- (single aluminum producer in US found to violate §2) – unlike §1, no evidence is necessary of any attempt to fix prices to violate §2, this case established the base requirements for a violation of §1 specifically Market Power & Intent to Monopolize.

1. **Required Elements = Market Power & Intent** – in order to be considered to have monopoly power under §2, two elements must be show: there must be *market power & exclusionary or anti-competitive acts* this requires only *general intent to perform act & not to monopolize*.

2. **Power Over Price = Market Power**- market power is essentially the *defined as power over price* – where the act of the one producer may set price in the industry, this market power is *inferred from market share*.

3. **Market Power Based on Market Share**- the power over price is *inferred from market share*, there is no black/white line of when market share creates market power, but the following can be inferred:

   a) 90% = *Monopoly* – if a firm has 90% of the market it will be considered a monopoly.

   b) 60-64% = *Doubtful Monopoly* – if a firm has a market share below 2/3 of the market total it is unlikely the court will find it has monopoly power. Droback says 75% is a good rule of thumb.

   c) 30% = *Not Enough* – if the firm has less than a third of the market, there should not be a finding of monopoly market power.

4. **Key = Market Definition**- the key to a finding of market power is the actual definition of the market – the broader defined, the more likely the percentage of the market of a particular firm will not be sufficient to have monopoly power. Markets are defined by looking at the following (see infra II.B)

   a) **Product Market & Geographic Market**- the market is defined by looking at the product and the geographic area – the defendant will want to define as broad as possible – (here all aluminum v. virgin aluminum sales) and a broad geographically (as whole US, rather than region, etc.).

   b) **Elasticity of Demand**- determining the breadth of a product market may be determined by looking at the elasticity of demand – elasticity is the *effect of a change in price on demand* – this depends on the *availability of adequate substitute products*.

   c) **Cross-Elasticity of Demand**- if a small change in price of product A, cause a large change in demand to Product B – then B is a good substitute of A, and the market definition should include A + B. However if a change in price of A doesn’t affect demand for B, it is not a substitute and should not be considered in market definition. *If high cross-elasticity = no power over price*. 
d) **Cross-Elasticity of Supply - Barriers to Entry** - the court will also look at how quickly a new firm could enter the market when considering market power – the higher the cost or longer time to entry, the less likely the court would consider the firm in a market definition.

5. **Intent to Monopolize = Low Threshold** - the court require *conducts by the defendant* that is intended to perform act that *create or maintain monopoly power*, this is typical through *exclusionary conduct or anti-competitive acts*. By the courts actions in Alcoa, it seems that it doesn’t take much to meet the intent requirement. *You can do everything honestly & fairly and still violate §2.*

   a) **Where Monopoly “Thrust Upon” = No Violation** - the intent requirement is inferred from the language of the act, the court makes clear that where a firm has monopoly power thrust upon them without any attempt to gain or maintain it, they are not liable under §2.

   b) **Defendant Burden to Prove Not Abuse** - once the plaintiff has proved the existence of monopoly power, the burden is on the defendant to demonstrate that the power was “thrust upon them” and not the product of anti-competitive conduct.

   c) **General Intent is all that is required** – in order to be liable under section 2, a firm *must only intend to perform the acts* that result in liability, there does not need to be proof of an overall attempt to monopolize.

6. **Anti-Competitive Conduct Necessary** - although it is a low threshold, the court still required some measure of anti-competitive conduct in order for §2 liability to attach - in Alcoa, the court found the following anti-competitive-

   a) **Increasing Production Capacity to meet all demand** - here there was evidence that Alcoa would only attempt to stimulate demand to the point it could satisfy it. This can be termed “predatory supply”

   b) **Kept Creating Excess Capacity = barrier to entry** – Alcoa maintain excess capacity so it could met any increase in demand before any competitor could enter the market.

B. **Importance of Market Definition – US v. Du Pont** – the court here found that Du Pont did not have monopoly power here despite control of 75% of market for cellophane, because made up only 20% of flexible packing material. Proving that antitrust cases are often won and lost at the market definition stage. Most believe this case was *incorrectly decided.*

1. **Dissent – Cross-Elasticity at Monopoly Price** – the dissent point out that demand that is inelastic will become elastic again once the monopoly price is passed – here Du Pont kept right around monopoly price. Creates illusion firm doesn’t have power over price.

2. **Demand Side Theory** - this focuses on *how many buyers will leave market if price is raised?* In this focuses on cross-elasticity of demand.

3. **Supply Side Theory** - this focuses on *home many sellers will enter if price is raised?* This looks are cross elasticity of supply – specifically barriers to entry, available substitutes, and geographic diversion.
4. **Sub-market Concept**- note that where a brand name good is differentiated enough (like arguably here), the product may be defined as its own market. Droback doesn’t like this, but it is good law.

III. **Conduct by Dominant Firms**- even if a firm has lawfully or naturally created monopoly, the use of that power to put competitors at a disadvantage, to foreclose competition, etc. is unlawful under the Act. The court has broadly held monopoly power as illegal under the act where it has “some effect” on competitors. Specifically the court want to make sure that the dominant firm is competing based on merit rather than market power.

   A. **Leveraging Markets**- leveraging is using monopoly power in one market to attempt to disadvantage competitors in a competitive situation. This is viewed as an illicit purpose – monopoly power cannot be used to attempt to create more monopoly power. (US v. Griffith – defendant owns movies theaters in competitive cities and in monopoly setting – using a leverage violated §2)

   B. **Exclusionary Conduct** – a monopolist may not attempt to maintain monopoly power by conduct that it intended to exclude competitors. (US v. United Shoe – conduct of only leasing machines found exclusionary under §2, controlled 80% of market) The court found the particular practices to be without valid business justification and designed to exclude conduct-

      1. **Barrier to Entry - Prevent Secondary Market**- here the manufacturer refused to sell the machines it made, and would only lease them. This effectively prevented a barrier to entry in the creation of a secondary market in used machines. (court rejected argument that consumers couldn’t afford to buy, but only lease – no reason to prohibit selling).

      2. **Bundling/Tying Products**- bundled services with the lease of machines, refused to sell service separately.

      3. **Cross-Subsidization - Price Discrimination** – company charged higher prices for machines with no competing machines on market and lower prices for machines with competition – used monopoly profits to have artificially lower prices for competitive goods.

      4. **Remedy** = note that court here disfavors divestiture – here the court ordered a conduct remedy, requiring the terms of leases to be altered and allowing sales.

   C. **Attempt to Monopolize**- §1 also makes attempts to monopolize illegal. The statute directs itself against the probability as well as against the completed result. (US v. Swift – meat companies wouldn’t bid against each other, set prices)

      1. **Required Elements**

         a) **Anti-Competitive Conduct**- this is an act of the nature described above and subsequently. The act must be unfair attempts – i.e. through other than business acumen.

         b) **Specific Intent to Monopolize**- this is a higher standard that the general intent of actual monopoly, there must be specific intent to monopolize, may still be inferred from act.
c) Dangerous Probability of Success - the plaintiff must also demonstrate that the relevant market - must show that there was a probably chance could have exerted market power.

2. Conspiracy to Monopolize – it is also illegal to combine or conspire to acquire/maintain the power to exclude competitors – this does not require an act actually be performed – the agreement itself is enough. This can be seen as a violation of §1 and §2. (American Tobacco)

D. Duty to Deal - ordinarily a company is under no obligation to sell another company, however, refusal to deal with another company or competitor may be an antitrust violation where there is “valid business justification.”

1. Refusal to Deal - a business with monopoly power may not refuse to deal with another business in order attempt to disadvantage a competitor. (Lorain Journal v. US – newspaper refused to sell ads to TV advertisers – violated §2).

2. Essential Facilities Doctrine - if a group of competitors or sole competitor create a facility that gives them a significant competitive advantage over excluded competition, is some situations, access must be afforded to the excluded parties on reasonable terms (Ottertail Power – refusal to wheel power violates §2). This doctrine is limited in scope, the conditions following must be met:

   a) Monopoly control over essential facility
   b) Inability of competition to reasonably duplicate or operate without facility
   c) Monopoly denies competition use of facility
   d) No business reason for denying use - this denial must not be based on business reasons (i.e. airlines denies competitor use of gate because it is using all the time).
   e) Dissent = Here valid business reason – here competition was seeking to eliminate Otter tail, no obligation to aid in own business demise.

E. Limits on Proximate Cause – Exclusionary Conduct – in order to be in violation of the Sherman Act, the alleged exclusionary contact must be done for some sort of benefit to the monopoly firm. Where action has no purpose to injure competition or expand the power of the monopolist, the conduct will not violate the Act. (Official Airlines Guide v. FTC – where act of monopolist does not give it an advantage – it is not “exclusionary” under the act.)

F. New Technologies - the goal of the antitrust act is to improve competition – with the development of new technologies, defendant began to argue that broad readings of the Alcoa doctrine would limit their ability to expand and meet new demands of global markets -

1. Invention & Innovation Doesn’t = Anti-Competitive - where the action by the defendant is the result of innovation or invention, the court is less likely to find a violation. This is a general policy to encourage innovation (Berkley Photo Inc. v. Eastman Kodak Co. – Kodak – introduces new camera w/new film and new processing = partially reversed as to violation §2) the actions of Kodak were challenged on several grounds:
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a) **Leveraging Illegal** – the court held that using monopoly power in one market to gain power in another, even if no monopoly power, will violate §2, this is a broad expansion of §2.

b) **No Duty to Disclose** – the court held as a matter of law Kodak had no duty to warn or competitors of

c) **Refusal to Sell Bulk Film/Chemicals** – may have duty to continue to deal – sell bulk film if decided not to continue to produce film that fit competitors cameras.

d) **Must Show Causation** – here in order to be eligible for damages, private party must prove causation – here never showed that actions of kodak = reduced sales.

2. **Efficiencies & Economics of Scale**- where a monopolist has a reasonable belief that market share will expand, he may expand production in anticipation to take advantage of efficiencies & economies of scale– the goal of the antitrust act is not to prevent the monopolist from competing *unfairly*. (DuPont (again) v. FTC – plant built in anticipation of increased demand for Titanium Oxide was justified).

a) **Possible Conflict w/Alcoa**- this may conflict w/Alcoa which held construction to preempt , FTC panel says here falls w/in “superior skill, foresight, and industry” exception to allow monopoly to be maintained.

b) **False Claims of Expansion will violate §2** – if a firm makes claims that it is planning to expand, but has no intent – because of potential coercive effect . Note that this could provide major loop hole – “Honestly, we thought there was going to an expansion, but it didn’t” to allow attempts to increase market share. May make good faith announcement and later change mind.

c) **False patent Claims May Violate §2** – if a firm makes fraudulent claims of patent, they are potentially liable in antitrust – again based on potential coercion of competitors.

d) **Here Low Price is from Scale not “Limit Pricing”** – limit pricing is the price where the monopolist still reaps monopoly profits, but is low enough that competitors will not enter the market.

G. **Predatory Practices**- a predatory conduct is any thing done by a dominate firm designed to drive out, discipline, or set back competitors by acts, that, but for their anti-competitive effect, would not be economically sensible for the dominant firm.

1. **Overview**-

a) **Chicago School Doesn’t Favor = Rare** – the Chicago school doesn’t find predatory practices a concern because they tend not to pay off. Before

b) **Government Doesn’t Like to Find Pricing Predatory** – clear evidence must be made that pricing is predatory – the government doesn’t

c) **Robinson-Patman Act** – prohibits price discrimination on wholesale, but not resale prices
d) **Clayton Act** – added to Sherman act to prevent discriminatory pricing. Has provision that prohibits tying of products.

e) **Primary Line Pricing** - this is price discrimination that is intended to harm other sellers

f) **Secondary Line Pricing** - this is price discrimination that is intended to harm other buyers.

2. **Predatory Pricing** - perhaps the most common form of predatory practice is predatory pricing or dumping – this is pricing below cost on the basis a competitor will be driven out of business - a war of attrition.

a) **Supreme Court Test = Below Cost & Dangerous Probability of Recouping** – cost is defined as an “appropriate measure of cost” this is the modern test. *Seems to suggest pricing above cost is per se legal.* (Brooke Group v. Brown & Williamson Tobacco).

1) **Recoupment Difficult to Prove** – the second part of the test has the effect of making it very difficult to prove that pricing is predatory.

2) **Consider New Market Participant** – the primary difficulty is a reliance on economic theory that before the firm could recoup losses from predation, a new firm would enter market to knock down prices – must show barriers to entry.

b) **Below Variable Cost = Predatory - Areeda/Turner Test** - this test focuses on if the pricing is below average variable costs, many court have held pricing below average variable costs is per se illegal as predatory.

c) **Ingles Test – 9th Circuit** – this is a burden shifting test that sets up the following situations based on Average Variable Cost/Average Total Cost

1) **Price Above ATC = Plaintiff Clear and Convincing Burden** – the court refuses to recognize prices over ATC as per se non-preditory.

2) **Price is Below ATC but above AVC = Plaintiff’s Burden**

3) **Price is Below AVC = Defendants Burden**

d) **Problem industries = High Fixed, Low Variable Costs** – this problem can be particularly evident in markets w/very high fixed cost but variable costs near zero – such as airlines & software.

e) **Acceptable Times to Price Below Cost** - this pricing strategy of items at below cost seems to be okay in three different situations -

1) **“Loss Leading”** – Wal-Mart strategy – pricing one item below cost to get consumers into store to purchase other items.

2) **Inventory Reduction** - “We over-stocked and everything must go!”

3) **Product Introduction** – cheap Pepsi One and Surge!
3. **Predatory Design Changes** - this activity is where a company changes its product for the sole reason of frustrating its competitors (generic IBM peripherals). Where a product change is only to raise competition barrier = violation.

   a) *If Superior/Innovative Product = Intent Immaterial* – however, if the product change improves the product, the intent of the producer – even if it is to screw the competitor, it is still okay. This includes cost savings, tech innovations, (Transamerica v. IBM)

   b) *Even if to make More Attractive* – even if the product is redesigned to appeal more to consumers, there is no duty of the producer to keep competitors apprised of design integration/changes.

H. **Duty to Continue to Dealing** - **Vertical Integration** – vertical integration occurs where a manufacturer/producer decides to eliminate the middleman and move into distribution/retail – instead of selling to a wholesaler. This raises an issue in antitrust based on a duty to continue dealing with other middlemen who the company sold to before. This is based on a duty to deal and leveraging principles.

   1. **Some Economic Theory = No Harm = Good business** – many economic theorist don't object to vertical integration because there is only one monopoly profit to be made, so integrating forward does nothing to harm consumer prices, in fact, because of economies of scale, they may even decrease prices. (Paschall v. KC Star – newspaper eliminates distributors = lower prices).

   2. **No Valid Business Reason = Must Continue to Deal** – refusal to deal will violate §2 if the firm doesn’t have a valid business reason for refusal to deal, essentially, where firm attempts to exclude rivals on grounds other than efficiency, behavior may be considered predatory (Aspen Skiing – where no reason to stop selling multi-resort passes – duty to continuing deal). *Narrow Situations = almost essential facilities.*

   3. **No Duty to Aid Competitors** - in general a monopoly has no duty to aid competitors – so a valid business reason is a broad escape of refusing to deal with competitors – where no consumer interests are affected and monopolist is not attempting to gain market advantage there is no violation. (Olympia Equip Leasing v. Western Union – WU liquidated remaining terminals to leave business – okay)

I. **Conduct Requirement - Differences Between Monopoly/Attempt** the requirement to violate the attempt provisions of section 2 are much higher than for a monopolist who has market power. Specifically, if there is no “dangerous proximity” to achieving a monopoly – even the most anti-competitive conduct will not violate the act.

   1. **Attempt = Must Have Dangerous Proximity of Success** - a company may perform extremely anti-competitive acts and not be liable under the Sherman Act where there is no dangerous proximity of success – i.e. barriers to entry are too low for a monopoly to be created (US v. Empire Gas).

   2. **Solicitation of Joint Monopoly = Attempt** - where there is a dangerous probability of success, attempt by one party to get another to split market and create a “joint monopoly” – will be considered attempt (would have been actual
monopoly if other party had agreed) (US v. A Airlines - AMR head attempts to get Braniff head to agree to split DFW market).

3. **Oligopoly Loophole**- note that in general the act makes no prohibition on the existence of oligopolies and doesn’t reach the “minuet of oligopoly” price raises.

**J. Summary – Anti-Competitive Actions**- the essential goal of the Sherman Act is to assure that monopolies are only acquired and/or maintained through superior business acumen, and not because of their power as monopolies. These case summarize 5 ways that firms compete on a non-merit basis:

1. **Predatory Conduct**- this is conduct that is injurious to the dominate firm, but the firm hopes to recoup costs after vanquishing their rival-
   
a)  *Pricing*- dumping product at below cost – war of attrition
   
b)  *Design Changes*- spending money to change product merely to frustrate competitors (Kodak, IBM)

2. **Leveraging Market Power**- this is using a monopoly power in one market in an attempt to gain power in another
   
a)  *Cross-Subsidizing* – charging more for monopoly product to absorb costs of producing a product with competitors allowing competitive product to be sold effectively below cost.
   
b)  *Tying Products*- market expansion may also be attempted by tying monopoly products to non-monopoly products.

3. **Refusal to Deal**- the monopoly may have a duty to deal w/competitors or customers where the only reason for refusing to deal is in order to assert market power-
   
a)  *Essential Facilities* - where a monopoly controls an essential facility – may have duty to allow competitor access for a reasonable fees. **VERY NARROW.**
   
b)  *Boycotting* - where monopoly refuses to deal with customer unless customer will deal exclusively with the monopolist.

4. **Exclusionary Conduct**- this is conduct that is designed to discourage new actors from entering the market by reducing their ability to be competitive against the monopolist.
   
a)  *Tying Products*– forcing consumer to buy bundles of goods & services in order to prevent secondary markets from being acquired by competitors.
   
b)  *Barriers to Entry* – making entry by another firm difficult by increasing costs of entering the market – (building excess capacity in factories, etc.)

5. **Merging/Integration** – eliminating competition by expanding market share and acquiring middlemen – such conduct is legal when done to increase efficiency, but not where only purpose is to increase market power.
IV. Horizontal Restraints of Trade–Sherman Act §1-

A. **Overview** - horizontal restraints are agreements between businesses *at the same level* – either producers or sellers, etc., who are typically competitors. Such restraints are regulated by §1 of the Sherman Act.

1. **Classification = Outcome Determinative** – the court has divided restraints of trade into two distinct categories – those that are subject to the rule of reason and those that are per se invalid (discussed below), this classification is often outcome determinative – per se are obviously invalid, restraints judged by the rule of reason are often upheld.

2. **Per Se Rule** – these are restraints that regardless of the intent of the parties.
   a) *Regulating Price* – agreements that effectively set price are judged by a per se rule.
   b) *Horizontal Market Division* – agreement to divide a market by competitors is also judged by the per se rule (Seller A sells to STL, Seller B to MSP, etc.)

3. **Rule of Reason** – these restraints are judged by looking if there is a justifying reason for the restraint and may be upheld by the court – particularly where the restraint is claimed to actually enhance competition.
   a) *Vertical Market Divisions* – discussed *infra* in section V.
   b) *Professional Societies/Organizations* – professional organizations that have membership requirements may be upheld as not violating antitrust laws.

4. **No Attempt Provision** – unlike §2, §1 doesn’t have an attempt provision, therefore there is no liability for attempting to fix prices where the other party doesn’t agree.

B. **Development of the Rule of Reason** – the Sherman Act does not create the rule of reason and per se distinctions that exist today – they are fashioned by court case law based on the fact that a literal reading of the Act would invalidate all contracts – clearly the intent of the act was only to limit *unreasonable restraints of trade*.

1. **Chicago Bd of Trade – Rule of Reason Established** – every contract re trains trade – the test of legality is whether the restraint imposed merely regulates and thereby promotes competition or whether it suppresses or destroys competition. *This is a very fact based analysis.* (Board of Trade v. US – restriction on trading hours upheld). Factors considered:
   a) *Nature of the Rule* – look at the reason for adoption of restraint – is any effect on competition ancillary to the goal of the restraint.
   b) *Scope of Rule* – is the restraint narrowly drafted to limit its effect
   c) *Effects of the Rule* – does the rule have any effect of stifling competition.
2. **Price Restrictions = Per Se Unreasonable** – agreements that set price are never considered to be reasonable by the court – they are no reasonable restraints on price. (US v. Trenton Potteries)

3. **More Lenient Where Competition Enhanced by Restraint** – in what has become an outlier case the – even in price cases – the court may consider if the effect of the restraint enhances rather than impedes competition. (Appalachian Coals v. US – In depression, agency to insure price floor in coal industry was reasonable to maintain profitability of agency).

4. **Don’t Need to Set Price to = Price Fixing** – a price fixing agreement does not actually have to agree on a fixed price so long as the agreement is made with the *intent of influencing price*, even if not done through setting price directly – here attempt was by control of supply. (Socony-Vacuum)

5. **Attempt to Influence Price = Price Restraint = Violate §1** – where an agreement is made with the intent of influencing prices regardless if the agreement has or could have any affect on price. Need only purpose, not power to fix price to violate §1. (Socony-Vacuum – Footnote 59).

C. **Modern Price Restraints**

1. **Intermediate Review - “Quick Look” Rule of Reason**- modern cases have seen the birth of the “quick look” rule of reason – a level of review that is in between rule of reason and per se. This rule is applied where per se rule is inappropriate, but where no elaborate industry analysis is required to demonstrate the anti-competitive character of an inherently suspect restraint. Most likely, restraints reviewed under this standard will be found invalid.

2. **Public Safety Rejected as Rational** – under this quick look, the court doesn’t look at other justifications for the restraint – the court rejected that argument that low prices can compromise safety – puts faith in competition. (Nat. Soc. of Engen. V. US – banning on bidding based on safety justification rejected as invalid- quick look review applied)

3. **Professional Organizations = Rule of Reason**- what the organization did in the instant case could have effectively been considered price-fixing, but the court was unwilling to apply per se rule to professional organization.

4. **Terms of Payment = Price Fixing = Per Se Rule**- where an agreement is made that sets the terms of payment, credit, interest, etc. between competitors – it is essentially an agreement on price and is judged by the per se rule (Catalano v. Target Sales – agreement between liquor wholesalers to eliminate short term credit invalidated by per se rule).

5. **Bundling/Set Prices Doesn’t Necessarily = “Price Fixing”**- blanket licensing of products that are bundled together and sold as a product may not be considered – here where product is *more than the sum of its parts*, and therefore is *increased efficiency* judged by the rule of reason rather than per se. (Broadcast Music v. CBS).

6. **Maximum Prices = Just as Illegal** – agreements between competitors setting maximum prices are also judged by a per se standard of review and are equally illicit under the Sherman Act. (Arizona v. Maricop Cty Med Soc. – maximum fee
schedule adopted by doctors invalidated – claim for bundling like Broadcast Music is rejected).

7. **Horizontal Market Division**- any agreement either explicitly or tacitly among businesses whereby the available market is divided up and each is given a share is per se illegal. (US v. Topco)
   
a) **Focus on Intra-brand rather than inter-brand of Competition**- here would only sell Topco brands, court does not even look at other brands products. It is unlikely that Topco agreement had any effect on price. Court rejects this argument on a Horizontal level.

b) **Applies Between Potential Competitors** – additionally agreements that are between potential competitors not to enter specific markets are also judged by the per se rule (Palmer v. BGR of GA – contract to exclusive license in GA in return for not entering state is invalidated under per se rule).

8. **Information on Price – Data Dissemination** – data on price is a double edged sword – by knowing competitors prices is allow for market competition by encouraging businesses to attempt to undercut prices – however information can also be used to fix prices. As a result – exchanges of pricing information are particularly suspect. However, in general they are examined under the rule of reason.

   a) **Market Structure - Few Sellers = Price Fixing = Per Se** – where there are few sellers in a market, the exchange of such data may be considered an implicit form of price. The court also noted that *price was only means of competition* in the instant case – all boxes the same, etc. (US v. Container Corp. of Amer. – specific exchange of specific data in narrow field judged by per se rule – illegal).

   b) **Where Not “Controlling Circumstance” = Not Per Se** – here seller claimed that buyers were lying as to the price of goods with other retailers. The court affirmed a commitment to evaluating by rule of reason based on the fact that unlike CCA above, price in this circumstance was not controlling. (US v. US Gypsum Co.) Additionally, the court noted a higher burden of proof exists for criminal cases:

   1) **Civil = Unlawful Purpose or Anti-competitive Effect**

   2) **Criminal = Mens Rea - Must prove intent - unlawful purpose**

   c) **High Risk Factors**- in particular the court will be likely to find such actions illegal in the presence of the following factors:

   1) **Exchange of Information about Current or Future Prices**

   2) **Exchange of Identity of Parties as well as Price**

   3) **Highly Concentrated Market w/Limited Number of Sellers**
d) *Avoiding Violation of Section 1* – as you might expect, if price data is exchanged, adopting the following.

1) **Use old price data**

2) **Aggregate Data** – by industry or producer – don’t give specific customers & specific prices

3) **Publish Info to Buyers** – the more persons to whom the information is available the less likely that a court will find evidence of price fixing.

e) *Inferring Price Fixing from Info Exchange* – in some cases, the court will infer that an agreement to fix price underlies the exchange to fix price.

1) **Evidence of Agreement = Per Se Rule** – where evidence exists that court may infer the date exchange is a part of an underlying agreement to fix price, it is judged by a per se rather than rule of reason. (Goldfarb v. VA state bar – bar published minimum fee schedule & influenced lawyers to follow)

2) “**Information Only” warning may be sufficient** – where information is regarding price is cushioned with warnings that the information is not intended to be followed by the other parties and independent pricing is encouraged, it may be upheld by the court (US v. Citizens & So. Nat. Bank – data on interest shared between banks – with info only warning attached)
9. **Product Standardization** - ever notice that all the candy bars are the same size? Often agreements exist between manufacturers explicitly between competitors regarding the nature & content of their products, while this can have pro-competitive affects by facilitating easy comparison – it also can lead to price fixin’. Courts look at the following to determine if the similarities are legal: (Pasta Problem)

a) Is the agreement facilitated by or does it facilitate a cartel?

b) Does the agreement lead to super-competitive or interdependent pricing?

c) Does the agreement limit customer choice through limiting nature and variety of product?

D. **Economic Boycotts – Concerted Refusals to Deal** - in general there is no obligation to deal with another business, however, where a group of individuals refuse to deal with one particular competitor, it will violate §1 of the Sherman Act. A boycott is defined as a concerted refusal to deal except on certain terms. Analysis in this area has been particularly difficult because courts have applied the rule of reason, per se rule, and quick look analysis in this situation.

1. ‘Blacklisting’ – in the eyes of the court there does not need to be a formal agreement to refuse to deal to be considered a boycott. Conspiracy can be inferred from the action of groups in concert. A harmless act when done by one can violate the act §1 where acting in concert as a conspiracy. (E. St. Lumber v. US – distributors who sell directly to retail w/o middleman were put on wholesaler blacklist)

2. Protecting Small Business – back in the day, the court may invalidate adhesive contract terms were a big business refuses to deal with another – such contracts may have the offending terms invalidated – it is doubtful this case would have the same outcome today. (Paramount v. US)

3. Self-Policing = Violate §1 – even if party’s actions violate unfair trade rules, others may not band together as a sort of self-policing policy – such actions would violate §1 (Fashion Originator’s Guild v. FTC – boycott by wholesalers of merchants who sold pirated dress patterns found illegal).

4. Vertical Conspiracies w/Horizontal Effects = Per Se Illegal – where vertical agreements are made by a competitor to excluded the vertical parties from dealing with a horizontal competitors – thereby restricting competitors supply. This was judged based on a per se rule – note that this sort of restraint had no effect on market – price or quantity – looking out for competitor – edge of §1 violations. (Klors v. Broadway Hale Stores – Klor’s conspired with suppliers to only deal w/Klor’s and not competitors.)

5. Modern Rule- Reason/Per Se - the decision of the Supreme Court in 1985 of *Northwest Wholesale Stationers v. Pacific Stationary* attempted to clarify the standard to be used for determining if boycotts violate section 1 of the Sherman act.

a) Per Se = Predominantly Anti-Competitive Effects – concerted refusals to deal are per se illegal when they involve joint efforts by a firm or firms to disadvantage
competitors by either directly denying or persuading/coercing suppliers/customers to deny relationships the competitors need in competitive struggle.

b) *Rule of Reason = Justified by Efficiency*- however, where a group is a *professional organization* formed for a purpose other than anti-competitive effects – here for greater purchasing power, etc. – their association may be subject to the rule of reason instead, but may still be found invalid.

6. **No Efficiency Justification = Illegal Under Rule of Reason** – *Quick Look* rule of reason was used to look at a restriction of dentists (professional organization) – however *without a efficiency justification* boycotts will not be upheld under a rule of reason analysis. (FTC v. Indiana Federation of Dentists – conspired to withhold x-rays from insurance companies). *Court reluctant to view professional orgs under per se rule.*

E. **Political Action Boycotts**- unlike economic restraints, concerted action by competitors designed to influence government action is not prohibited by the Sherman Act. The political action of the state immunizes the firms/persons for liability for antitrust violations.

1. **Noerr-Pennington Doctrine – Seeking Political Reform Okay** – efforts by groups to petition the government are protected by the doctrine – *even if they are undertaken for anti-competitive purposes*. This is based on an implicit right to petition the government for change. (E. RR Presidents Conf. v. Noerr Motor Freight)

a) *Doesn’t Apply to Agencies* – note the doctrine protects actions toward legislators or the executive, but doesn’t apply to attempts to influence agencies or courts.

b) *Doesn’t Apply to Private ‘Regulatory’ bodies-* efforts to influence the standard-setting process of private association not immune under the doctrine – even through standards are utilized by governments. (Allied Tube v. Indian Head – conspiracy to excluded competitors product from draft of National Fire Protection Association’s Code not protected).

2. **Sham Actions Not Protected** – however, if the attempt to influence is nothing more than harassment of a competitor or a mere shame the court may still find it in violation of §1. Where a lawsuit is filed and *no reasonable litigant could realistically expect success on the merits* the court may inquire if it conceals an attempt to interfere directly with a competitor’s business relationships. (Prof. RE Invest. v. Columbia Pictures – filing lawsuit w/no chance of winning = not protected).

3. **Political Motives = Not Subject to Sherman Act** – where a boycott is undertaken as a purely political motive, rather than economic, such as civil rights violations, etc. – it is not subject to regulation by the Sherman Act.

F. **Joint Ventures**- when companies pool resources to create professional organization or new entities that provide services to members – issues are created in antitrust as to if such organization constitute cartels designed to exclude competition or to foster it.

1. **Overview- Is it a joint venture?** of utmost concern of the court is if the collaboration is a *bona fide integration or merely cartel-like*. This *characterization*
is almost certainly outcome determinative because – the court will apply rule of reason analysis to the former and quick look or per se analysis to the latter.

2. **Analyzing Joint Ventures** – the court will look at a joint venture under the rule of reason – the court will ask the following three questions in determining if the joint venture is within the rule of reason:

   a) Is the integration achieved through the venture unreasonably anti-competitive?

   b) If the Integration is accompanied by related contractual restraints that have anti-competitive properties are they on balance anti-competitive?

   c) Will the venture confer such advantages on participants that they must grant access to the venture to outsiders in order to protect competition?

3. **Required Access to Venture** – in limited situations a joint venture may be compelled to deal with potential competitors in order to avoid being characterized as a group in restraint of trade -

   a) **Essential Facilities Revisited** – where a joint venture is the owner of facility that is essential to other competitors (limited situations) – they may be required to give – required more than equal access – must have ability to join venture. This was imposed as a prophylactic measure – no evidence of discrimination necessary. (US v. Terminal RR Assoc. of STL).

   b) **Restricted Memberships** – where a joint venture exists that has vast market power – it may have a duty to allow others to join on equal terms – here veto clause could prevent from joining - note that this balances return on entrepreneurial risk/reward v. competition. (AP v. US)

   c) **Factors in Considering** – in determining if access to a venture is required, the following should be considered-

      1) Is the facility truly essential?
      2) What are barriers to entry?
      3) Does venture impair competition?
4. **Contractual Restraints – Covenants Not to Compete** - these are restraints that are included in contracts in joint venture that a participant will not compete against another participate. The court will allow these restrictions in some areas-

   a) **Ancillary Restraint = Rule of Reason** – where the covenant not to compete is ancillary to the agreement rather than its motivating factor, the court will judge it by a rule of reason.

   b) **Lack of Market Power = Okay Under Rule of Reason** – if the parties market share is very small (here 5-6%) the court will find that the rule of reason is not violated by the restraint = no real balancing necessary.

**G. Proving Agreement - Evidence of Conspiracy** - clearly business aren’t always so stupid as to put in writing restraints of trade that have a potential to violate the Sherman Act – as a result a “conspiracy or agreement” must often be proved by circumstantial evidence. This section deals with what evidence is considered sufficient to establish the existence of such an agreement.

1. **Price Leadership - Conscious Parallelism** – where action of raising prices is quick matched by others in the field, the court may find this parallel pricing to be part of a conscious choice by the competitors = evidence of a tacit agreement to set price. (Interstate Circuit v. US).

2. **Conscious Parallelism Plus** – the court subsequently held that *conscious parallelism by itself is not illegal* – that in order to trigger liability – there needs to be the presence of some plus factor, these factors are unclear, but the court has cited the following: (Theatre Enterprises v. Paramount)

   a) **Circumstances Cast Suspicion** - secret meeting between business members – the proverbial “smoke-filled room”

   b) **Circumstances Unlikely to Mere Coincidence** - where there is blind bidding and 4 competitors all come up with the same exact bid.

   c) **Interdependence provided motive for common action - Rimless Wheel** - where the action taken by the leader would not make any economic sense unless was part of common action.

3. **Must Establish Anti-Competitive Intent –OR- Lack of Business Justification** – proving conspiracy was made harder by the addition of the requirement in addition to paralleling prices – the government must show anti-competitive intent or lack of business justification for the actions. (DuPont (AGAIN) v. FTC – inclusion of transportation cost & year long contract provisions in DuPont and sole competitors terms upheld).

**H. Oligopolies** - also referred to as “shared monopolies” is where a small number of firms control the market. However, since none of the firms individually have market power, they are not subject to §2 of the Sherman Act. Additionally, because of the few number of sellers – prices can be easily made public, price parallelism is possible and can evade possible liability under §1 of the Sherman Act. Essentially these firms have power over price and are unable to be reached by current laws.

**V. Vertical Restraints of Trade – Sherman Act §1** - vertical dealings are transactions between various levels of production and distribution - such as manufacture, wholesale and retail – vertical restraints are ones made between these two
different levels. These transactions are also regulated by Section 3 of the Clayton act and where monopoly power is implicated by §2 of the Sherman Act.

A.  Restrictions by Sellers Restricting Options of Buyers-

1. Resale Price Maintenance - Formal Agreement to Fix Price = Per Se Illegal – Dr. Miles – It is a per se violation of §1 for a seller to contractually set the price at which a buyer may sell the good. This applies whether it is a maximum or minimum price (see infra – maximum resale price). (Dr. Miles Medical Co. v. John Park)

   a)  Rational = Buyer Autonomy – at least one of the consideration of the court was that after title is passed to the buyer, he should be able to resell the product at whatever price he chooses.

   b)  Focus = Intra-brand Competition- again, RPM only affects intra-brand competition – so long as there are other substitute product, such practices have no effect on the price and choice of consumers – Dr. Miles would have to keep price low to keep from losing customers to other Alcohol-based cold remedies.

2. Avoiding Dr. Miles – Consignment – Manufactures countered the ruling in Dr. Miles by placing goods on consignment with retailers (retailer sells good, but manufacturers kept title until good is sold). These schemes were initially upheld (US v. GE), however, the tides turned. Where consignment is used to disguise fixing prices through retail outlets – it is illegal. (Simpson v. Union Oil Co – consignment found to be sham – risk of loss passed to retailer, but not title = illegal). Consignment agreements are looked at under rule of reason.

3. Unilateral Refusal to Sell- Colgate Exception – the next way manufacturers attempted to avoid the ruling against Dr. Miles was by unilaterally refusing to deal with retailers who didn’t follow their guidelines. This action was upheld by the court (US v. Colgate).

   a)  Rational = focus on manufacturer autonomy. This is based on the right of a business to choose who to sell to and who not to sell to.

   b)  Focus = Intra-Brand Competition – again, notice that these agreements only affect intra-brand competition.

   c)  Narrowing Colgate – Limit to Refusal to Deal – subsequent decisions have limited the scope of the Colgate rule – the action by the seller must be wholly unilateral and must not use any other means to effect adherence to the prices (such as coercion or wholesaler, etc.) – (US v. Parke Davis – refusal to deal with wholesalers who didn’t enforce retail prices on retailers found illegal.)

   d)  Testing the Limits of Colgate – when does “unilateral” become an agreement or coercive?

   1)  Warnings – if supplier gives warning before cutting off retailer – does that violate unilateral action requirement?
2) **Discounts** – what if supplier gives discounts to those who follow recommendations and takes them away from naughty resellers? Is this still unilateral – Drobak says gray area – best you don’t f*ck with da man!!

3) **Permanent Termination?** – if a supplier cuts of a retailer, how long after the termination can a retailer be added back without there being an implicit agreement on price?
e) **Proving Bi-Lateral Agreement – Complaints Plus Doctrine** – the agreement may be to exclude another reseller - a dealer is terminated by the seller after complaints of another dealer – the complaints alone will be insufficient to find an implicit agreement to fix price – and another factor or evidence is necessary – (Monsanto v. Spray-Rite – complaints of dealers about terminated dealer & newsletter on prices = sufficient to prove implicit agreement.)

4. **Dr. Miles Today = Still Good Law** – note that Congress has amended the antitrust provisions of the act several times and has never legalized the conduct prohibited by Dr. Miles. The DOJ has published guidelines in which it states it believes much of the conduct in Parke Davis was in fact unilateral – congress has criticized.

5. **Non-Price Restraints – Refusal to Deal – Terminating Discounters** – often a seller may requested by his buyer or unilaterally may not want to sell to a discounter – this is because of the “free ride” that discounter often take on full price resellers. These restraint decisions are judged under a rule of reason and are often upheld. (Busin. Electronics v. Sharp)

   a) **Must Not Include Agreement on price** – as long as the full price dealers and supplier don’t make an agreement on price (see Monsanto above) there is no application of the per se rule.

   b) **Measures Taken to Prevent Inference** – companies often as part of their reselling price policy place warnings that it is a unilateral policy and not to discuss it with the firm.

   c) ***Could = Horizontal Division*** – note that in Sharp – one competitor approached Sharp to try and get another terminated – but if two had done so, that would have been considered horizontal market restraint – an attempt by the 2 to divide the market and give rise to liability under §1.

   d) **Could = Monopoly Power** – if the merchant who approached the seller to attempt to terminate the other reseller had sufficient monopoly power – the action could be in violation of §2 as an attempt to use market power to exclude a competitor.

6. **Maximum Resale Price = Rule of Reason** – once judged the same as price floors, price ceilings are now judged under the rule of reason rather than the per se rule. This was based on a belief that price ceiling cannot be so injurious as to merit judgment by the per se rule. (State Oil Co. v. Kahn)

   a) **Potentially pro competitive** - In fact they were potentially pro-competitive.

   b) **Antitrust goal = Interbrand Competition** - how does this affect Dr. Miles?

7. **Standing & Injury Requirements for RPM & Maximum Resale Price Injury** – in order to be a successful private plaintiff a party must meet standing and antitrust injury requirements. The injury must stem from unfair competition – not regular competition or mere integration (Brunswick – manufacturer takes over local bowling alley – competitor sues – no antitrust injury)
a) *Injury Must Be Intended to be Prevented by Antitrust Laws*— even if the injury to the party is a result of the Antitrust violation of another — if the injury in not the type intended to be prevented by the law — here competitor injured by competition after violation occurred — then there is no antitrust injury — (Brunswick, Jack Walters v. Morton)

b) *Government Always meets standing*— note the government doesn’t have to meet the injury requirement and always has standing to sue under the act.

B. **Territorial, Consumer & Supplier Vertical Non-Price Restraints**— these are restraints that deal with franchising and other rights where the vertical provided may wish to maintain some control over the activities of the retailer — these restraints are typically looked at under the rule of reason.

1. **Early Rule = Post Sale Restraints = Per Se**— initially the courts followed the *Schwinn* rule — which made any post sale restriction subject to the per se rule. This was based on a policy of *buyer autonomy*.

   a) *Free Riding Problem*— note that this created a free riding problem that was unreachable by restraints — discounters profit from serves provided by full service dealers.

   b) *Consignment Avoidance*— sellers would attempt to avoid the Schwinn rule by giving goods to retailers on consignment rather than outright sale.

2. **All Non-Price Restraints = Rule of Reason — Continental TV v. GTE Sylvania**— in this case the court overturned the Schwinn rule and held that all vertical non-price restraints were subject to the rule of reason. This was based on the rational that such restraints only limit intra-brand competition, but foster inter-brand competition.

   a) *Large Market Power or Few Substitutes = Unreasonable*— the court cautions that where the firm possesses a large share of the market or there are a lack of substitutes, such restraints may violate the rule of reason.

   b) *Undermines Dr. Miles*— note that under the same logic, Dr. Miles would also be incorrectly decided, but it is still good law.

3. **Intra-brand Exclusive Selling Agreements = Rule of Reason**— a manufacturer is able under the rule of reason to establish exclusive agreements between reseller in certain areas etc. Note that this again only reduces intra-brand competition and would have little effect on consumers.

   a) *Influenced by retailer(s) may = per se violation*— it important to remember that if the manufacturer is possible horizontal division if the manufacturer terminates the retailer at the request of other retailers. Or if one retailer — may create §2 liability for retailer.

4. **Inter-brand Exclusive Dealer/Requirement Provisions = Invalid by §3 of Clayton Act**— these are contracts that impose limits on buyers — the retailer must buy all he needs from the one provider of a goods.
a) *Clayton Act §3* - this section condemns all sales/agreements when the *effect may be to substantially lessen competition* or tend to create a monopoly. This broadens the prohibitions of §1 and §2 of the Sherman Act. It is an *incipiency statute* – i.e. the conduct doesn’t have to be proved to actually reduce competition – only possibly effect. *Applies only to goods.*

b) *Don’t Need Effect to Violate - Incipiency Statute* - the agreement in question need only have the likelihood of substantially reducing competition – no actual effect needs to be shown for an agreement to violate it. (Standard Fashion v. Magrane-Houston – agreement barring other manufacturers patterns found in violation of §3).

c) *Foreclosure of Substantial Market Share = Violate §3* - the court has adopted a substantial market share test where size of the market share foreclosed by the contract is substantial – in terms of percentage, not money. The court considers other factors, such as barrier to entry. (Standard Oil v. US)

d) *De Facto Exclusive Dealing* – even if a contract doesn’t specifically state that it is exclusive, if the terms of such a contract are such that it would be considered effectively exclusive – then it will be treated as such (US v. Microsoft – Competitor pays per computer charge, regardless if computer shipped w/operating system).

e) *Factors In Determining Violation of §3* – in determining if the contract substantially forecloses the market – key to this determination is definition of the market – like §2 cases. (Tampa Electric Co. v. Nashville Coal – 20 year contract upheld because less than %1 of market foreclosed) Following are considered:

1) **Line of Commerce** - the nature of the business – are such contacts necessary for valid business reasons – efficiency. Additionally what is considered to be the This definition is key to finding of violation.

2) **Market Area** - part of market definition – midwest/national area.

3) **Competition Foreclosed** - does the seller have a dominate market position?

4) **Droback** = says 15% is a good rule of thumb.
C. **Tying Products** - also referred to bundling – tying involves taking one product which a buyer is eager to buy and making supply of the item conditional on the purchase of another item. (Tying product = desirable product, tied product = required purchase product) This sort of arrangement is also subject to §3 of the Clayton Act. *Note the Clayton act applies only to goods – not intangibles or other- such intangibles are covered by §1 of the Sherman Act.*

1. **Early Decisions = Market Power in Tying Product Key** - in early cases the court focused on if the tying agreement was “monopolistic in nature” – absent this threat, the court seemed unlikely to find that the agreement violated the Clayton Act (IBM v. US – tying use of IBM brand cards in tabulators leased – violated Clayton Act).

2. **What is ‘A Product’** – there can be an issues as to what exactly a single product is, rather than multiple products tied together. Court will look to if a business justification exists for considering the items one product. (US v. Jerrol Electronics – system sold as one product – competitors sold separately – court upheld as single product during start up).

3. **Market Power in Tying Product & Must Affect Tied Product Market** – where the seller has sufficient power in the market of the tying product to appreciably restrain free competition in the market for the tied product and a “not insubstantial” amount of interstate commerce is affected will be unreasonable per se. (Northern Pacific RR v. US)

4. **Modern Rule = Modified Per Se** – the court has subsequently clarified that the real evil in tying products is coercion of the buyer – *is the buyer forced into buying tied product?* As a result the court adopted a modification to the per se rule (Jefferson Parish Hosp v. Hyde – Hospital contracted with anesthesiology firm to provide all its needs for sleep inducing – per se unlawful to tie products, but here no coercion – not tying)

   a) **Per Se Rule if Tying = Forced Choice** – is seller’s exploitation of control over tying product to force buyer into buying tied product that he doesn’t want or would rather purchase elsewhere on different terms.

      1) **Market Power key** – in order for there to be any belief that the buyer was forced – the seller must have market power.

      2) **Purchase Separately Elsewhere = No Tying** – if products can be bought elsewhere separately - then probably tying is not illegal.
b) O’Connor- concurring – tying may in some situation be economically beneficial – should be judged by rule of reason.

c) Rule of Reason ? – concurring justices all wanted to judge by rule of reason standard – isn’t the modified per se rule approximately the same thing?

5. Service & Parts as Separate Product – a market for a good and for parts and services for the goods may be considered separate and distinct where consumer demand is such that it is efficient for a firm to provide service separate from parts. The defense of “quality control” may be considered – but was rejected here. (Kodak v. ITS)

6. Franchise Agreements- when a franchiser buys a McDonalds – he may be expected to but a number of other products – such as fryers, cups, potatoes from the franchiser – the issue arises whether such practices count as “tying” of products – or are claims that the franchise w/this stuff is one product or that the product restrictions is necessary to maintain good will, etc.

a) May define separately – where the court finds that such equipment is not necessary to be part of the franchise product, such practice will be considered tying and will be illegal (Siegel v. Chicken Delight – required purchase of fryers from franchiser constituted tying).

b) Where Business Purpose = Integrated Product – if the practice is such that it is required – here required to franchisee to use building provider by franchiser = assure quality/placement – no profit of building, only franchise. (Principe v. McDonald’s).

7. Modern Test- after these cases the following four part test can be distilled concerning product tying, allow of the following must be answered in the affirmative in order for the per se rule to be triggered, otherwise it will be judged by rule of reason:

a) Are there two products? – one product, there’s no issue

b) Does Seller have market power in tying product market?

c) Is there a “not unsubstantial” amount of commerce affected by the seller in the tied product market?

d) Is the power in the tying market used to prevent competition on the merits between products in the tied product market?

8. Available Defenses- the court does seem willing to accept some limited defenses to claim of tying products that may otherwise violated the test:

a) Single Product – obviously, the defendant can claim that there is no tying – that the whole item is one integrated product (Windows/Internet Explorer).

b) “New Industry” Defense – courts have excepted arguments that tying is necessary for an enterprise to begin a new business or product line.
c) “Quality Control” Defense - that the tied product is necessary to assure the quality and good will toward the tying product – typically this is a claim in parts/service and franchising cases – such a claim is rarely successful.

VI. Mergers – Clayton Act §7 – oh no!! Corporations rears its ugly head again – time for old learnin’ – mergers are of obvious antitrust concerns because of their ability to greatly alter the competition in a market. Specifically, mergers that increase efficiencies and therefore competition will be encourage while the law will frown on mergers that are for the sole purpose of increasing market power.

A. Overview

1. Clayton Act §7 – this provision applies in cases of merger and provides: “no corporation shall acquire another corporation where in any line of commerce in any sector of the country the effect of acquisition may be to substantially reduce competition or tend to create monopoly.”

   a) Incipiency Statute – again, the government doesn’t have to prove actual affect on market, only that the merger may be bad.

   b) §1 or §2 Liability - could also arise, drobak says beyond scope of exam.

2. Merger Guidelines of 1982 – initially propagated based on output-limitation principle, merger are to be prevented only if would create inefficiencies.

3. Government Must Pre-approve Large Mergers – under Har-Scott-Rodino Act, the government must approve larger mergers before they become effective – actually they have an period of time to object.

4. Types of Mergers- there are essentially three types of mergers that antitrust law is concerned with:

   a) Horizontal Mergers – these are mergers with other competitors and lead to more concentrated markets.

   b) Vertical Mergers – these are mergers between levels of producers and retailers – this is a concern because of possible foreclosure of market to potential competitors. If a supplier acquires a customer – other suppliers will not be able to sell to them anymore.

   c) Conglomerate Mergers – these mergers can only violate antitrust law where they eliminate an actual or perceived potential competitor.

5. Analyzing a Merger = probable market impact- the concern of the government is the impact of a potential merger on markets, therefore the following are of concern:

   a) What is the relevant market? – market definition is key to every antitrust violation.

   b) Measuring shares of merging corporations before and after merger

   c) Measuring Market Concentration before and after merger
d) **Drawing inferences from surrounding facts:**

1) **Barriers to Entry**

2) **Strength of Potential Competitors**

3) **Demand Elasticity**

4) **History of Competition**

6. **Justifications of a Merger** – where a merger has a *statistical impact on competition*, the following defenses have been employed to justify mergers that may otherwise be considered anti-competitive-

   a) **Small Firm Doctrine** – may allow two smaller firms to merge in order to compete more effectively against a larger dominant firm (see Brown Shoe).

   b) **Failing Company Doctrine** – in the absence of other purchasers, the court should allow a competitor to purchase a failing company. However, company must be in real & imminent danger of failure. (Citizen Publ. Co. v. US) must show:

   1) **Acquirer is only available purchaser**

   2) **Firm is on verge of Liquidation** – this includes a lack of possible reorganization under bankruptcy, etc.
c) *Lack of Competitive Harm* - once a prima facia case of potential harm by the merger, then the defendant firms seeking to merge will have to prove that such harm is illusory.

d) *Economic Efficiencies* – more recently courts have been willing to accept increased efficiency as a reason to allow a merger. This is a claim that the merger is ultimately beneficial to competition.

7. **Measuring Concentration – CR-4 Ratios** - the concentration ratio is a way of measuring the level of concentration of a market before and after a proposed merger – under the approach – the market shares of the four largest firms are added together – the resulting percentage would be placed on the following scale: -This approach has been ABANDONED BY MODERN GUIDELINES IN FAVOR OF HHI – INFRA.

a) \( CR-4 < 40\% \) - presumptively legal

b) \( CR-4 > 75\% \) - presumptively illegal

c) \( 40\% < CR-4 < 75\% \) - gray area – use change in concentration.

d) *Not Conclusive* – in addition, other factors such as barriers to entry – change in concentration – who’s merging with who.

B. **Merging of Competitors- Horizontal Mergers** - these are mergers between competitors – companies that perform similar functions – concerns here include concentration of market share that can result in – cartel behavior or monopoly price extraction.

1. **Factors in Determining Validity – Brown Shoe Analysis** - in one of the first cases decided after the amendment of §7 of the Clayton Act, the court set forward the following criteria in invalidating a merger. The court stressed *congressional intent to protect viable small local businesses* (Brown Shoe v. US – Merger nixed by gov’t)

a) Market Share Evidence

b) Economic and Historical Factors tending to create concentration

c) Lack of Any Affirmative Justification

d) Barriers to Entry

2. **“Presumptively Illegal” Test** – court seem to establish a *prima facia* illegality for horizontal mergers – a *rebuttable presumption* is created where a merger would create a firm *controlling an undue percentage of the market and significant increase in the concentration* of the market may have an anti-competitive effect. (US v. Phil. Nat. Bnk – invalidate merger where resulting firm would have 33% of market share and increased concentration of the market by 30%). *Note* - §7 subsequently amended to exclude banks.

3. **Other Factors – Aggressive/Innovators** – market share is no the sole factor looked at by the court, here the court invalidate a merger because the firm being
merged with was an aggressive and innovative firm which would have had a noticeable *impact on competition*. (US v. Alcoa – merger between Alcoa and Rome – a competitor with 1.3% of market share found illegal).

4. **Broad Limits of ‘Line of Commerce’** - where area of effective competition cuts across industry lines, so must the relevant line of commerce – the acquired company must be a competitor – this has been broadly interpreted by the court in the past. This is based on a the theory of *potential competition*. (US v. Continental Can – can manufacturer’s acquisition of glass jar manufacturer – despite no overlap in products).

5. **Stop Concentration in Incipiency** – the court has in the past stopped mergers on the sole basis that they are tending to concentration of the market and that such concentration must be stopped before the effects are realized – this has been sharply criticized for failure to look at other factors. (US v. Von’s Grocery – court enjoins merger between to small share grocers – want to protect small business – ignore lack of barrier to entry).

6. **Lack of Competitive Harm** - note that even where a prima facia case is made by the government, the defendant may be able to rebut the presumption of illegality – the key question is *what market share data is best indicator of future competitiveness?* (US v. General Dynamics – should look at changes in industry – presumption rebutted and merger allowed).

   a) *Post-Merger Evidence Often not admitted* – as a general rule evidence of a lack of effect on competition after the merger will not be looked at by the court – since the merged company is likely to be on its best behavior (smiles everyone!!!).

C. **Current Merger Enforcement**

1. **1992 Justice Department Guidelines** – these are the guidelines that the Justice Department uses in deciding to prosecute cases under §7, these guidelines are used by the FTC & Justice Department, but not by the courts in making decisions.

   a) *Differences between Supreme Court & Guidelines* - it is important to note the contrasts between these guidelines and supreme court case law, the higher standard of the guidelines means *less cases are prosecuted* than could be under existing law:

      1) **Different Measure of Concentration**- the guidelines use the HHI index, which has not been officially adopted by the court.

      2) **Must Have Anti-competitive effect**- the concentration of markets alone is not sufficient under the guidelines – this is in part because the guidelines allow for efficiency based mergers.

   b) *Factors in Guidelines* - beyond market share and concentration, the guidelines also consider the following factors:

      1) **Maverick Factor** – is the firm that is sought to be merged with an aggressive competitor whose presence may be missed more than the mere market share data indicates?
2) **Ease of Entry**- can a new competitor successfully enter the market in less than two years

3) **Increased Efficiency**- in a change from earlier policy, the government will allow mergers based on an increase of efficiency but not for the sole purpose of increasing market share.

4) **Asset Purchase Also Triggers** – note that the guidelines also regulate transactions that are defacto mergers, such as asset sales, etc.

2. **HHI Index** – the guidelines replace the four-firm concentration test with the Herfindahl-Hirschman Index or HHI. The test is used to determine the effect of merger by looking at the concentration in the market and the change caused by the market. *This test is used by the FTC but not by the Court.*

   a) **Calculation**- the HHI score is taken by defining a market by adding the *squared values of market share of every firm* in the market.

   b) **Level of Concentration**- the level of scrutiny depends on the level of concentration of the market:

      1) **Less than 1000 = Unconcentrated Market**
      2) **1000-1800 = Moderately concentrated market**
      3) **More than 1800 = Highly Concentrated Market**

   c) **Change in Concentration**- the level of scrutiny depend on the ending level of the market and the change affected by the merger:

      1) **Unconstrated Market** – if the change still results in an unconcentrated market, the merger will not be challenged by the FTC.
      2) **Change 100 in Moderate = Challenge**
      3) **Change 50 in High = Challenge**
      4) **Change 100 in High = Presumptively Illegal**
3. **Private Suits** – the act still provides remedies for private firms, including the remedy of divestiture (Drobak – not bloody likely for private suit), however there is often an issue of standing because of a requirement for an antitrust injury.

   a) **Competitors of Merging Firms**– where two firms are merging, the competitors of the firms may have a suit against them – however, they must show an injury as a result of a violation of the antitrust law, this is often difficult.

   b) **Hostile Takeover Defense**– a firm that is subject to a hostile take-over attempt to claim the takeover would violate antitrust laws, again it is difficult to show any antitrust injury – such claims have not been successful.

**D. Joint Ventures**– merger regulation can be used to a lesser extent to attempt to regulate joint ventures. However, if only subject to scrutiny under §1 of the Sherman act – which there are often approved under. Again, this cooperation between competitors has the ability to foreclose competition – or enhance it.

1. **Joint Ventures Subject to Clayton Act §7** – the court has held joint ventures were subject to the same analysis under §7 of the act.

2. **Factors Considered** – the following factor are likely to be considered by the court in determining the propriety of a joint venture.

   a) **Purpose of the Venture**

   b) **Structure of Market** – will the venture have market power?

   c) **Is the venture a forum for collusion?**

   d) **Are there efficiency & pro-competitive effects?**

   e) **Is the venture necessary to achieve these effects?**– are there other alternatives?

3. **Toe-Hold Doctrine** – merger or joint venture may not be allowed to have potential competitor join with existing market competitor. Effectively, a potential competitor cannot enter into the market by purchasing a potential competitor. Specifically such a merger/venture should be disapproved where:

   a) **Reasonable probability firm would have entered market w/o merger/joint venture.**

   b) **Entry would have de-concentrated market**

   c) **Market under review is concentrated**

4. **Research Ventures = Rule of Reason** – by special act of Congress, joint ventures for the purposes of research are exempt from the regulation and are looked at under the rule of reason.

**E. Foreclosure Problems - Vertical Mergers**– these are mergers where a buyer buys his supplier (upstream merger) or a supplier buying a retailer (downstream mergers).

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F. Conglomerate Mergers - Mergers of Potential Competitors

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