

7-1-1985

Local Government Practices and the Antitrust Merits

Mark R. Lee

Follow this and additional works at: <https://repository.law.miami.edu/umlr>



Part of the [Antitrust and Trade Regulation Commons](#)

Recommended Citation

Mark R. Lee, *Local Government Practices and the Antitrust Merits*, 39 U. Miami L. Rev. 589 (1985)
Available at: <https://repository.law.miami.edu/umlr/vol39/iss4/2>

This Article is brought to you for free and open access by the Journals at University of Miami School of Law Institutional Repository. It has been accepted for inclusion in University of Miami Law Review by an authorized editor of University of Miami School of Law Institutional Repository. For more information, please contact library@law.miami.edu.

University of Miami Law Review

VOLUME 39

JULY 1985

NUMBER 4

Local Government Practices and the Antitrust Merits

MARK R. LEE*

I. INTRODUCTION	589
II. REASSESSMENT: THE INTELLECTUAL PROCESS	593
III. THE PROCESS ILLUSTRATED	602
A. <i>Deducing Functions</i>	603
B. <i>Are Any of the Functions Objectionable?</i>	638
IV. THE IMPACT OF REASSESSMENT ON ANTITRUST LAW	642

I. INTRODUCTION

The Supreme Court made it clear in *Community Communications Co. v. City of Boulder*¹ that local governments are subject to antitrust suits unless they can show that the state action immunity doctrine of *Parker v. Brown*² shields their conduct. Almost as soon as the Court decided *Boulder*, local government officials and their trade association representatives descended upon Congress to demand legislation that would reduce their exposure to antitrust lia-

*Associate Professor of Law, Southern Illinois University School of Law. A substantial portion of this article will appear in a forthcoming book by the same author, *ANTITRUST LAW AND LOCAL GOVERNMENT*, published by Greenwood Press. The author would like to express his appreciation to Lynn Taylor at Greenwood Press, who is Editor of Quorum Books. The author would also like to acknowledge the assistance of Lynn Sedlack Flint, of Greenwood Press, and Vera Felts, of the Southern Illinois University School of Law, in the preparation of this article.

1. 455 U.S. 40 (1982). The city of Boulder, through broad powers granted by the state constitution, passed a moratorium ordinance preventing a cable television company from expanding its services. The company sought an injunction and the Court held that the moratorium ordinance was not exempt from antitrust scrutiny.

2. *Parker v. Brown*, 317 U.S. 341 (1943).

bility. Their lobbying reached a fevered pitch when, for the first time, a court entered a judgment for treble damages against a local government, the town of Grayslake, Illinois.³ The lobbyists asserted straightforward arguments:⁴ Local governments have commonly engaged in practices that are identical or closely analogous to those of private enterprise, and those practices are subject to extensive antitrust scrutiny and occasional condemnation. Without fairly iron-clad immunity from suit, local governments engaging in business as usual would risk incurring budget-busting litigation costs and adverse antitrust judgments, including the possibility of treble damage awards. The lobbyists claimed that the enormity of the risks would force local governments to substantially reduce their use of those common practices and concomitantly, the programs accompanying those practices. Thus, they concluded, unless Congress adopted some "Boulder legislation," the antitrust juggernaut unleashed by the Court would smash local government as we now know it.⁵

Congress apparently found the argument and the lobbying persuasive for it passed a bill which, upon President Reagan's signature, became the Local Government Antitrust Act ("Act") of 1984.⁶ That Act bars claimants seeking treble damage (except those who filed before September 24, 1984) from obtaining any monetary relief from local governments if the perpetrators of the offenses acted in an official capacity. This bar will reduce the gain that some potential claimants will expect to realize from antitrust

3. *Unity Ventures v. Village of Grayslake*, 46 ANTITRUST & TRADE REG. REP. (BNA) No. 1157, at 595 (1984).

4. For similar arguments, see *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389, 438-40 (1978) (Stewart, J., dissenting); Areeda, *Antitrust Immunity for "State Action" after Lafayette*, 95 HARV. L. REV. 435 (1981); Civiletti, *The Fallout from Community Communications Co. v. City of Boulder: Prospects for a Legislative Solution*, 32 CATH. U.L. REV. 379, 385-86, 388 (1983); Note, *Community Communications Co. v. City of Boulder: The Emasculation of Municipal Immunity from Sherman Act Liability*, 32 CATH. U.L. REV. 413, 432 (1983). Lobbyists also argued that the Court's decisions would dramatically alter the relationships between state and local government, in general, and the "home rule" movement, in particular. See also 435 U.S. at 435-38; Bangasser, *Exposure of Municipal Corporations to Liability for Violations of the Antitrust Laws: Antitrust Immunity after the City of Lafayette Decision*, 11 URB. LAW. vii (1979); Civiletti, *supra* note 4, at 387-89; Note, *supra* note 4, at 431; Comment, *City of Lafayette v. Louisiana Power & Light Co.: Will Municipal Antitrust Liability Doom Effective State-Local Government Relations?*, 36 WASH. & LEE L. REV. 129 (1979).

5. "The Court's decision in this case is flawed in two serious respects, and will thereby impede, if not paralyze, local governments' efforts to enact ordinances and regulations aimed at protecting public health, safety, and welfare . . .", 455 U.S. 40, 60 (Rehnquist, J., dissenting); accord 435 U.S. 426 (Stewart, J., dissenting); Civiletti, *supra* note 4, at 387.

6. Local Government Antitrust Act of 1984, Pub. L. No. 98-544, 98 Stat. 2750.

claims against local governments.⁷ It will also result in the filing of fewer claims against local governments. The fewer claims filed, the smaller the threat posed to local governments by post-*Boulder* antitrust actions.

Many claimants will still file claims. The Act will not deter the Federal Trade Commission and the Department of Justice from filing claims in the course of their enforcement work. Nor will it deter many private enterprises from filing claims. Even before the passage of the Act, some antitrust claimants against local governments sought only equitable relief, and many others must have known that it was unlikely that they could obtain more than equitable relief. The plaintiffs in the *Boulder* case exemplified such claimants. The Act creates no bar for them; they may still obtain equitable relief along with "the cost of suit, including a reasonable attorney's fee."⁸ The Act may increase the chances that such claimants will obtain that relief because it renders the remedy at law—monetary damages—inadequate. In any event, it should not reduce the number of claims that these potential claimants file. Also, it should not affect those initiating disputes with local government who realize they could press antitrust claims at a rather small incremental cost. This group includes any who could plausibly challenge the government's actions not only on antitrust grounds, but also on a deprivation of constitutional rights, a breach of contract, a tort, or other ground. There are apparently many who could mount such a challenge. In the reported cases dealing with antitrust claims against local governments, most of the claimants did just that, including the claimants in *Boulder* and those in

7. For some of those potential claimants, the reduction in expected gain will be small. Many of them will have little hope of proving that they suffered any damages as a result of a local government's alleged misbehavior, and even less hope of proving that whatever damages they did suffer stemmed from an antitrust injury. See *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977). These claimants can reasonably expect to obtain monetary relief equal only to the cost of the suit, including a reasonable attorney's fee, discounted by the probability of prevailing. The Local Government Antitrust Act of 1984 will not change this situation at all.

Of course, claimants who filed before September 24, 1984, might still reasonably expect to obtain that relief, and perhaps more. These claimants number "in the hundreds" according to the *National Law Journal*. *New Antitrust Act May do Little to Stem Suits*, NAT'L L. J., Dec. 3, 1984, at 1, col. 4. The Act provides that the bar to obtaining monetary relief "shall not apply to cases commenced before the effective date of [the] Act unless the defendant establishes, and the court determines, in light of all the circumstances, including the stage of litigation and the availability of alternative relief under the Clayton Act, that it would be inequitable not to apply this subsection to a pending case." 15 U.S.C.A. § 35(b) (Supp. 1985).

8. 15 U.S.C.A. § 35(a) (Supp. 1985).

the Court's original city immunity case, *City of Lafayette v. Louisiana Power & Light*.⁹ This group also includes any defendant sued by a local government who could file a colorable counterclaim as an antitrust offense, attacking behavior connected with the underlying claim. The antitrust claimants in *Lafayette* were such defendants. Even those who would find it expensive to press an antitrust claim against local government will do so if they perceive a reasonable chance of persuading a fact finder that the perpetrators of the offense did not act in an official capacity.¹⁰ Because it is likely that local governments will continue to be named in a sizable number of antitrust claims despite the Act, it is also likely that the Act will not seriously reduce the threat posed by post-*Boulder* antitrust law.

The purpose of this article is not to criticize the Act for failing to substantially protect local governments. Despite the *Grayslake* treble damage award, it is doubtful that local governments require much protection from antitrust law. Those who lobbied for the Act exaggerated the risks that *Boulder* and *Lafayette* created, because they ignored the possibility that courts might reassess the merits of the challenged practices when the courts removed local government immunity. Such a reassessment would involve grappling with two questions: What is the real objection to the practices, even when they are employed by private enterprises; and, would sustaining a challenge on that basis be consistent with the purpose of the antitrust statutes? Answering those questions would reveal that most of the challenged practices are objectionable, if at all, only on the basis of populist notions about the distribution of wealth between private enterprises. It is considered desirable, perhaps for political and social reasons, to prefer "smaller," "less advantaged" firms to "larger," "more advantaged" firms in a quest for egalitarianism.¹¹ But those populist notions, whatever their merits, do not address disputes between local government and pri-

9. 435 U.S. 389 (1978).

10. This group will consist largely of those who can show that the perpetrators failed to discharge their responsibilities to constituents, or otherwise breached the duties imposed by nonantitrust law. The plaintiffs in *Affiliated Capital Corp. v. City of Houston* would have belonged to this group. 519 F. Supp. 991 (S.D. Tex. 1981), *rev'd*, 700 F.2d 226 (5th Cir.), *vacated*, 714 F.2d 25 (5th Cir. 1983), *rev'd on reh'g* 735 F.2d 1555 (5th Cir. 1984) (en banc). For an analysis of the relationship between such misbehavior and antitrust law, see *infra* notes 13 & 14 and accompanying text.

11. In some cases even these unofficial populist notions would not justify condemnation of the practices. See, e.g., *Ladue Local Lines, Inc. v. Bi-State Dev. Agency*, 433 F.2d 131 (8th Cir. 1970); *Heille v. City of St. Paul*, 512 F. Supp. 810 (D. Minn. 1981), *aff'd*, 671 F.2d 1134 (8th Cir. 1982).

vate enterprise. Moreover, local government probably holds a higher place than any other institution in the pantheon of populism. Therefore, courts undertaking this reassessment would presumably find the practices lawful. Such findings would reduce the risk of incurring adverse judgments that result in budget-busting litigation costs. It could also produce some extraordinary changes in antitrust law. The principal purposes of this article are to demonstrate how that reassessment might, and should, be conducted, and to identify what changes might occur.

II. REASSESSMENT: THE INTELLECTUAL PROCESS

To discover the actual objection to a challenged practice, a judge would have to ascertain the functions that the practice was supposed to serve and to find an antitrust principle inconsistent with those functions. Before describing that intellectual process, an explanation must be given of why the process would focus on what the practice was supposed to do, rather than focusing on what it did do. Such a focus is consistent with, and probably dictated by, the consumer welfare goal of the antitrust laws. In most cases an inquiry into the actual impact of a particular practice would be extraordinarily time-consuming and, in the end, fruitless.¹² Even if that were not so, it would nonetheless be inefficient. A practice would fail to serve its supposed function only if its users miscalculated or misbehaved. If they miscalculated, subjecting them to antitrust sanctions would be unnecessary because the market would punish them. Worse still, subjecting them to antitrust sanctions would deter others from correctly using the practice because of the fear that they too would miscalculate, or because of the risk that a court might err in assessing the actual impact of the practice. If the users of the practice misbehaved by taking advantage of their principals—or perhaps selling them out—then the antitrust laws would not address their conduct. Current antitrust laws are simply not designed to limit the opportunistic behavior of agents.¹³ They

12. R. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 128-29 (1978). Cf. *United States v. Socony-Vacuum Oil Co., Inc.*, 310 U.S. 150 (1940).

13. It is difficult for any principal to absolutely control the behavior of his agent. Admittedly, it is particularly difficult for citizens to control the behavior of their agents because it is usually costly for those citizens to give directions, to ascertain whether their directions are being followed, and if not, to revoke the authority granted to act on their behalf. These problems, no matter how acute, raise none of the efficiency concerns that are germane to antitrust law. The Sherman and Clayton Acts do not address any aspect of the principal-agent relationship. A contrary interpretation would likely have an extraordinarily wide-ranging, and surely unintended, impact on ordinary business activities. For example, it

are also not designed to prevent local politicians and bureaucrats from taking advantage of or selling out their constituents.¹⁴ If they

would probably convert an executive's breach of the fiduciary duty owed to his corporation's shareholders into an antitrust offense. Moreover, given the Supreme Court's decision in *American Soc'y of Mechanical Eng'rs, Inc. v. Hydrolevel Corp.*, a contrary interpretation would likely yield perverse results in litigated cases. 456 U.S. 556 (1982). In *Hydrolevel*, the Court held that a principal could be held liable for an antitrust offense committed by his agents if they acted with apparent authority. *Id.* at 565-66. Thus, if a failure to do a principal's bidding constituted an antitrust offense, the principal, who was victimized by that failure, could be held liable.

14. Of course, local government officials do sometimes act opportunistically, perhaps engaging in malfeasance or even crime. See, e.g., *Affiliated Capital Corp. v. City of Houston*, 519 F. Supp. 991 (S.D. Tex. 1981), *rev'd*, 700 F.2d 226 (5th Cir. 1983), *vacated*, 714 F.2d 25 (5th Cir.), *rev'd on reh'g*, 735 F.2d 1555 (5th Cir. 1984) (en banc). They may also fail to ascertain a court's evaluation of the citizens' demand for a good. (Failing to ascertain what the court believes to be the citizens' demand schedule for a good could reflect either the prohibitive cost of ascertainment or honest disagreement). In other words, they may participate in an exchange that appears to be a bad deal because of corruption, bias, or stupidity. Rose, *Municipal Activities and the Antitrust Laws after City of Lafayette*, 57 UNIV. DET. J. URB. L. 483, 490-94 (1979). Even so, a court should not rule that the practice constituted an antitrust offense.

The fact that government officials did not act in a manner consistent with their responsibilities towards citizens was of no consequence under the Sherman or Clayton Acts. *Sun Valley Disposal Co. v. Silver State Disposal Co.*, 420 F.2d 341 (9th Cir. 1969); *Huron Valley Hosp., Inc. v. City of Pontiac*, 466 F. Supp. 1301, 1315 (E.D. Mich. 1979); *contra Cirace, An Economic Analysis of the "State Municipal Action" Antitrust Cases*, 61 TEX. L. REV. 481, 485-86 (1982). It is easier to comprehend the inevitability of that result where there has been no exchange. For good illustrations of that situation, see *Schiessle v. Stephens*, 525 F. Supp. 763 (N.D. Ill. 1981); *Highfield Water Co. v. Public Service Comm'n [of Md.]*, 488 F. Supp. 1176 (D. Md. 1980). *Highfield Water* developed from an alleged expropriation of a water utility by government officials who acted in contravention of state regulatory law. *Schiessle* arose from an alleged misuse of eminent domain powers by government officials who planned to transfer property from one real estate developer to a group of others. In both cases, local government officials allegedly acted in violation of nonantitrust law. Their actions would have been inconsistent with their responsibilities to local citizens, and injurious to private enterprise. Such conduct would certainly be objectionable—in fact, it might expose the actors to suit for failure to abide by state civil statutes or city ordinances, and to tort actions, or even criminal prosecution—but clearly not on any principle embodied in the antitrust statutes. The same observation holds for zoning decisions allegedly undertaken for the benefit of the officials making them. See *Whitworth v. Perkins*, 559 F.2d 378 (5th Cir. 1977), *vacated*, *Impact v. Whitworth*, 435 U.S. 992, *on remand*, *Whitworth v. Perkins*, 576 F.2d 696 (5th Cir. 1978), *cert. denied*, 440 U.S. 911 (1979); *Stauffer v. The Town of Grand Lake*, 1981-1 Trade Cas. (CCH) ¶ 64,029 (D.C. Colo. 1980); *Miller & Son Paving, Inc. v. Wrightstown Township Civic Ass'n*, 443 F. Supp. 1268 (E.D. Pa. 1978), *aff'd mem.*, 595 F.2d 1213 (3d Cir. 1979); *Nelson v. Utah Co.*, 1978-1 Trade Cas. (CCH) ¶ 62,128 (D. Utah 1977). *But cf.* Dabney, *Antitrust Aspects of Anticompetitive Zoning*, 24 ANTITRUST BULL. 435 (1979) (arguing that a court should deem a zoning decision an antitrust offense if made for the purpose of restricting competition or, for some other purpose, if an alternative means less restrictive of competition is available). Commentator Dabney does not reveal how a court would go about ascertaining the purpose of a zoning decision. That could be problematic because all denials of zoning changes requested by the owner of the affected property tend to suppress competition in a sense. Nor does Dabney explain how a court should take into account efficiency and cost in evaluating alternative means. The same is true of similar

were so designed, federal courts would operate as superlegislatures when applying these laws to local government defendants.

Microeconomics has explained the function of most private enterprise practices that claimants challenge under antitrust statutes,¹⁵ but it has yet to do the same for local government practices.¹⁶ This contrast may reflect *Boulder's* recent vintage. Analysts may not have had sufficient opportunity to develop the required explanations. Traditionally, practices have been challenged long before they have been explained,¹⁷ but this is not the only possible reason. An intellectual obstacle may be blocking the development of any explanations. Local government is institutionally very different from private enterprise. In particular, local government decision-making involves far more voting that is not weighted according to wealth, than does private enterprise decision-making. Furthermore, local government officials are more subject to control from the residents of the governed community than are officials of private enterprises. Because of these differences, it would be unrealistic to adopt the common assumption normally used to describe private enterprises when discussing local governments. It is unlikely that local governments act to maximize the wealth of their principals. Yet, it is precisely that assumption which gives microeconomics its explanatory power. Consequently, analysts may be avoiding the development of microeconomic explanations until they are better able to integrate it with a more advanced theory of public choice than they currently possess.¹⁸

A judge undertaking the reassessment of a local government practice should nonetheless turn to microeconomics for an explanation of the practice's function. The important institutional differences between local government and private enterprise are unimportant for the purposes of antitrust analysis. Antitrust does not speak to the relationship between those who govern and those who are governed. Nor does it speak to decision-making methodology. In *Boulder* and *Lafayette*, the Supreme Court declared its intention to have those opinions interpreted so that they would not con-

conduct that happens to be related to an exchange. The exchange, in these situations, is incidental.

15. Easterbrook, *Is There A Ratchet in Antitrust Law?*, 60 TEX. L. REV. 705 (1982).

16. *But see Omega Satellite Products Co. v. City of Indianapolis*, 694 F.2d 119 (7th Cir. 1982).

17. Easterbrook, *supra* note 15.

18. For a discussion of public choice theories, see J. BUCHANAN & G. TULLOCK, *THE CALCULUS OF CONSENT* (1962); D. MUELLER, *PUBLIC CHOICE* (1979); M. OLSON, *THE LOGIC OF COLLECTIVE ACTION* (1965); G. TULLOCK, *THE LOGIC OF LAW* (1970).

strain the political process.¹⁹ Moreover, the Court concluded that local governments should be subject to antitrust scrutiny because of the danger of wealth-maximization even in a local government setting.²⁰ If antitrust is to be confined to its proper sphere, courts must analyze the practices of local governments as well. Local governments must act to maximize the wealth of the residents of the governed community, and their conduct should be condemned only if these practices amount to an offense.

Almost every local government practice challenged under the antitrust statutes, including the one analyzed in this article, was used as an integral part of a complex sales transaction in which the local government may have been the supplier, the purchaser, or more likely, the agent for parties occupying one of those positions.²¹ Such practices are termed vertical restraints.²² Solely on the basis of that observation, a judge reassessing local government practices will be able to determine that the challenged practice was intended to serve some instrumental function in effectuating the transaction. Applying the wealth-maximization assumption, he will then realize that, in most situations, the local government intended that function either to secure the benefits that are the subject of the transaction or to reduce the costs of making it. In a large number of cases it will be clear to the judge that without the challenged practice the transaction would not have taken place because the benefits would have appeared ephemeral or the costs prohibitive. The judge will want to make more specific deductions on the basis of more intricate observations about the function of the challenged practice; however, with only his general deductions in hand the judge will still be able to search for an antitrust principle inconsistent with that function.

Whatever the principle may be, it must speak to the likely effects of the transaction, or to ones like it. Antitrust law is concerned with the effects of economic activity. Nonetheless, some activity is condemned under the so-called rule of per se illegality

19. 435 U.S. at 405 n.31, 416-17, quoted with approval in, *Boulder*, 455 U.S. at 57-58.

20. *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389, 403-04, 412-13, discussed with approval in *Communications Co. v. City of Boulder*, 455 U.S. 40, 49-51 (1982).

21. Cf. *Omega Satellite Products Co. v. City of Indianapolis*, 694 F.2d 119, 123 (7th Cir. 1982) (Action involving exclusive franchises for cable television).

22. Because this article focuses on vertical restraints, it adopts a transaction costs approach. For an illustration of transaction cost analysis, see Williamson, *Assessing Vertical Market Restrictions: Antitrust Ramifications of the Transaction Cost Approach*, 127 U. PA. L. REV. 953, 975-80 (1979).

without an elaborate inquiry into its actual anticompetitive effects, because the effects are so likely to be undesirable that making the inquiry would be wasteful.²³ Because of the relationship between the local government practice and the transaction itself, the only effects that are of interest are those that arise out of the transaction. These effects will be of two kinds: (1) those that relate to the creation of wealth, which antitrust scholars usually call consumer welfare, and (2) those that relate to the distribution of wealth, the question of who gains and who loses. The creation of wealth is commonly considered beneficial. When applying that principle, the transaction that creates wealth would usually be considered desirable. The parties to it will have perceived themselves as better off for having entered into the transaction, unless a miscalculation has been made.²⁴ Otherwise, they would not have agreed to the exchange. The same observation may be made about parties to any sales transaction. Thus, when viewed statically, such transactions tend to create wealth.²⁵ Viewed dynamically, they certainly do create wealth. Producers and consumers tend to shift resources to higher value uses by entering into these transactions. After making the agreements, the total personal value the owners attach to the exchanged goods and services tends to be larger than it was before.²⁶

Two possible exceptions to the general rule that sales transactions create wealth merit discussion. First, certain sales transactions may be, in large part, transfer payments.²⁷ For example, a transportation enterprise owned by a local government might sell bus service to senior citizens at prices well below the marginal costs of providing it. Local government might be making an inkind transfer payment to those citizens. Aside from endowment effects that are likely to be negligible, transfer payments themselves have no impact on the creation of wealth. The method by which they are financed, for example taxation in the case of governments,

23. See *United States v. Container Corp. of Am.*, 393 U.S. 333, 341 (1969) (Marshall, J., dissenting); *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958).

24. Making miscalculations is likely to be a self-limiting activity and therefore an unimportant one in the aggregate. Because the market would adequately punish miscalculations, and because the use of law to punish them would create risks likely to deter some efficient behavior, we ignore the possibility of such miscalculations in antitrust analysis.

25. A. ALCHIAN & W. ALLEN, *EXCHANGE AND PRODUCTION: COMPETITION, COORDINATION, AND CONTROL* 28-31 (2d ed. 1977).

26. *Id.* at 30-31.

27. Some of these transactions may involve the sale of a durable good, like a house, subject to resale limitations. See Strauss & Stegman, *Moderate-Cost Housing After Lafayette: A Proposal*, 11 *URB. LAW.* 209 (1979).

would almost certainly have an impact by reducing incentives to work or invest. Accordingly, in applying our principle that the creation of wealth is beneficial, transfer payments, while not necessarily desirable, are certainly not objectionable.

The second exception consists of sales transactions that are strategically designed to secure market power by restricting output. For example, the transportation enterprise described in the preceding paragraph could be selling its services to senior citizens at low prices in order to drive competitors out of the market. Once successful, the enterprise would attempt to raise its prices and obtain monopoly profits by reducing the supply of bus services in response to the drop in demand. The public would find this type of transaction highly objectionable.

It is unlikely that judges hearing an antitrust suit against a local government would encounter transactions having monopolistic effects. For reasons which have been discussed elsewhere, most enterprises would not engage in such strategic behavior because the expected losses from doing so would exceed the expected gains.²⁸ Even scholars who believe that such behavior will be exercised often enough to raise serious antitrust concerns assume that only dominant enterprises or those that are part of a collusive oligopoly will be the culprits.²⁹ It is particularly unlikely that local governments would engage in such conduct. Local government managers have little incentive to participate in strategic market behavior in light of the considerable difficulties in capturing the expected revenues derived from such behavior. Moreover, it would be difficult to implement this type of strategy because local governments tend to be plagued by greater turnover among top policy-makers and more cumbersome operating procedures than are

28. See R. BORK, *supra* note 12, at 144-60; R. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 184-96 (1976); Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263 (1981); Elzinga, *Predatory Pricing: The Case of the Gunpowder Trust*, 13 J. LAW & ECON. 223 (1970); McGee, *Predatory Price Cutting: The Standard Oil (N.J.) Case*, 1 J. LAW & ECON. 137 (1958).

29. *E.g.*, Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284 (1977) [hereinafter cited as *Predatory Pricing*]; Williamson, *Predatory Pricing II*, 88 YALE L.J. 1183 (1979) [hereinafter cited as *Predatory Pricing II*]. Williamson defines a dominant firm as one having 60% of the relevant market, and asserts that collusive oligopoly is likely to occur "mainly in mature, highly concentrated industries producing homogeneous products under uniform cost conditions and having significant barriers to entry." *Predatory Pricing*, *supra* note 29, at 293. He suggests that highly concentrated industries are those in which four or fewer firms account for more than 70% of the output. *Predatory Pricing II*, *supra* note 29, at 1194.

private enterprises of similar size.³⁰

In almost every case, therefore, the effects of the transaction do not appear to be objectionable from a consumer welfare point of view. These effects might be objectionable, if at all, only in terms of wealth distribution. The judge will have to search for a controlling principle that will allow him to prefer one group to another. As long as the plaintiff may plausibly argue that he belongs to the disfavored group and the defendant to the favored, the judge may loosely define both groups despite their being comprised of ever-changing populations. After all, the principle must require that the objecting party, the plaintiff, prevail upon proof of his claim.

Judges will encounter three serious problems in conducting their search: (1) a problem of logic, (2) a problem of advocacy, and (3) a problem of case analysis. Logistically, no matter what principle of preference the judge considers, he will find that it does not require the plaintiff to prevail. The judge will have no difficulty designating any number of groups to which the parties belong. Let the plaintiff belong to group P and the defendant to group D. In addition to the plaintiff and would-be parties, P presumably has many members who would accede to the particular transaction by virtue of a favorable disposition of the pending suit.³¹ The judge would then consider the principle that it is good to prefer members of group P to members of group D. He must determine whether that principle requires the plaintiff to prevail upon proof of his claim. The answer would be yes if penalizing the defendant for entering into the transaction tends to make the members of P better off than they otherwise are. The answer, however, is no; the reason inheres in the dynamics of markets.³² First, consider the impact of penalizing the defendant from P's point of view. Members of that group wishing to bind themselves by making promises similar to those of the plaintiff would encounter a major obstacle. Everyone would realize that if he entered into a transaction in which a member of P made such a promise, he would then subject himself to the risks of paying substantial litigation costs and suffering an adverse antitrust judgment. The result is that members of P would not be

30. The approach described is, at least to this point, analogous to that which Williamson advocates. See Williamson, *supra* note 22, at 975-80.

31. Otherwise, the principle of wealth-distribution being tested would be a meaningless, tautological trap in our system of jurisprudence—that the plaintiff should prevail in a given dispute because he and those allied with him will be better off if he does.

32. For a brief overview of market dynamics, see A. POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 107-10 (1983).

able to obtain the value of that promise; indeed, they would forfeit a "property right."

Now consider the impact of penalizing the defendant from D's point of view. When contemplating a transaction, members of D would take into account the prospect of penalties under the antitrust laws. They would freely expend resources to avoid that result. Therefore, the transactions would be more costly than they otherwise would have been, and members of D would tend to make fewer or less valuable offers to members of P. In short, penalizing the defendant for entering into the transaction would tend to make members of P, although not the plaintiff, worse off.³³

At this point the judge might wish to call off the search, but he may not feel free to do so lest he be accused of casting aside precedent and the many antitrust cases which seem to have been resolved on the basis of some elusive principle of wealth distribution.³⁴ To continue his search for that principle, the judge would have to ignore market dynamics. Such willful ignorance has been aptly called sentimentality.³⁵

A sentimental judge is critical to the plaintiff's case. Yet, even if he is, he will likely obtain little meaningful assistance from plaintiff's counsel in conducting his search. Counsel will likely insist that the court should decide the case based on whether the challenged practice denied plaintiff the opportunity to do business, eliminated the plaintiff as a rival, excluded the plaintiff from the market, subjected the plaintiff to abuse, or limited the freedom of the plaintiff to run his business independently. Characterizing the inquiry obscures rather than reveals the alleged controlling principle of wealth-distribution. This is an advocacy problem. Counsel will create this obscurity for two strategic reasons. First, he may then rely on that loose Jeffersonian ideology that prevades so many antitrust opinions.³⁶ That ideology, which is so vague and yet

33. The illogic of applying a wealth distribution-principle to resolve antitrust disputes makes for unpredictable outcomes. Unpredictable outcomes are evidence that the courts are making policy decisions that traditionally belong to legislatures. Thus, they raise the question of who governs. See R. BORK, *supra* note 12, at 418-25. That question is raised rather starkly in those cases in which a local government is the defendant. See cases cited *infra* note 40.

34. For a recent example of such a case, see *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*, 676 F.2d 1291 (9th Cir.), *cert. denied*, 459 U.S. 1009 (1982).

35. See R. BORK, *supra* note 12, at 54-55; Will, *As I Was Saying*, NEWSWEEK, Apr. 16, 1979, at 100.

36. See 1 P. AREEDA & D. TURNER, *ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION* ¶ 1096 (1980); R. BORK, *supra* note 12, at 54-56. See generally 1 P. AREEDA & D. TURNER, *supra* note 36, at § 103-12; C. KAYSEN & D. TURNER, *ANTITRUST*

so appealing, is likely to receive a more sympathetic reception than any particular wealth-distribution principle that might otherwise be more appropriate. Second, he may be able to invoke antitrust precedent that involves private enterprises engaged in arguably similar practices. This is particularly true where the court characterized the inquiry in the same way and condemned or found the practice suspect.

Unfortunately, the judge will likely turn to those cases for some help in conducting his search. He will probably find it difficult to distinguish the ideological rhetoric used in those opinions from the wealth-distribution principle that, market dynamics aside, dictated the result. This is the case analysis problem. Patient study will reveal that private holdings of wealth, usually referred to as firms,³⁷ that are "smaller" or "less advantaged", are preferable to firms that are "larger" or "more advantaged." The judge will have been searching for this principle. It reflects a crude theory of public choice, and of that collection of sentiments and beliefs known as populism.³⁸ This theory explains political behavior largely on the basis of the relative wealth of the private antagonists interested in influencing the behavior. Populism holds that behavior will be better the wider and more even the distribution of wealth.³⁹

Having finally completed his search, the judge will find that his efforts were in vain. Neither the principle discovered, nor the public choice theory and the ideology that it reflects, will suggest that the judge rule against the defendant local government. The principle does not even speak to whether the court should prefer private holdings of wealth to either public or collective holdings,

POLICY: AN ECONOMIC AND LEGAL ANALYSIS 17-18 (1959).

37. This reference is permissible for casual discussion. It does not, however, reflect recent advances in the theory of the firm. See, e.g., Alchian & Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777 (1972); Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386 (1937). Furthermore, for the purposes of sophisticated analysis, this reference may be misleading, particularly when too much is made of the corporate legal form which many "firms" take.

38. Analyst Bork refers to them as a "jumble of half-digested notions and mythologies." R. BORK, *supra* note 12, at 54. They usually include a professed concern for the "free choice" of the "independent" businessman and his "opportunity to do business" (what analyst Bork calls the bondage theme), a stated preference for atomistic markets ("fragmentation for its own sake"), and a devotion to "fairness," which usually means equality of outcomes. *Id.* at 50-56.

39. See 1 P. AREEDA & D. TURNER, *supra* note 36, at ¶ 1096; R. BORK, *supra* note 12, at 54-55. Some leading antitrust opinions reflect both this theory and ideology. See, e.g., *United States v. Von's Grocery Co.*, 384 U.S. 270 (1966); *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962); *United States v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945).

like those of local governments. The theory has little, if anything, to do with political behavior related to disputes between private enterprises and local government. Moreover, populism does not suggest that the situation would be better if private enterprise were made wealthier at the expense of local government. Indeed, populism, as it is commonly understood, probably dictates that the courts prefer local government, together with the taxpayers it purports to represent, to any firm. Local government is populist-preferred; thus, any objection to the wealth-distribution effects of the transaction would not be well taken. Because there is no principle according to which the judge might consider the effects of the transaction undesirable, he will be bound to reject the plaintiff's attack on the challenged practice.

III. THE PROCESS ILLUSTRATED

Every local government enters into agreements with suppliers, and occasionally purchasers, pursuant to which they decline to buy from, or sell to, some or all of their rivals. Of course, this practice displeases rivals who too frequently claim that it runs afoul of the Sherman Act. It has probably been the focus of more antitrust litigation against local government than any other practice.⁴⁰ These

40. *E.g.*, *Catalina Cablevision Assocs. v. City of Tucson*, 1984-2 Trade Cas. (CCH) ¶ 66,249 (9th Cir. Oct. 25, 1984); *Daley v. Town of New Durham*, 733 F.2d 4 (1st Cir. 1984); *Tom Hudson & Assocs., Inc. v. City of Chula Vista*, 1984-2 Trade Cas. (CCH) ¶ 66,251 (9th Cir. Oct. 25, 1984); *Springs Ambulance Serv., Inc. v. City of Rancho Mirage*, 1983-2 Trade Cas. (CCH) ¶ 65,646 (C.D. Cal. Sept. 27, 1983), *granting preliminary injunction pending trial in 1984-1 Trade Cas. (CCH) ¶ 66,014 (C.D. Cal. May 3, 1984), rev'd in part*, 1984-2 Trade Cas. (CCH) ¶ 66,261 (9th Cir. Oct. 25, 1984); *Englert v. City of McKeesport*, 564 F. Supp. 375 (W.D. Penn. 1983), *rev'd*, 736 F.2d 96 (3d Cir. 1984); *Central Iowa Refuse Sys., Inc. v. Des Moines Metropolitan Area Solid Waste Agency*, 557 F. Supp. 131 (S.D. Iowa 1982), *aff'd*, 715 F.2d 419 (8th Cir. 1983), *cert. denied*, 105 S. Ct. 1864 (1985); *Omega Satellite Prods. Co. v. City of Indianapolis*, 694 F.2d 119 (7th Cir. 1982); *All Am. Cab Co. v. Metropolitan Knoxville Airport Auth.*, 547 F. Supp. 509 (E.D. Tenn. 1982), *aff'd mem.*, 723 F.2d 908 (6th Cir. 1982); *Glenwillow Landfill, Inc. v. City of Akron*, 485 F. Supp. 671 (N.D. Ohio 1979), *aff'd sub nom. Hybud Equip. Corp. v. City of Akron*, 654 F.2d 1187 (6th Cir. 1981), *vacated and remanded*, 455 U.S. 931 (1982) (for consideration in light of *Community Communications Co. v. City of Boulder*), *remanded mem.*, 701 F.2d 178 (6th Cir.), *on remand*, 1983-1 Trade Cas. (CCH) ¶ 65,356 (N.D. Ohio April 6, 1983), *aff'd*, 742 F.2d 949 (6th Cir. 1984); *Shrader v. Horton*, 471 F. Supp. 1236 (W.D. Va. 1979), *aff'd*, 626 F.2d 1163 (4th Cir. 1980); *Alpin v. Henson*, 392 F. Supp. 813 (D. Md. 1975), *aff'd*, 538 F.2d 85 (4th Cir. 1976), *cert. denied*, 429 U.S. 960 (1976), *amended*, 552 F.2d 1033 (4th Cir. 1977), *cert. denied*, 434 U.S. 823 (1977); *Padgett v. Louisville & Jefferson County Air Bd.*, 492 F.2d 1258 (6th Cir. 1974); *E.W. Wiggins Airways, Inc. v. Massachusetts Port Auth.*, 362 F.2d 52 (1st Cir. 1966), *cert. denied*, 385 U.S. 947 (1966); *Mercy-Peninsula Ambulance, Inc. v. County of San Mateo*, 1984-2 Trade Cas. (CCH) ¶ 66,264 (N.D. Cal. Aug. 8, 1984); *Midway Airlines, Inc. v. County of Westchester*, 584 F. Supp. 436 (S.D.N.Y. 1984); *Mays v. Hosp. Auth.*, 582

unhappy rivals refer to this practice with various labels. "Refusal to deal" and "exclusive dealing" arrangements are favorites, along with a related catch-all phrase, "boycott."⁴¹ Where the agreement is with a supplier, the rivals may also claim that the practice creates a monopoly in the market consisting of the local government's purchases. This arrangement between local government and its suppliers is used in countless situations, but it serves a limited number of functions. Some of those functions are best illustrated by garden-variety uses, and others by more striking ones.

A. *Deducing Functions*

Consider first a garden-variety use, the one that was attacked in *Pinehurst Airlines, Inc. v. Resort Air Services, Inc.*⁴² In North Carolina, the Moore County Board of Commissioners had made arrangements with Resort Air Services for Resort to serve as a fixed base operator at the county's Southern Pines Airport. All fixed based operators sell aviation fuel, lubricants, and aircraft maintenance and storage. Some of them sell and rent aircraft, charter flights, and offer flying lessons.⁴³ The Board apparently leased a portion of the airport to Resort, and Resort promised to sell a number of products and services to airport patrons.⁴⁴ Having made those arrangements, the Board allegedly refused to make similar ones with Pinehurst Airlines, a would-be rival of Resort.⁴⁵ That re-

F. Supp. 425 (N.D. Ga. 1984); *Campbell v. City of Chicago*, 577 F. Supp. 1166 (N.D. Ill. 1983); *Cincinnati Riverfront Coliseum, Inc. v. City of Cincinnati*, 556 F. Supp. 664 (S.D. Ohio 1983); *Jonnet Dev. v. Caliguiri*, 558 F. Supp. 962 (W.D. Penn. 1983); *Hopkinsville Cable TV, Inc. v. Pennyroyal Cablevision, Inc.*, 562 F. Supp. 543 (W.D. Ky. 1982); *Crocker v. Padnos*, 483 F. Supp. 229 (D. Mass. 1980); *Tulsa County Pub. Health Nursing Serv., Inc. v. Tulsa City-Co. Health Dep't*, 475 F. Supp. 152 (N.D. Okla. 1979); *Continental Bus Sys., Inc. v. City of Dallas*, 386 F. Supp. 359 (N.D. Tex. 1974); *Azzaro v. Town of Branford*, 1974-2 Trade Cas (CCH) ¶ 75,337 (D. Conn. Nov. 4, 1974); *Murdock v. City of Jacksonville*, 361 F. Supp. 1083 (M.D. Fla. 1973).

41. "Boycott" could be substituted for almost any other label commonly affixed to alleged antitrust offenses. See R. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 207-11 (1976).

42. 476 F. Supp. 543 (M.D.N.C. 1979).

43. *Id.* at 548 & n.1.

44. *Id.* at 547-48 & n.1.

45. *Id.* at 555 & n.19. The opinion does not reveal whether Pinehurst alleged that the Board refused to make such an arrangement pursuant to an explicit agreement. See *id.* at 549 & n.4. Pinehurst may have merely alleged that the Board and Resort perceived that the Southern Pines Airport had limited facilities suitable for a fixed based operator, and that the construction of new ones would be expensive. Believing that the other party shared those perceptions, Pinehurst may have understood that the Board would refuse to make arrangements for FBO service with any enterprise other than Resort. Legally, little, if anything, turned on which allegation Pinehurst had made—functionally, nothing turned on it.

fusal prevented Pinehurst from serving as a fixed based operator de jure. Pinehurst, however, was already a user of airport facilities and structures, so it could easily have sold to airport patrons some of the products or services sold by Resort. To prevent Pinehurst from serving as a fixed based operator de facto, the Board allegedly took the additional step of denying a request for maintenance space, thereby making it prohibitively costly for Pinehurst to operate.⁴⁶

Pinehurst claimed, inter alia, that the Board's course of conduct, a garden-variety use of the practice analyzed here, ran afoul of Section one and Section two of the Sherman Act. The Board and Resort allegedly conspired to prevent Pinehurst from competing in the market for the services of fixed based operators at the Southern Pines Airport⁴⁷ and to monopolize that market.⁴⁸ Pinehurst could have invoked other antitrust labels, such as "monopolizing" or "attempting to monopolize" the market,⁴⁹ "boycotting,"⁵⁰ and "conspiring to exclude"⁵¹ Pinehurst from the market.

46. *Id.* at 555 & nn.19-20. Pinehurst also alleged that the Board denied it a fuel facility to serve aircraft other than that of Pinehurst and that it treated Pinehurst differently from Resort with regard to improvement generally. Moreover, Pinehurst claimed that the Board made deceptive and false representations about it to the F.A.A., levied "inflated" electricity charges, required it to file financial statements, and helped Resort harass it. Finally, presumably to add insult to injury, Pinehurst asserted that the Board insisted that it deal with the airport through Resort. *Id.*

47. *Id.* at 550-55.

48. *Id.* Resort's motion to dismiss for failure to state a claim upon which relief could be granted was grounded, in part, on what it argued was Pinehurst's failure to allege the relevant geographic and product markets. *Id.* at 551. The court rejected that argument, observing that Pinehurst did allege that (1) "the Airport is the only one in Moore County that is federally funded and equipped to service passenger air service for the Southern Pines resort community," and that (2) "Resort enjoys the position as the sole FBO at the airport." *Id.* Apparently, the first observation suggested to the court that the airport was the geographic market; the second one implied that the alleged product market was the one for all goods "required and used by customers of the airport FBO." *Id.* On that "analysis," almost every exclusive franchise at a major public facility would constitute a monopoly.

49. For cases so labelling the practice, see *E. W. Wiggins Airways, Inc. v. Massachusetts Port Auth.*, 362 F.2d 52 (1st Cir.), *cert. denied*, 385 U.S. 947 (1966); *Pueblo Aircraft Serv. Inc. v. City of Pueblo*, 498 F. Supp. 1205 (D. Colo. 1980), *aff'd*, 679 F.2d 805 (10th Cir. 1982), *cert. denied*, 103 S. Ct. 762 (1983); *Alphin v. Henson*, 392 F. Supp. 813 (D. Md. 1975), *aff'd*, 538 F.2d 85 (4th Cir.), *cert. denied*, 429 U.S. 960 (1976), *amended*, 552 F.2d 1033 (4th Cir.), *cert. denied*, 434 U.S. 823 (1977); *Metro Cable Co. v. CATV of Rockford, Inc.*, 375 F. Supp. 350 (W.D. Ill. 1974), *aff'd*, 516 F.2d 220 (7th Cir. 1975); *Murdock v. City of Jacksonville*, 361 F. Supp. 1083 (M.D. Fla. 1973).

50. For cases so labelling the same practice, see *Corey v. Look*, 641 F.2d 32 (1st Cir. 1981); *Metro Cable Co. v. CATV of Rockford, Inc.*, 375 F. Supp. 350 (W.D. Ill. 1974), *aff'd*, 516 F.2d 220 (7th Cir. 1975).

51. For cases so labelling the same practice, see *Pueblo*, 498 F. Supp. 1205; *Guthrie v. Genesee County*, 494 F. Supp. 950 (W.D.N.Y. 1980); *Huron Valley Hosp., Inc. v. City of*

All labels describe, albeit incompletely, the Board's course of conduct. In addition, because of the misleadingly pejorative language, none of the labels reveal the true objection to the Board's course of conduct.

The court never ascertained the true objection. If the court had properly analyzed the issues raised by the motions that were pending before it, there would be no need to ascertain the true objection because none of those issues bore on the merits of Pinehurst's claim.⁵² Unfortunately, the court analyzed one of them, the governmental exemption issue, as if there were a need.⁵³ The issue was whether the Board's alleged course of conduct could be scrutinized under the federal antitrust statutes.

Apparently,⁵⁴ the court reasoned that because the alleged course of conduct was "anticompetitive,"⁵⁵ the North Carolina legislature must not have authorized the conduct when it empowered⁵⁶ counties to establish and operate airports, and to lease por-

Pontiac, 466 F. Supp. 1301 (E.D. Mich. 1979), *vacated and remanded*, 666 F.2d 1029 (6th Cir. 1981).

52. Both the private and governmental defendants moved for dismissal pursuant to Federal Rules of Civil Procedure 12(b)(1) & (6). These motions raised issues relating to standing, exhaustion of remedies, primary jurisdiction, subject matter jurisdiction (nexus to interstate commerce), statute of limitations, and market definition, as well as state action "immunity."

53. 476 F. Supp. 543, 551-56 (M.D.N.C. 1979).

54. The court's unfocused discussion of the "governmental exemption" issue permits only a qualified statement of the court's reasoning. Moreover, particularly confusing is the court's much ado about the North Carolina statute empowering local governments "to determine . . . the terms and conditions under which . . . properties [which they control] may be used, provided that in all cases the public is not deprived of its rightful, equal, and uniform use of such property." N.C. GEN. STAT. § 63-53(5) (1975). The court stated that this statute showed that the North Carolina Legislature had not contemplated the challenged practice because that practice prevented the public from equal and uniform use. 476 F. Supp. at 554-55. But the court must not have meant what it said, for the practice only limited equal and uniform use by would-be airport concessionaires.

55. 476 F. Supp. at 551, 553. What the court meant by "anticompetitive" is not clear. " 'Competition' may be read as [1] the process of rivalry; . . . [2] the absence of restraint over one person's or firm's economic activities by any other person or firm; . . . [3] that state of the market 'in which the individual buyer or seller does not influence the price by his purchases or sales'; . . . [4] the existence of 'fragmented industries and markets' preserved 'through the protection of viable, small, locally owned businesses'; or . . . [5] a term of art, designating any state of affairs in which consumer welfare cannot be increased by moving to an alternative state of affairs through judicial decree." R. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* 58-61 (1978). For the reasons suggested by analyst Bork, only the latter is suitable for the purposes of antitrust law. If, however, the court meant that the transaction between the Board and Resort decreased consumer welfare, then it was mistaken.

56. The North Carolina statute empowers a local government "[t]o determine the charge or rental for the use of any properties under its control . . . and the terms and

tions of them in connection with those activities.⁵⁷ Therefore, applying *Lafayette*, the court concluded that the Board's actions were subject to scrutiny under the federal antitrust statutes.

The conclusion may have been correct, but the analysis was flawed. The court ignored the Supreme Court's cautionary language in *Lafayette* about inferring state authorization and direction.⁵⁸ More importantly, it confused legality with immunity.⁵⁹ Nevertheless, the court should have ascertained the true objection to the Board's course of conduct before pronouncing it anticompetitive.⁶⁰

To determine the true objection, the court would have had to first ascertain the function that the Board's course of conduct, the "practice," was supposed to serve. Careful observation of the economic context in which the Board used the practice would have revealed that it was part of a transaction whereby the Board purchased a service from Resort. That may seem counter-intuitive because the transaction did not require the Board to transfer money to Resort, whereas under the lease, Resort did transfer money to

conditions under which such properties may be used" N.C. GEN. STAT. § 63-53(5) (1981). Those "charges," the statute provides, "shall be . . . established with due regard to the property and improvements used and the expense of operation to the municipality." *Id.* It could be argued that § 63-53(5) directs local governments to try to capture as cost-effectively as possible the quasi-rents generated by properties they control, which is what the Moore County Board was apparently doing.

57. *Cf. Guthrie*, 494 F. Supp. 950. Guthrie complained, inter alia, that the county had violated the antitrust laws by (1) making arrangements with Prior Aviation Service to replace Guthrie's Batavia Aviation as the fixed base operator at the county's airport and then refusing to make similar arrangements with him, and (2) taking additional steps in concert with Prior, who also served as the airport manager, to make sure that Batavia could not continue to use the airport to sell any products or services to airport patrons commonly sold by fixed base operators. The county moved to dismiss the complaint for failure to state a claim upon which relief could be granted. One of the grounds for its motion was "that the Sherman Act does not apply to conduct undertaken by a local government . . . pursuant to state legislation which authorizes a restriction of competition." *Id.* at 953. In fact, New York law expressly provides for the exclusive lease of portions of airports for the availability of various services. N.Y. GEN. MUN. LAW § 352(5) (Consol. 1982). Nevertheless, the court denied the motion on the same analysis employed by the *Pinehurst* court.

58. The Court opined that it would infer state authorization or direction when it found "from the authority given a governmental entity to operate in a particular area, that the legislature contemplated the kind of action complained of." 435 U.S. 389, 415 (1975) (quoting the decision of the court of appeals, 532 F.2d 431, 434 (5th Cir. 1976)).

59. Areeda, *Antitrust Immunity for "State Action" after Lafayette*, 95 HARV. L. REV. 435 (1981).

60. The opinion contains the assertion that "[t]he [c]ourt expresses no opinion as to whether any antitrust violation has occurred. . . ." but that assertion is belied by the key role played by the "anticompetitive" label in the court's reasoning as well as the tenor of the opinion. 476 F. Supp. at 555.

the Board. An explanation may be necessary.

The Board managed an airport on behalf of the taxpayers of Moore County, the "owners."⁶¹ Presumably, the Board, like the management of any private enterprise took actions calculated to maximize the value to the airport.⁶² In this context, "value of the airport" means the expected value, discounted to its present value, of the stream of income which the Board could use the airport to generate. Apparently, the Board believed that the value of the airport would be increased if it arranged to use some of the facilities and personnel at the airport to meet the demand of patrons for products and services which are typically sold at other airports by fixed base operators (FBO). Meeting that demand is itself a service which, for lack of a better name, shall be called FBO service.

The Board could have arranged for FBO service either hierarchically, by directing one or more of its employees to provide it, or across a market, by entering into a contract.⁶³ Regardless of which method the Board chose, it would have had to pay for FBO service. Had the arrangements been hierarchical, it would have been obvious that the Board was paying. Its employees would have been selling products and services to airport patrons, and they would have looked to the Board for their wages.⁶⁴ Under the more complex arrangements that the Board actually made, which were across a market, the Board's payment for the services was not so obvious. In fact, it might seem that the Board cleverly obtained FBO services for free. The Board probably did obtain services for less than it would have paid had the arrangements been hierarchical. On the basis of our wealth-maximizing assumption, we may presume that the Board arranged for services across a market be-

61. Identifying the taxpayers as the owners and the local government as their agent is consistent with the mandated assumption that local governments act to maximize the wealth of those they represent. Of course, as individuals, the taxpayers held rather limited rights in the airport, to say the least. For example, if a taxpayer wished to divest himself of his "interest" in the airport, he would have had to leave Moore County. Nevertheless, as a group, the taxpayers possessed the usual incidents of ownership. They even have the collective right to any residual income generated by the operation of the airport whose value they could capture via a reduced tax assessment.

62. Recall the mandated assumption that local governments act to maximize the wealth of the residents of the governed community.

63. The distinction between the two is not nearly so stark as the text may imply. In fact, they merely identify two ends of a continuum. See O. WILLIAMSON, *MARKETS AND HIERARCHIES: ANALYSIS AND ANTITRUST IMPLICATIONS* (1975); Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386 (1937); Klein, Crawford & Alchian, *Vertical Integration Appropriate Rents, and the Competitive Contracting Process*, 21 *J. LAW & ECON.* 297 (1978).

64. Wages reflect only the most obvious costs that the Board would have had to pay.

cause it believed that it would be cheaper to do so.⁶⁵ Nonetheless, the Board did pay. When the Board entered into the contract with Resort, it gave up the opportunity to earn a stream of income from sales that could have been made by its employees. Such opportunities are frequently called concessions or franchises. That concession was worth quite a bit of money, probably just a bit less than the present value of Resort's expected net revenues. The Board transferred it to Resort in return for FBO services.

The lease, pursuant to which Resort transferred money to the Board, can now be seen in proper perspective. The lease itself was really incidental to a more complex transaction, pursuant to which the Board transferred a concession to Resort. Thus, while it is true that Resort rented a portion of the airport which the Board controlled, it is equally true, and far more significant in terms of value as well as antitrust law, that the Board rented some of the equipment and personnel which Resort controlled. When the Board engaged in the practice challenged by Pinehurst, it was purchasing FBO service from Resort. That was the economic reality which the court apparently failed to grasp.

Had the court understood the economic realities, it would have had grave doubts about the validity of Pinehurst's complaint since it would have been painfully obvious that the Board had no discernible interest in restricting the output of FBO service. It is unlikely that the Board entered into the transaction with Resort for the purpose of making a transfer payment. Fixed based operators are probably too successful to qualify for charity and too weak to command subsidies. It is even less likely that the Board entered into it for strategic purposes. The airport probably had neither existing rivals to drive from the market nor any potential rivals to keep out. Even if it had, it is difficult to see how the Board's arrangements with Resort could have effectuated either goal. Given the relatively large number of would-be fixed base operators and the relatively small start-up costs of becoming one, those arrangements probably would have had no effect on the ability of an existing or potential rival airport to obtain FBO service.⁶⁶ As an ordi-

65. That belief may have occurred because, pursuant to the contract, Resort would have the same incentives to provide fbo service that the Board had, thus obviating the need for expensive monitoring. See Alchian & Demsetz, *Production, Information Costs, and Economic Organization*, 62 AM. ECON. REV. 777 (1972).

66. It is also rather unlikely that Resort was engaged in a strategic maneuver not only because of the reasons stated in the text but also because the Board probably would have captured all of the expected monopoly revenues in the form of "rent."

nary purchaser, of course, the Board would have been interested in expanding output. The grave doubts engendered by these observations might have prompted the court to systematically study the functions that the challenged practice was supposed to serve.

The Board's refusal to make arrangements with Pinehurst for FBO service was likely aimed at serving an instrumental function in the complex sales transaction between it and Resort.⁶⁷ Generally, that function was to help secure the transaction's benefits, or otherwise reduce the costs associated with the transaction. The question is, how could the Board's refusal produce those results?

There are two ways the Board could have benefited by promising to make arrangements with Pinehurst. First, their action might have created the most efficient way of providing that service. Recall the presumption that the Board acts in a manner calculated to maximize the value of the airport. Necessarily, then, the Board would permit the use of airport-connected resources to provide FBO service only up to the point that they added more to the value of the airport than they would add if put to some other use. With those limited resources, it is plausible that FBO service could be most efficiently provided, all else being equal, by a single operator. That "natural monopoly" might reflect scale economies in "producing" the service. It might, however, also reflect economies either in coordinating the delivery of the service with other airport-related activities, like departures and arrivals, or in adapting that delivery to major changes promoted by significant maintenance projects or structural modifications.⁶⁸ The Board's promise would have assured the chosen operator of the opportunity to provide efficient service throughout the entire term of the agreement. That assurance would have raised the expected value of the operator's net revenues and, thereby, the actual value of that portion of the airport which the operator was to lease. Thus, the Board could have obtained more "rent." Of much greater significance, the Board could have also obtained more revenues from airport patrons. If the FBO service was provided efficiently, the service would make its maximum possible contribution to the value of the

67. Of course, the Board may have refused to make arrangements with Pinehurst because one of the members of the Board wanted to do a favor for his friend, a principal shareholder of Resort, but that is not what is important for the purposes of antitrust analysis.

68. These planning economies provide one of the principal inducements for entering into requirements contracts, of which the arrangements between Board and Resort is but one example. See generally *Standard Oil Co. v. United States*, 337 U.S. 293 (1949).

airport. By promising to make arrangements with Pinehurst, the Board, entering into the transaction, achieved its goal.

The second way of effectuating a gain is related not to efficiency in providing the service, but in arranging for it. By making its promise to Pinehurst, the Board could have avoided substantial transaction costs. These costs are among the things least likely to be equal. Obviously, the Board bore fewer negotiating costs by entering into only one transaction rather than two or more.⁶⁹ Less obviously, but more importantly, the Board may have borne lower monitoring costs than it otherwise would have.⁷⁰ Monitoring, along with contract enforcement, is required to limit opportunism—"making false or empty, that is, self-disbelieved threats or promises,"⁷¹ and "cutting corners for undisclosed personal advantage, covering up tracks, and the like."⁷² Limiting opportunism, that is controlling cheating, is the key to "the viability of a pattern of exchange."⁷³ That is not to say that all economic actors, or even all fixed based operators, would cheat. But some would, and it is expensive to sort out the cheaters and the noncheaters.⁷⁴ Monitoring a fixed based operator by conventional methods, with inspection, may have appeared ineffectual or, if effectual, expensive. The Board may have believed that it would be more cost-effective to induce satisfactory performance by permitting the operator to earn returns which would be put at risk, like a hostage, if the operator acted opportunistically.⁷⁵

The Board could have also used its promise to help capture some of the quasi-rents generated by the investment in the airport. A "quasi-rent [is] [a]ny payment that does not affect the amount

69. The Board might have found itself bearing additional negotiating costs in the future if it decided to replace the single provider. There is no reason to believe, however, that the Board would make the decision to replace any more often if it had a single provider than if it had several providers.

70. "'Monitoring' connotes several activities in addition to its disciplinary connotation. It connotes measuring output performance, apportioning awards, observing the output behavior of inputs as a means of detecting or estimating their marginal productivity, and giving assignments or instructions in what to do and how to do it. (It also includes . . . authority to terminate or revise contracts.)". Alchian & Demsetz, *supra* note 65, at 783 (monitoring and the importance of monitoring costs in determining economic organization is the central focus of this article).

71. E. GOFFMAN, *STRATEGIC INTERACTION* 105 (1969).

72. Williamson, *supra* note 22, at 957.

73. Hirshleifer, *Economics from a Biological Standpoint*, 20 *J. LAW & ECON.* 1, 27 (1977).

74. Williamson, *supra* note 22, at 957.

75. See Klein, Crawford & Alchian, *supra* note 63, at 303-07.

[of a good] *currently* available but will affect the *future* amount."⁷⁶ Specialized capital assets are prime generators of quasi-rents. By making its promise, the Board eliminated the possibility of any competition for airport patrons among fixed base operators at the Southern Pines Airport. By eliminating that possibility, the Board created an opportunity, albeit an evanescent one, for the chosen operator to appropriate some of those quasi-rents. Would-be operators could be expected to compete for that opportunity. They would do so by offering lump-sum or installment payments which might take the form of a franchise, or a license fee, or additional "rent."⁷⁷ It would be reasonable to expect that in the process of competing, at least one of the operators would be driven to offer a payment almost as great in value as the quasi-rents which they had hoped to appropriate.⁷⁸ The Board could accept such an offer and thereby capture those quasi-rents, or at least most of them, for itself and its constituent taxpayers. This may appear to be yet a third way for the Board to gain by making its promise, but this appearance is deceiving. The Board's gain would stem from the avoidance of substantial transaction costs. The Board could capture some of the quasi-rents as long as it contractually prevented unlimited competition between operators for the patronage of airport customers. A variety of stratagems would do that, but making the promise the Board allegedly made was likely the most cost-effective one.

To summarize, the challenged practice was probably supposed to serve one or both of two basic instrumental functions. First, it might have helped secure efficient FBO service. Second, it might have helped reduce the costs of negotiating and, especially, monitoring and enforcing arrangements for that service.⁷⁹ It also permitted the capturing of some quasi-rents generated by the taxpayers' investment in portions of the airport used in providing that service.

A similar explanation could apply in most instances in which a local government enters into an agreement with suppliers, or pur-

76. A. ALCHIAN & W. ALLEN, *EXCHANGE AND PRODUCTION: COMPETITION, COORDINATION, AND CONTROL* 99 (2d ed. 1977). Quasi-rents are closely related to economic rents which are "market receipts that affect neither the present nor the future amount of that good." *Id.* For an excellent analysis of quasi-rents as a determinant of economic organization, see Klein, Crawford & Alchian, *supra* note 63.

77. Here I use the word in its lay rather than in its technical sense. Sometimes, but not always, "rent" payments reflect quasi-rents.

78. See generally Demsetz, *Why Regulate Utilities?* 11 J. LAW & ECON. 55 (1968).

79. A. ALCHIAN & W. ALLEN, *supra* note 76, at 110.

chasers, pursuant to which it declines to buy from, or sell to, some or all of their rivals. That practice, of which the Board apparently made garden-variety use, is usually employed to serve the same kind of functions as those which were supposedly served by the Board's alleged promise.⁸⁰ Indeed, it is often supposed to serve those functions even when put to more striking use, as when the cities of Dallas and Fort Worth used it in arranging for taxicab service at the Dallas/Fort Worth (D/FW) Regional Airport, the focus of the controversy in *Woolen v. Surtran Taxicabs, Inc.*⁸¹

In the 1960's and early 1970's the cities of Dallas and Fort Worth had the Texas-sized, multiterminal D/FW Regional Airport (Airport) built in a relatively undeveloped area between the two cities. They created an Airport Board to manage it, and they also created the D/FW Surtran System (System), a joint venture charged with the responsibility of ensuring that an adequate ground transportation network served the Airport. The network was to include an inter-terminal shuttle, one or more modes of mass transportation, and most importantly, for this discussion, taxicab service.

The System discharged that responsibility, in part, by auctioning off the exclusive right to pick up passengers and transport them from the Airport to all points in the ten surrounding counties. The Airport Board decided to make this right exclusive. The cities of Dallas and Fort Worth, and two smaller cities in which portions of the Airport are located, enacted similar ordinances of exclusivity.⁸² The ordinance barred anyone who had not obtained a permit issued by the Airport Board from offering for-hire ground transportation from the Airport. The Board decided to issue a permit for taxicab service only to the winner of the System's auction. It is unclear from the court's opinion whether the city enacted the ordinance and the Board made its decision prior to the auction, but it cannot be seriously doubted that the Board induced the par-

80. For examples of when it probably did so when local government defendants used it, see *Corey v. Look*, 641 F.2d 32 (1st Cir. 1981); *E. W. Wiggins Airways, Inc. v. Massachusetts Port Auth.*, 362 F.2d 52 (1st Cir. 1966), *cert. denied*, 385 U.S. 947 (1966); *Pueblo Aircraft Serv., Inc. v. City of Pueblo*, 498 F. Supp. 1205 (D. Colo. 1980), *aff'd*, 679 F.2d 805 (10th Cir. 1982), *cert. denied*, 459 U.S. 1126 (1983); *Guthrie v. Genessee County*, 494 F. Supp. 950 (W.D.N.Y. 1980); *Alpin v. Henson*, 392 F. Supp. 813 (D. Md. 1975), *aff'd*, 538 F.2d 85 (4th Cir. 1976), *cert. denied*, 429 U.S. 960 (1976), *amended*, 552 F.2d 1033 (4th Cir. 1976), *cert. denied*, 434 U.S. 823 (1977); *Metro Cable Co. v. CATV of Rockford, Inc.*, 375 F. Supp. 350 (W.D. Ill. 1974), *aff'd*, 516 F.2d 220 (7th Cir. 1975); *Murdock v. City of Jacksonville*, 361 F. Supp. 1083 (M.D. Fla. 1973).

81. 461 F. Supp. 1025 (N.D. Tex. 1978).

82. The cities are Irving and Grapevine, Texas.

ticipants in the auction to prepare their bids on the basis that the winner would obtain an exclusive right.

The winner was Surtran Taxicabs, Inc. (Surtran), a joint venture of Yellow Cab of Dallas, Inc., and Fort Worth Cab and Baggage. Surtran offered to pay the System seventy-five cents per trip and fifty percent of all "profits" in excess of a five percent "operating profit."⁸³ It may have also offered to pay an additional lump-sum fee for the permit, but the court's opinion does not reveal whether it did or not. Pursuant to the contract that the parties signed following the auction, Surtran agreed to supply, at set rates, something akin to the taxicab service requirements of arriving passengers at the Airport, and to pay the System in accordance with the terms of its bid.

These arrangements were the source of considerable unhappiness among some licensed taxicab operators in the ten counties surrounding the Airport. Dallas and Fort Worth refused to let those operators pick up passengers at the Airport. Several of those operators, including John Woolen, filed a class action suit challenging that refusal as violative of sections one and two of the Sherman Act.⁸⁴ The cities moved to dismiss the suit for failure to state a claim upon which relief could be granted, which should have, but did not, prompt the court to determine the true objection to the cities' practice.⁸⁵

83. 461 F. Supp. 1025, 1027 (N.D. Tex. 1978). "Profit" has so many meanings that it is not clear from the court's opinion precisely how the word was used in the agreement between the System and Surtran. "Operating profit" is, if anything, more nebulous.

84. The opinion does not reveal what labels, if any, plaintiff's counsel tried to affix to the practice. Perhaps that is because, mercifully, the court did not completely succumb to the allure of literalistic jurisprudence—resolving disputes largely on the basis of whether plaintiff's counsel "proves," necessarily by analogy, that some pejorative label "fits" a practice. For a more extended description and analysis of this type of judicial decision-making, see articles analyzing the opinions of the United States Court of Appeals for the Seventh Circuit: Lee, *Antitrust: Market Definition, The Section Two Offenses and Literalism*, 57 CHI.-KENT L. REV. 25 (1981); Lee, *Antitrust: A Collage of Vertical Territorial Restraints, Tying and Monopoly "Misuse," Arbitrability, and the General Dynamics Defense*, 55 CHI.-KENT L. REV. 1 (1979); Lee, *Economic Regulation of Business: The Seventh Circuit's Non-Economic Approach*, 56 CHI.-KENT L. REV. 205 (1980). It did, however, make some related errors. See *infra* text accompanying note 86.

85. In support of their motion, the cities pressed two arguments. The first was that the practice was immune under *Parker v. Brown*, 317 U.S. 341 (1943). The court responded with the same mistaken analysis employed by the *Pinehurst* court. *Woolen*, 461 F. Supp. at 1028. The court reasoned that since the Texas legislature had not contemplated such an "anti-competitive" practice, it was subject to scrutiny under the antitrust statutes. 461 F. Supp. 1025, 1028-33 (N.D. Tex. 1978). The cities' second argument, at least as the court apparently understood it, was that the practice was *per se* legal. *Id.* at 1033. The cities asserted that, as owners of the Airport, they could exclude any commercial enterprise from airport

Had the court done so, it could have begun its analysis by observing that the cities used this practice in the context of purchasing a service. To them, the service was meeting the taxicab transportation requirements of arriving passengers at the Airport. The cities could have arranged for that service by using one of two basic methods. They could have purchased vehicles, hired drivers, and then directed that the System provide the service hierarchi-

property without committing an antitrust offense. *Id.* at 1036. Therefore, the plaintiffs were not entitled to any relief under the Sherman Act. *Id.* at 1033.

The court's response to this second argument was two-pronged. The first prong consisted of a line of analogical reasoning which, in the final analysis, begged the question. It might be unlawful, began the court, for a monopolist, even one who had acquired his market power lawfully, to agree to sell his products exclusively to one distributor. *Id.* at 1037-38. For the purposes of the motion to dismiss, the challenged practice was to be treated as analogous to such an agreement. *Id.* at 1039. The cities, taken together, were to be treated as a monopolist. After all, "ownership of land," stated the court, "may because of its unique location or other property attributes give to the landowner a specie of natural monopoly. . . ." *Id.* at 1037, meaning, presumably, the opportunity to obtain quasi-rents. Denying entry to such land to all but one vendor of a particular kind of service could have the same effect as a monopolist's exclusive distribution agreement. *Id.* Therefore, the court concluded, the cities' refusal to let those taxicab operators unaffiliated with Surtran pick up passengers at the Airport might be unlawful. *Id.* at 1040.

The analogy is surprisingly apt. The court did not explain, however, why a court should ever consider a monopolist's exclusive dealing agreement unlawful. In fact, such an agreement would be objectionable on consumer welfare grounds only if the monopolist entered into it strategically for the purpose of disrupting the optimal distribution patterns of potential rivals. See Williamson, *supra* note 22, at 952, 960-66. Such behavior could not possibly be successful unless the dealers' activities required investments in rather specialized assets. *Id.* at 964. Only under such circumstances, if at all, would it likely be observed. Of course, the court may be forgiven for its omission because it may have reasonably believed that no explanation was necessary in the light of then existing authority. See, e.g., L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST 429-31 (1977) (citing cases). Nevertheless, it is that omission which obscures the flaw in the court's line of reasoning. To provide the missing explanation, the court would have had to engage in a two-step inquiry: (1) what functions are likely served by a monopolist's exclusive distribution agreement? and (2) according to what principles might those functions be deemed objectionable? That is substantially the same inquiry as the one the court should have made in order to determine whether the cities' practice was per se legal. Thus, the first prong of the court's response was begging the question.

The second prong was no more than a non sequitur. The cities' property rights, stated the court, had to give way to the policy of the Sherman Act, particularly when those rights had been "diluted" by the dedication of the airport for public purposes. 461 F. Supp. 1025, 1038 (N.D. Tex. 1978). It is not at all clear why property rights would ever have to give way to the policy of the Sherman Act unless that policy were one calling for wealth redistribution. See generally Coase, *The Problem of Social Cost*, 3 J. LAW & ECON. 1 (1960). Even assuming that it is clear how the court is to balance property rights and the policy of the Sherman Act, the relevance of dedication to public purposes is not. The court's discussion of airport solicitation cases is inapposite. That statement is simply beside the point of the cities' argument, which was, in essence, that the way in which they exercised their property rights was necessarily consistent with that policy. Thus, the court, in effect, substituted two logical fallacies for an inquiry into the function of the challenged practice.

cally. Alternatively, they could have arranged for the service across the market in a myriad of ways. For example, they could have permitted unrestricted use of airport roads, and then relied on self-interested taxicab operators for the service. As another option, the cities could have purchased the service pursuant to a more well defined contract.⁸⁶ Obviously, they chose to do the latter, presumably because it was more cost-effective. An instrumental part of this sales transaction was the cities' promise to make arrangements for taxicab transportation from the Airport with only one company.

It might appear that the cities, in making such a promise, could not secure efficient taxicab transportation. After all, at most large airports, taxicab operators affiliated with several companies solicit business. That would not be the case if a single company could provide taxicab transportation more efficiently. That assumption, however, could well be incorrect. A sole supplier of airport taxicab transportation might have an advantage over several competing companies because of reduced congestion problems. Suppose that airport congestion is such that, all else being equal, a reduction in the supply of taxicab transportation would be efficient. One would expect a sole supplier to make that reduction since he would reap most of the benefits. Despite bearing most of the operating costs, there is the expectation that the benefits would exceed those costs. One would not necessarily expect several suppliers, acting independently, to do the same. Each one would fear the prospect of bearing the costs of such a reduction while reaping none, or a small fraction, of the benefits. Coordinated action might solve the problem, but the cost of arranging and monitoring such action might be prohibitive. If this advantage were quantitatively significant, a sole supplier might be able to provide airport taxicab service more efficiently than several suppliers. To exploit this advantage, however, a taxicab company would have to secure the exclusive right to pick up passengers at the airport. The cost of securing that right might be prohibitive. If the supplier purchased the rights from other taxicab companies, enforcement costs might well be substantial. Moreover, such purchases would likely spur the strategic entry of other companies anticipating a buy out.⁸⁷ Thus, even though a single company might provide taxi-

86. Permitting unrestricted use of airport roads and then relying on self-interested taxicab operators for the desired service may be characterized as a less well defined contract pursuant to which unrestricted use is exchanged for the service.

87. If the rights had been purchased from an airport board which had in the past permitted unrestricted use, then realignment costs might have been larger. See Demsetz, *Some*

cab transportation more efficiently than several companies, the fact remains that taxicab operators affiliated with several companies solicit business at most large airports. The result is that by promising to make arrangements for taxicab transportation from the Airport with only one company, Dallas and Fort Worth may have helped secure the delivery of that service more efficiently.

It is even more likely that by promising exclusivity Dallas and Fort Worth helped reduce the costs of negotiating, and especially monitoring, the taxicab service. Had they made arrangements with several companies, they would have had to negotiate not only more than one contract, but also, the potentially delicate interrelationships existing among the operators of those companies.⁸⁸ Perhaps more importantly, to ensure satisfactory performance under the contracts, the cities might have had to engage in disproportionately more monitoring, like data gathering, supervision, and other relatively expensive activities, than they would have had otherwise had they made arrangements with but one provider. This is particularly true when the provider fears the losing of returns to exclusivity. This fear often induces satisfactory performance.

It is highly likely that by promising to make arrangements with only one company, the cities helped to reduce the costs of capturing some of the quasi-rents generated by the taxpayer's investment in the Airport. By so promising, the cities practically assured themselves that the System's auction for the right to pick up passengers would elicit offers to make payments equal in value to those quasi-rents. Under the circumstances, one would be hard-pressed to conceive of a less expensive method of doing that.⁸⁹

There is no evidence whatsoever that the cities' promise functioned to insufficiently restrict the output of taxicab transportation from the Airport. It would have been surprising had there been any. It is unlikely that the cities were making either a transfer payment or a strategic move calculated to secure market power. The rationale is similar to that applied to the actions of the Moore County Board.⁹⁰ As the purchasers of a service in a complex sales transaction, the cities were interested in obtaining no less than economically optimal output. No doubt, that interest prompted the

Aspects of Property Rights, 9 J. LAW & ECON. 61, 65-67 (1966).

88. Disputes related to those delicate interrelationships may themselves give rise to antitrust litigation which might ensnare local government. *See, e.g.*, *All Am. Cab Co. v. Metropolitan Knoxville Airport*, 1982-3 Trade Cas. (CCH) ¶ 65, 163 (E.D. Tenn. 1982).

89. *Cf. K. DAM, OIL RESOURCES: WHO GETS WHAT HOW?* (1976).

90. *See supra* text accompanying note 23.

cities to insist that Surtran's rates be prescribed by contract.⁹¹ Had the contract not prescribed the rates, Surtran, as the sole supplier, would probably have found it profitable both to charge higher rates, thereby causing a decline in the amount demanded, and to restrict output.⁹² Under the terms of the contract, the less efficient the output, the less Surtran would pay the cities. The cities would capture less quasi-rents, and Surtran would capture more of them.

That the cities' promises served the same kind of functions as did the Moore County Board's promise suggests, without proving, that those kinds of functions are usually served when a local government enters into agreements with suppliers and purchasers to decline to buy from or sell to some or all of their rivals. This is true regardless of whether the practice of making the promise is put to a striking use, or merely a garden-variety one. Of course, the cities' use of the practice seems striking only because we have come to expect taxicab operators affiliated with several companies to solicit business at major airports. In contrast, most of us have no expectations about the number of fixed based operators we would find at any airport. Those few of us who do have such expectations may well expect to find only one provider at smaller airports.

Occasionally, a local government's use of this practice seems striking not so much because the practice is used in an unconventional context, but because it really is supposed to serve some different, although not completely unrelated, function. These functions are linked not to inducing efficient use of an existing capital facility, but rather to enduring an additional investment in such a facility which itself would represent an efficient use of resources.

The prospect of obtaining quasi-rents induces investment. Thus, whether an investment is made will depend in large part on the amount of quasi-rents it is likely to generate and the proportion of those quasi-rents which the investors are likely to capture. Often, capture poses few, if any, problems. For example, the rivalry between potential suppliers of taxicab transportation and the relatively low cost of replacing one supplier with another—in the event the cities became dissatisfied with the service being rendered—assured the cities of Dallas and Fort Worth of capturing some of the quasi-rents generated by the taxpayers' investment in the Airport.⁹³ Without such assurance, the cities may have put less

91. The rates were probably part of the bid specifications.

92. *Id.* This would be an instance of the general phenomenon of "subgoal pursuit." See Williamson, *supra* note 22, at 955.

93. In the absence of collusion, the System could expect the potential suppliers to com-

capital into the airport, or none at all. Generally, in the absence of such rivalry and low transactions costs, investors might reasonably fear that any quasi-rents generated by their investment would be captured or expropriated by others. They might hesitate to make the investment, which they otherwise would have made, unless before making it they enter into an agreement which provides assurance of capturing those quasi-rents.

A local government might wish to conclude such an agreement either because one or more private enterprises wish to induce it to make an investment on behalf of its taxpayers that it is otherwise hesitant to make, or the local government wishes to induce one or more private enterprises to make an investment that they are hesitant to make. In either case, an integral part of the agreement might very well be the common practice that was attacked in *Pinehurst*⁹⁴ and in *Woolen*.⁹⁵ That was certainly true of the agreements that were the focus of *Hecht v. Pro-Football, Inc.*,⁹⁶ and *Mason City Center Associates v. City of Mason City*.⁹⁷ Congress enacted statutes in 1957 and 1959, authorizing the District of Columbia Armory Board to build a stadium, subsequently named after Robert F. Kennedy, "in order to provide the people of the District . . . [with one] suitable for holding athletic events,"⁹⁸ including professional football games. The Armory Board functioned as a city agency, and was so treated by the courts.⁹⁹ Nonetheless, the legislative history of the authorizing statutes shows that Congress intended to have the Armory Board use private enterprise methods for the management of Robert F. Kennedy (RFK) Stadium.¹⁰⁰

The Armory Board did not initiate construction immediately. Rather, in an effort to carry out Congress's intention, it initiated negotiations for a long-term lease of the proposed stadium with the professional football and baseball teams that played in the District

pete for the exclusive right to pick up passengers at the Airport by offering to purchase that right for a payment almost equal in value to the quasi-rents which they hoped to capture. Given the number of those potential suppliers, collusion was unlikely. The System could also expect this supplier not only to offer the desired service but also to provide it, because the supplier would know that if it welched, there were others who would be only too happy to replace it and could do so quickly.

94. *Pinehurst Airlines, Inc. v. Resort Air Serv., Inc.*, 476 F. Supp. 543 (M.D.N.C. 1979).

95. *Woolen v. Surtran Taxicabs, Inc.*, 461 F. Supp. 1025 (N.D. Tex. 1978).

96. 570 F.2d 982 (D.C. Cir. 1977), *cert. denied*, 436 U.S. 956 (1978).

97. 468 F. Supp. 737 (N.D. Iowa 1979), *aff'd in part, rev'd in part*, 671 F.2d 1146 (8th Cir. 1982).

98. D.C. CODE ANN. §§ 2-1720 to -1721 (1967).

99. *Hecht*, 444 F.2d at 939.

100. *Id.* at 946.

of Columbia. The football team was, and is, the Washington Redskins, whose corporate name is Pro-Football, Inc. Apparently, the Armory Board would not have built the stadium had the negotiations proved fruitless.¹⁰¹

The negotiations were successful. The Armory Board entered into a thirty-year lease with the Redskins, commencing with the start of the 1961 professional football season. The Board then leased the land and built the stadium pursuant to a contract with the Department of the Interior. The focus of the subsequent litigation was a restrictive covenant contained within the lease. The covenant provided that the Armory Board would not lease RFK Stadium to any other professional football team.

In 1965 Norman Hecht and his associates applied to the American Football League (AFL) for an expansion franchise to be located in the District of Columbia. At that time, the AFL was a rival of the National Football League (NFL). The Redskins belonged to the NFL. To have AFL team owners seriously consider his application, Hecht had to make some arrangements for the use of a stadium to play a home game schedule. Apparently, the Armory Board's stadium was the only suitable facility in the District of Columbia,¹⁰² so Hecht offered to lease it for dates on which the Redskins were not scheduled to play. The Armory Board expressed a strong interest in accepting Hecht's offer, as did its landlord, the Secretary of the Interior.¹⁰³ Despite their interest, the Board advised Hecht that it would reject his offer unless the Redskins waived their rights under the restrictive covenant. The Redskins refused to do so. Hecht then sued, among others,¹⁰⁴ the Armory Board and the Redskins. Hecht claimed that the restrictive covenant was a contract in restraint of trade and a device to monopolize the professional football market in the District of Columbia.¹⁰⁵

101. *Id.*

102. It is not clear from the opinions what happened to Griffiths' Park, the stadium where the Redskins, as well as the Washington Senators baseball team, had been playing their home games.

103. Note the all-too-ready willingness to welch, to act opportunistically, on the part of this office-holder. This willingness reduced the value of the promises made on behalf of the government he served. For a discussion of the implications of this phenomenon, see *Gold Cross Ambulance v. City of Kansas City*, 538 F. Supp. 956 (W.D. Mo. 1982), *aff'd*, 705 F.2d 1005 (8th Cir.), *cert. denied*, 105 S. Ct. 1864 (1985); *Mason City Center Assoc. v. City of Mason City*, 468 F. Supp. 737 (N.D. Iowa 1979), *aff'd in part, rev'd in part*, 671 F.2d 1146 (8th Cir. 1982).

104. Hecht also sued the individual members of the Armory Board and the National Football League.

105. Initially, the District Court for the District of Columbia entered judgment for the

An inquiry into the real objection to the restrictive covenant would have revealed that the economic context in which the Board used it was largely identical to that in which the cities of Dallas and Fort Worth made their controversial promise to Surtran. The similarity would have been somewhat easier to see had the Armory Board built RFK Stadium before trying to lease it. Suppose, for analytical purposes, that it had. It now becomes clearer that the Armory Board was trying to maximize the value of the stadium, a capital facility like an airport, by arranging to have professional football games exhibited there. The games added to the value of the stadium in a more dramatic, but similar, manner as meeting the requirements of arriving passengers for taxicab transportation added to the value of the Airport. To the Armory Board, the exhibition of football games was a "service" which it "purchased" from the Redskins in exchange for an opportunity to earn a stream of income. The Armory board "hired" the Redskins just as much as the Redskins "hired" RFK Stadium. Further, assume that the Armory Board had "hired" the Redskins by auctioning off the exclu-

defendants on the ground that, under *Parker v. Brown*, the restrictive covenant was not subject to scrutiny under the Sherman Act. 312 F. Supp. 472 (D.C. 1970) (citing *Parker v. Brown*, 317 U.S. 341 (1943)). The Court of Appeals for the District of Columbia Circuit reversed and remanded for a trial on the merits. 444 F.2d 931 (D.C. Cir. 1971).

The suit was tried by a jury, which reached a verdict for the defendants. The district court entered judgment accordingly, and Hecht appealed. During the trial Hecht had requested that the district court instruct the jury pursuant to the "essential facility doctrine." That doctrine is: "where facilities cannot practicably be duplicated by would-be competitors, those in possession of them must allow them to be shared on fair terms' or stand condemned under the antitrust statutes." 570 F.2d 982, 992 (D.C. Cir. 1977) (quoting A. NEALE, *THE ANTITRUST LAWS OF THE UNITED STATES* 67 (2d ed. 1970)). This peculiar notion, that the antitrust laws require those with market power to share with at least some of their would-be rivals, is also known as the bottleneck doctrine. Apparently, the disposition of a number of reported cases has turned on this notion. *See, e.g.,* *International Boxing Club of New York v. United States*, 358 U.S. 242 (1959); *Associated Press v. United States*, 326 U.S. 1 (1945); *United States v. Terminal R.R. Ass'n of St. Louis*, 224 U.S. 383 (1912); *Rogers v. Douglas Tobacco Bd. of Trade*, 266 F.2d 636 (5th Cir.), *cert. denied*, 361 U.S. 833 (1959); *Gamco v. Providence Fruit & Produce Bldg.*, 194 F.2d 484 (1st Cir.), *cert. denied*, 344 U.S. 817 (1952); *United States v. Standard Oil Co.*, 362 F. Supp. 1331 (N.D. Cal. 1972), *aff'd on appeal*, 412 U.S. 924 (1973). Hecht asked that the jury be told that if it:

found (1) that use of RFK stadium was essential to the operation of a professional football team in Washington; (2) that such stadium facilities could not practicably be duplicated by potential competitors; (3) that another team could use RFK stadium in the Redskins' absence without interfering with the Redskins' use; and (4) that the restrictive covenant in the lease prevented equitable sharing of the stadium by potential competitors, then . . . [it] must find the restrictive covenant to constitute a contract in unreasonable restraint of trade, in violation of the Sherman Act

570 F.2d 982, 993 (D.C. Cir. 1977). The district court denied Hecht's request, which the court of appeals held was error.

sive right to exhibit professional football games at the stadium, and it becomes clear that the restrictive covenant represented the same kind of practice as the one challenged in *Woolen*. Under the hypothesized conditions, the restrictive covenant would likely have served the same kind of functions as did the cities' promise to Surtran not to use any other taxicab supplier. In particular, it would have helped the Armory Board capture the quasi-rents generated by the investment in the stadium.

Under the actual circumstances, giving the Redskins a restrictive covenant probably helped the Board capture the quasi-rents, but it did much more. If the Armory Board had not been assured of capturing those quasi-rents, it would not have built the stadium. Thus, the restrictive covenant helped induce the Armory Board to make what we must presume to be an efficient investment.¹⁰⁶

Contrary to our supposition, of course, the Armory Board tried to lease the stadium before building it. It did so because rivalry on the supply side of the professional football market in the District of Columbia did not assure it of capturing those quasi-rents. Had the Armory Board built the stadium first, it would have found that the Redskins were the only folks interested in obtaining the short-term rights to use the stadium for professional football games. Long-term rights might have generated some interest among speculators hoping to resell them to teams that might be assembled in the future. Given the risk of nonresale, however, such speculators would probably not have offered to pay nearly as much for those rights as the Redskins were prepared to offer. An auction for the short term, or even the long term, rights would have been costly and fruitless. Thus, also contrary to supposition, the Armory Board tried to lease the stadium by negotiating directly with the Redskins.

Given the limited rivalry, if the Armory Board had built the stadium first, the Redskins would likely have offered to lease it for little more than the costs of operating it. That would be far less than the Redskins would have been willing to offer in order to make it worthwhile for the Armory Board to build it. The low-ball offer would have been accepted because the Armory Board would not have had a higher offer to choose from, and rejection would have made the Armory Board worse off. Thus, the Redskins would

106. Because we must assume that the Armory Board acted to maximize the wealth of those whom it represented, the mere fact that it was willing to pay for the stadium shows that the value of the stadium in use exceeded its price.

have captured most or all of the quasi-rents generated by the investment in the stadium. Because rivalry in the professional football market would not assure the Armory Board of capturing the quasi-rents, the Board tried to make contractual arrangements that would afford them this assurance before building the stadium. Those arrangements took the form of a lease.

To assure sufficient capture of the quasi-rents, the lease had to have two key features. First, it had to be long-term.¹⁰⁷ Presumably, the Redskins were willing to make yearly payments equal in value to only a fraction of the quasi-rents. If they had been willing to pay more, then they could have built the stadium themselves. The longer the term of the lease, the greater the capture. A long-term lease also provided some assurance to the Redskins that they would capture the quasi-rents generated by their investment in good-will. Those quasi-rents could be dissipated, in part, if the Redskins had to move their NFL franchise to another metropolitan area because of the inability to renew their short-term lease in the only Washington stadium suitable for playing home games.¹⁰⁸

Of course, entering into a long-term lease incurred costs for both the Armory Board and the Redskins. By doing so, each forewent future opportunities to earn more revenues by making alternative arrangements, and each ran the risk of opportunistic behavior on the part of the other. The Redskins would not have incurred such costs unless they expected the gains from entering into such a lease to be greater than the potential loss. Assuming that the Armory Board acted with a profit motive, they too expected gains to exceed losses. Apparently, for a lease term of thirty years, the sum of the expected gains to the Redskins exceeded the sum of the expected costs by the greatest margin. That the Armory Board obligated itself to repay the principal to its bondholders during the same period may reflect a similar trade-off. Presumably, the Armory Board expected that by doing so, it minimized its capital costs.

The District of Columbia Circuit Court of Appeals heard the appeal in this case and implicitly recognized that the lease had to be long-term to assure sufficient capture of quasi-rents.¹⁰⁹ It did so by acknowledging that the Armory Board would not have built the

107. See Williamson, *The Vertical Integration of Production: Market Failure Considerations*, 61 AM. ECON. REV. 112, 116-17 (1971).

108. The costs of relocating might be substantial, and the costs of building the loyalty of fans in the new locale might be even greater.

109. *Hecht*, 444 F.2d at 934.

stadium unless it had entered into a long term lease with the Redskins. The court did not similarly recognize that the lease also had to be exclusive, the second key feature. It is easy to see why it had to be exclusive if one simply imagines what would have happened had it not been. The Redskins would have perceived a far greater chance of competition for ticket buyers with another football team sometime during the thirty-year term of the lease. They would then have been much less certain that they could charge those ticket buyers enough to cover the quasi-rents generated by the investment in the stadium. Therefore, they would be unwilling to pay as much to the Armory Board. The Armory Board would capture substantially less of those quasi-rents, although, given the limited rivalry in the District of Columbia professional football market, it might have still captured some. Moreover, exclusivity reduced the costs of entering into a long-term lease. Each side would be somewhat more reluctant to act opportunistically for fear of losing the returns to exclusivity. As in *Woolen*, those returns became "hostage."

To conclude, the purpose of entering into a long-term lease that assures sufficient capture of quasi-rents would have been largely frustrated unless the lease had also been exclusive. Without such assurance, the Armory Board would not have built the stadium. Thus, the restrictive covenant functioned not only as did the cities' promise to Surtran not to employ a competitive taxicab service, but also to induce an investment that presumably represented an efficient use of resources.

In *Hecht* the practice helped induce the purchaser of a service to make an investment. In the appropriate situation, however, it could just as easily help induce the provider of a service to make an investment.¹¹⁰ For example, consider again the situation in *Pinehurst*. When the Moore County Board was making its initial arrangements for FBO service at the Southern Pines Airport, it may have been searching for an operator who would expend resources either to develop goodwill or to acquire tangible, specialized capital assets, like a building or some durable equipment. It may have even been searching for an operator who would expressly promise to make such investments. The Board may reasonably have believed, however, that its search would likely come to nought unless it allayed the fears of prospective operators that they would

110. It is rather unlikely that the practice helped induce the Redskins to make any investment.

be unable to capture the quasi-rents that might be generated by such investments. On the one hand, the post-investment franchising of one or more additional operators might frustrate capture. They might take a free ride on any goodwill that the original operator had developed, or through destructive competition eliminate the value of all the specialized capital assets that the original operator had acquired. On the other hand, opportunistic behavior might frustrate capture on the part of the Board. By promising to make arrangements with only one operator, the Board may have hoped to allay such fears. Presumably, that promise would tend to foreclose the establishment of additional operators and dramatically reduce the threat posed by any potential rivalry. Curiously, a dramatic reduction in that threat would tend to substantially reduce the threat of opportunistic behavior on the part of the Board. Such behavior could very well provoke the operator to retaliate in kind. This retaliation would be more costly in the absence of in-place alternative sources of FBO service. Thus, the Board would be less likely to risk it.

By providing some contractual assurance of quasi-rent capture, the Board's promise may have helped to induce Resort to make an investment. One cannot be sure because it is not clear from the court's opinion whether Resort sought any investment. Typically, when the practice under discussion is put to garden-variety use, the user seeks no significant investment. Consider then a more striking use of that practice, for example, the one challenged in *Mason City Center Associates v. City of Mason City*.¹¹¹ In that case, the plaintiffs sought a sizeable investment: the establishment of a downtown regional shopping center. The Mason City City Council promised the developer that it would use its powers to discourage the development of any similar centers within the city limits. That promise helped induce store owners to locate in the downtown center, and thereby collectively make the desired investment.

One might well wonder, however, what the City Council's promise might have had to do with maximizing the wealth of Mason City residents. After all, if the residents valued a downtown regional shopping center so much, they presumably would have been willing to pay for it. Investors would have then perceived the center, a rather specialized asset, as a generator of quasi-rents, and all else being equal, responded to the opportunity to earn those

111. 671 F.2d 1146 (8th Cir. 1982).

rents by making an optimal investment in the center. An explanation is necessary.

It is true that if the residents had valued a downtown center so highly, they would have been willing to pay for it—*provided* that they could not have enjoyed it otherwise. But each resident, as an individual, would have perceived that it would be equally available to him regardless of whether or not he paid. Downtown store owners could not have even attempted to deny service to nonpayers without negotiating an extraordinarily large number of contracts, and then monitoring all of them. Prohibitively high transaction costs would have made it uneconomical for those owners to capture the quasi-rents that their investments would generate. Hence, they would have tended to make smaller ones than they would have made had transaction costs been negligible.

The citizens of Mason City could have obtained more investment by arranging for the store owners to capture those quasi-rents. The arrangements could have involved a promise to pay a separate fee, a promise to maintain patronage at the downtown stores even if store owners raised their sales prices to reflect those quasi-rents, or a combination of the two. As long as the cost of the arrangements was less than the value of the additional investment, the new level of investment would be more optimal than the old. Presumably, the citizens would have been interested in making such arrangements only if the costs were low. By making such arrangements, the citizens would have been purchasing a service—a central business district service. It was in the context of such a purchase that the City Council made its promise.

No arrangements would have been economical unless the citizens could have avoided some of the transaction costs that the owners would have had to incur in order to capture the quasi-rents. The citizens could have eliminated the costs of negotiating a very large number of contracts by acting through a previously designated agent with wide-ranging powers, the City Council.¹¹² They would have had to do more, however, in order to reduce monitoring and enforcement costs because even arrangements made by the City Council might have entailed substantial costs.

112. Of course, the agent might not serve the interests of the principals as well as the principals might like, but that is a problem endemic to the agency relationship. See Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288 (1980); Jenson & Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305 (1976); Williamson, *The Modern Corporation: Origins, Evolution, Attributes*, 29 J. ECON. LIT. 1537 (1981).

To illustrate, suppose that the Council promised, on behalf of all the citizens, that they would maintain their patronage of the downtown stores even if sales prices were raised to reflect quasi-rents. The costs of monitoring, compliance, and enforcing such a promise would boggle the mind. But those costs could almost be eliminated while achieving the same end if the Council made a functionally equivalent promise. The promise would be to discourage the development of any other regional shopping centers where the residents might shop.

The making of that promise was the centerpiece of the arrangements that the City Council actually made.¹¹³ Presumably, the promise made those arrangements cost-effective. Until the City Council made that promise, its developer was notably unsuccessful in obtaining commitments from store owners to locate in the proposed downtown shopping center.¹¹⁴ The promise helped induce an investment. That was the function it was supposed to serve.

Nevertheless, Mason City Center Associates (MCCA) and Beaver Farms, Inc. challenged the practice as an antitrust offense. Unfortunately, that challenge never prompted any court to make the foregoing functional analysis, although the challenge ultimately failed following a jury trial and an unsuccessful appeal by MCCA.

In arranging for central business district service, the Mason City City Council took steps to assure investors that they would capture the quasi-rents generated by any investment that they might make in downtown stores. Those steps precluded the costs that investors would otherwise have had to incur in order to effectuate that capture. Clearly, the Council took those steps as the agent for the consumers of that service, the residents of the city. We must assume that a private enterprise agent in similar circumstances would have done the same. Presumably, it would have taken those steps only if by doing so it would have provided sufficient assurance, at a low enough cost, so that the service could be obtained most cost-effectively by purchasing it from a privately owned provider, thereby paying the investors to bear the risk of noncapture or expropriation. Therefore we must infer that the Council somehow provided that assurance.

Not all local governments attempting to arrange for central business district service would have been able to do likewise. For

113. The City Council also made some payments. It hired the developer and funded, with bonds, some of the development.

114. 671 F.2d at 1148.

example, consider the city council of a city occupying far fewer square miles than Mason City. On the one hand, had it taken the same steps as the Mason City City Council, it might have provided negligible, if any, assurance. Moreover, it might not have had the power to take other steps that would have provided more assurance. On the other hand, it might have been able to provide sufficient assurance but only by taking expensive steps, like making ancillary arrangements with the owners¹¹⁵ of land lying beyond the city limits. Taking these steps might cost more than the additional central business district service was worth.

Generally, when arranging for any service requiring an investment, any local government might be unable to provide investors with sufficient assurance of quasi-rents capture,¹¹⁶ or be unable to provide sufficient assurance without incurring prohibitive costs. Prospective investors dealing with a local government that was so disabled would face a greater risk of expropriation. Presumably, they would not invest without being compensated for it, so they would demand a larger payment from the residents. That demand might make the Mason City's method for obtaining service much more expensive than an alternative method which might be more cost-effective. That alternative could be the purchasing of the service from a collectively owned provider and internally bearing the risk of expropriation.

Using that method, without more, might itself be so expensive that residents would be better off by simply doing without the service. Using it would entail more than just arranging for the service to be provided. It would also entail entering into a risk-bearing agreement, which might involve extraordinarily large negotiating costs. It may also prevent the parties from expropriating the quasi-rents,¹¹⁷ and this might involve even larger monitoring and enforcement costs. Presumably, residents would use this alternative only if they could adequately contain these costs.

115. Among those owners who would likely have been the residents of other cities who exercised their rights, including the power to zone, collectively, through their local governments. Making arrangements with such owners would have been especially expensive because enforcement costs might be infinite.

116. More precisely, the cost of proving it would have been infinite.

117. If the residents did not collectively prevent each other from individually expropriating the quasi-rents, then, in the end, the majority of the citizens would probably pay substantially more for the service than it was worth to them. That would be obvious where the local government had borrowed the funds to make the investment from bondholders. See *Glenwillow Landfill*, 485 F. Supp. 671 (N.D. Ohio 1979), *aff'd sub nom. Hybud Equip. Corp. v. City of Akron*, 654 F.2d 178 (6th Cir. 1983), *on remand*, 1983-1 Trade Cas. (CCH) ¶ 65,356 (N.D. Ohio 1983), *aff'd*, 742 F.2d 949 (6th Cir. 1984).

The owners of a private enterprise could find themselves in a similar situation. They might wish to obtain a service, like wholesale distribution or retail marketing, that could only be provided if a substantial investment were made. Their management, however, might be disabled in the same way as was our hypothetical local government. They could then obtain the service most cost-effectively by creating their own service provider, subject to the commands of their management, and bearing the risk of expropriation themselves. Using that method to obtain the service would still be expensive. Whether the owners used it or simply did without the service would depend upon how well they thought management could use hierarchical controls to contain those costs. Apparently, owners of private enterprises find themselves in such situations all the time and frequently believe that their management skills can contain these costs. That is why we often observe pervasive and persistent use of this method, which we call vertical integration.¹¹⁸

In such situations residents may be able to best contain these transaction costs by acting through their local government. Indeed, in some instances that might be the only way in which they could avoid incurring prohibitive transaction costs. By having their local government bear the risk of expropriation, they could practically eliminate the costs of negotiating an agreement. For that agreement, they could in effect substitute their governance arrangements where local government is constituted and empowered to act as the residents' general agent.

Ironically, this action, which could practically eliminate negotiation costs, could raise monitoring and enforcement costs. By having the local government bear the risk, the residents would give themselves an incentive to act as free-riders and thereby expropriate the quasi-rents generated by their collective investment. A free-rider, as an individual consumer, would reap all of the gains from his behavior, while, as an "owner," he would suffer only a fraction of the losses because the total loss would be shared with all other residents. Monitoring residents who have such incentives and enforcing "anti-free-rider" ordinances against them would likely be prohibitively expensive, even if residents had their local government undertake these activities.

The residents might be able to effectuate the same end far more cheaply by having their local government control the behavior, not of the potential free-riders, but of those with whom they

118. Klein, Crawford & Alchian, *supra* note 63, at 297.

would deal. That, of course, is precisely what the residents of Mason City had their City Council do. As in the Mason City case, the local government will typically exert control pursuant to an agreement with those responsible for actually performing the service, or those who stand in their shoes financially. Under that agreement, local government will be obligated to refuse to make similar agreements with some, or all, of their rivals. In short, it will use the same practice challenged in *Mason City* and *Hecht*. Its use will be distinctive in that it will be laced with coercion. Indeed, an ordinance may complement this practice. It will, however, serve the same kind of functions as seen in prior cases.

The local government's "ownership," or more precisely for our purposes acting "ownership" of the service provider, may obscure the practice itself and, especially, the functions it is supposed to serve. For example, suppose that the Mason City City Council had "owned" the downtown stores. It might have then been difficult to even recognize that the Council had entered into an agreement with the supplier of a service to refuse to deal with the supplier's rivals. It would certainly have been difficult to understand what functions were served by the Council's promise to the developers and its related refusal to grant the plaintiff's rezoning request. Because it would not have been at all clear that the Council had acted on behalf of the consumers of central business district service, it might have appeared that the Council's actions were designed to restrict output. Similar difficulties would have beset the *Hecht* analysis had the District of Columbia Armory Board "owned" the Redskins.¹¹⁹

Where a local government does "own," or act for the "owners" of, the service provider, however, it is critical that the court recognize the practice and understand its functions. It is critical because such situations are particularly apt to arise in connection with services designed to promote the health and safety of residents. In arranging for them, a local government would find it most difficult to bind itself¹²⁰ and its residents,¹²¹ or to protect itself and its residents from being "held up" by a privately owned service pro-

119. That is not as farfetched as it might seem, as the resident "owners" of the Green Bay Packers football team can attest.

120. For example, a promise not to regulate the providers of such services would probably be unenforceable and would certainly be incredible. See generally T. SCHELLING, *THE STRATEGY OF CONFLICT* 43-46 (1960).

121. Politicians and bureaucrats who attempted to directly control the choices of residents with respect to such services would probably succeed only in getting themselves voted out of office or fired.

vider.¹²² Residents might, therefore, wish to obtain them from a collectively owned provider and bear the risk of expropriation themselves; however, that might not be economical unless the local government used the practice to control the behavior of free-riders. Only local government can control behavior because only local government can use power laced with coercion. Indeed, it is a fundamental purpose of local government to use the practice to make arrangements for just such services. In legal argot, these actions are called exercises of the police power. Thus, if the practice ran afoul of the antitrust statutes, local government, as we know it, would truly be transformed. For this reason, it is worth illustrating the appropriate analysis of the practice when used by a local government that "owns," or acts for the "owners" of, the service provider. To that end, consider *Gold Cross Ambulance v. City of Kansas City*.¹²³

Gold Cross Ambulance arose out of efforts by Kansas City officials to create a publicly owned advanced-life-support/quick-response ambulance system. As part of that effort, the city contracted with Ambulance Services, Inc. (ASI) to meet ambulance system requirements for Kansas City residents. ASI was obligated to use the city's emergency vehicles.¹²⁴ It was also obligated to provide service with specified medical care and response-time characteristics. In fact, the city was to pay for ASI's service only if ASI fulfilled its obligations. The city was obligated to actually make the payments that were due. ASI was thereby relieved of the task of directly collecting from resident users. The city also promised, explicitly or implicitly, that similar arrangements would not be made with any of ASI's rivals during the term of the contract. It fulfilled that promise by granting an operating license only to ASI, and by adopting a complementary ordinance that provided that only those holding such licenses could pick up patients within the city lim-

122. A local government that was "held up" would find itself in a "hostage" situation, with those demanding the service serving as the hostages. It is rather difficult to respond to that situation with a "we-will-not-negotiate" posture, which is one reason why we find governments noteworthy that do so consistently, like the Israeli national government.

123. 538 F. Supp. 956 (W.D. Mo. 1982), *aff'd*, 705 F.2d 1005 (8th Cir.), *cert. denied*, 105 S. Ct. 1864 (1985).

124. Initially, the city leased the vehicles from ASI and then subleased them back. By the time of the second contracting, the city had purchased them outright in accord with the full implementation of the "public utility model," a plan that avoids the problems associated with emerging ambulance services due to its cost structure. *Gold Cross Ambulance v. City of Kansas City*, 705 F.2d 1005, 1009 (8th Cir. 1983), *cert. denied*, 105 S. Ct. 1864 (1985).

its.¹²⁵ Thus, Kansas City used the practice analyzed in this article in the context under discussion.

That practice was challenged as an antitrust offense in a suit brought against the city and ASI by two privately owned ambulance companies. The companies operated out of nearby Independence, and both had been unable to compete for several large contracts to provide nonemergency ambulance service at institutions located in Kansas City. The city and its affiliates moved for summary judgment on the grounds, inter alia, that the practice was permissible under the state action exemption to the antitrust laws.¹²⁶

The court granted their motion, ruling that when the Missouri legislature enacted statutes that permitted municipalities to own and operate ambulance systems¹²⁷ and subjected private ambulance operators to licensure and related regulations,¹²⁸ the state had authorized Kansas City to use the challenged practice.¹²⁹ On appeal, the Eighth Circuit affirmed.¹³⁰ Nevertheless, the ruling was erroneous because it does not appear that those statutes even speak to the practice, much less reflect any discernible state policy favoring its use.¹³¹ Because the court's holding may not be followed

125. *Id.* at 1009-10.

126. *Gold Cross Ambulance v. City of Kansas City*, 538 F. Supp. 956, 961 (W.D. Mo. 1982). The city also moved for summary judgment on the ground that the tenth amendment to the Constitution insulated its regulations from the antitrust laws. *Id.* at 967. The plaintiff-ambulance owners, however, moved for summary judgment on several grounds. They asserted that their activities were in the nature of lobbying efforts, which the first amendment also insulates from the antitrust laws. With respect to the plaintiffs' fourteenth amendment claims, the court reasoned that the city had properly exercised its police powers in regulating ambulance companies and that the plaintiffs did not have a property right in a license to operate an ambulance company. *Id.* at 970. Finally, regarding the plaintiffs' equal protection claim, the court stated that the plaintiffs were not in fact similarly situated as are other ambulance companies because plaintiffs did not have a license to operate. *Id.* at 973.

127. Mo. ANN. STAT. § 67.300 (Vernon 1985).

128. *Id.* §§ 190.105, .115, .120, .125, .145, .175.

129. *Gold Cross Ambulance*, 538 F. Supp. at 964.

130. 705 F.2d 1005 (8th Cir. 1983).

131. The Missouri statute on point reads as follows:

67.300. Counties and cities, towns and villages authorized to operate ambulance service—rates may be set—insurance may be purchased

1. Any county, city, town or village may provide a general ambulance service for the purpose of transporting sick or injured persons to a hospital, clinic, sanatorium or other place for treatment of the illness or injury, and for that purpose may

(1) Acquire by gift or purchase one or more motor vehicles suitable for such purpose and may supply and equip the same with such materials and facilities as are necessary for emergency treatment,

in similar actions, it is useful to consider the legality of Kansas City's practice.

Had the court not considered Kansas City's conduct "exempt from the operation of the Sherman Act,"¹³² the court might still have deemed the city's practice legal. That would have depended, or at least should have depended, on the functions served by the city's conduct. Those functions can best be deduced by examining the economic context in which the city used the practice, and then applying the familiar assumption that Kansas City officials acted to maximize the wealth of the city's residents.

The residents of Kansas City had been purchasing ambulance service long before the creation of the advanced-life-support/quick-response system. In the years immediately preceding the system's creation, they made their purchases from a number of providers on a spot market. Apparently, Kansas City officials came to believe that the available service on the market was substantially inferior, in terms of medical care and response time, to the service for which residents would have been willing to pay. That belief was reasonable because considerable transaction costs would have stood between the residents' willingness to pay, and any provider's receipt of revenues. Those transaction costs would have been the costs of exclusion, search, and collection. Because of them, a provider of superior ambulance service would have had little, if any, chance of earning enough to cover his higher costs. This is true when realizing that the return on his larger investment would not be commensurate with his sizeable risk. Consider those costs

and may operate, maintain, repair and replace such vehicles, supplies and equipment;

(2) Contract with one or more individuals, municipalities, counties, associations or other organizations for the operation, maintenance and repair of such vehicles and for the furnishing of emergency treatment;

(3) Employ any combination of the methods authorized in subdivisions (1) and (2) of this section.

2. The municipality or county shall formulate rules and regulations for the use of the equipment and may fix a schedule of fees or charges to be paid by persons requesting the use of the facilities and provide for the collection thereof.

3. The municipality or county may purchase insurance indemnifying against liability of the county or city and the driver and attendants of the ambulance for the negligent operation of the ambulance or other equipment or supplies or in rendering services incidental to the furnishing of the ambulance service.

MO. ANN. STAT. § 67.300 (Vernon 1985).

132. 538 F. Supp. at 967.

seriatim.

The costs of exclusion would have prevented a provider of superior ambulance service from obtaining revenues from most of those who would have benefited from it. This may seem counter-productive under the rationale that those who are transported and cared for in ambulances usually pay a fee. Those who are transported and receive care in ambulances, however, are not the only parties who benefit by the service. Almost every resident of Kansas City benefits because in the course of producing the services, a provider also produces another valuable good: the availability of that service. The provider would find it rather expensive, however, to stop any resident from enjoying the benefits of that availability. In fact, the costs of exclusion would probably be prohibitive since availability is regularly deemed a public service. As a result, no resident would have any incentive to pay for the service. A provider of a superior service would obtain revenues, then, only from those wishing to be transported in an ambulance.

Not all of those who need ambulance transport and assistance would have used the provider's service. The costs of advertising their services would have prevented the provider from obtaining the patronage of those residents willing to pay a premium for superior ambulance service, but unaware of its availability. Attempting to remedy such ignorance by supplying credible information about medical care and response time would have been quite expensive. Moreover, it might not have done much good because those who summon an ambulance are rarely the users, and the summoner might be ignorant, fail to appreciate the preferences of the user, or act opportunistically.¹³³

Obtaining patronage, of course, does not itself fill the coffers of ambulance service providers. Collecting fees does. Their costs of collection, however, prevent them from obtaining revenues from all of their patrons. In large part, these costs are high because an ambulance provider usually seeks payment after, rather than before, service is rendered. If a provider refused service, especially emergency service, until it had secured payment, or at least information suggesting that payment would be made in the near future,¹³⁴ resi-

133. For example, the dispatcher at a nursing home might summon an ambulance from a particular provider because he was paid to do so. Jack Stout, one of the defendants in *Gold Cross Ambulance* and a consultant to cities on ambulance service, told me that he was aware of ambulance companies who strongly encouraged their female personnel to date male dispatchers for that purpose.

134. The provider might insist, for example, that the would-be user prove that he

dents would become aware of that practice¹³⁵ and tend to summon a rival provider. Thus, there may be a substantial disparity between the revenues that an ambulance service provider earns, and those that it receives. That disparity would be especially painful to a provider of superior service because of the greater costs superior service incurs.

These three transaction costs must be large enough to offset the economics of dispatching and positioning that a single provider would have enjoyed.¹³⁶ Otherwise, a single provider would probably have been able to drive all his rivals out of the market. In any event, such costs were likely to be so large that the revenues obtainable on the spot market would have been insufficient to induce any provider to acquire emergency vehicles, hire trained personnel, and operate the sophisticated positioning and dispatching system necessary to supply advanced-life-support/quick-response ambulance service in an amount which would otherwise have been optimal.

Not surprisingly, then, Kansas City officials also came to believe that the amount of ambulance service supplied would be closer to optimal if it were sold off the spot market. It does appear that by selling off the spot market a provider could reduce the costs of exclusion, search, and collection. He could reduce the costs of exclusion by selling his service pursuant to a requirements contract, and he could reduce the costs of search and collection by including provisions in the contract that specified the requirements that his service must meet, and by placing the risk of nonpayment

owned an effective insurance policy which covered ambulance service or, in the alternative, durable assets not exempt from execution, and of sufficient value to exceed the costs of the service and collection.

135. It may seem inconsistent to assert that, on the one hand, many residents would have become aware of a provider's refusal to render ambulance service prior to receiving payment while, on the other, those same residents would have remained unaware of the superiority of that service. But it is not. The difference between the two assertions simply reflects the different costs of acquiring and verifying different information. To acquire and verify information about the quality of ambulance service (response times and medical care), residents would have had to undertake an arduous study. To acquire and verify information about a pay-before-you-go-to-the-hospital practice, however, he would have had only to open a local newspaper or tune to a local broadcasting station for a report on the resulting deaths.

136. If transaction costs were negligible, one firm could provide dispatching and positioning service and other firms could make the ambulance runs. The transaction costs, however, are considerable, in large part because the firms providing the runs tend to resist directions from the dispatcher involving the less profitable runs. Center for Economic & Management Research, University of Oklahoma, *A Process for Setting Community and State Policies Regarding EMS System Performance Capabilities* (1974) (unpublished work).

on the buyers. None of the suppliers entered into such a contract because the costs of negotiating, monitoring, and enforcing this type of contract are prohibitive. The provider would have to negotiate contracts with perhaps hundreds of thousands of residents in order to make the nonpayment provisions palatable. Each contract would necessitate complex performance standards, require a long-term commitment, and be contingent upon obtaining the signature of all the parties. Once the parties signed contracts, the provider would have to identify nonsigners and prevent them from using the service. This would have been difficult because many users might have been away from their homes. Consequently, they would be unable to identify themselves or their location. Denial of service in those situations would have catastrophic consequences. If the demand charge or option fee were low enough, the provider would also have to prevent signers from using rival providers. Otherwise, he would fail to cover those capacity costs reflected in his schedule of user fees, such as the charges for transportation and care. Moreover, the provider would have to assure residents that they would receive the service for which they had contracted. That would not have been easy because residents would be hard-pressed to assess the provider's performance, and even harder pressed to take action against the provider if the users found the service wanting because a recalcitrant provider might respond to enforcement with a curtailment of service.

Kansas City residents could have reduced these costs had they taken collective action through the city. The city could have struck the necessary agreements on their behalf and thereby dramatically reduced negotiating costs. The city also could have used coercion to prevent would-be rivals who had not already entered into an agreement from selling ambulance service to residents. This would have substantially reduced the costs of monitoring the behavior of residents and enforcing anti-free-rider provisions against them. Finally, the city could have hired personnel to assess the service that was provided and, if its quality did not meet contractual standards, withhold payment or otherwise secure better service. That action might have reduced monitoring and enforcement costs somewhat because the city would likely have enjoyed some economies of scale in carrying out those tasks. Monitoring and enforcement costs probably would have remained prohibitive unless the city made arrangements with only one provider. If the court required the city to make arrangements with more than one provider, each provider then would have an incentive to act oppor-

tunistically in order to try to avoid those calls where performance standards were most difficult to meet.

Although taking such collective action would have reduced the costs of negotiating, monitoring, and enforcing requirements contracts for ambulance service, it would probably not have provided assurance to investors of quasi-rent capture sufficient to induce the investment necessary to create an advanced-life-support/quick-response system. In fact, it is likely that those actions would have inadvertently put the prospective owners at greater risk. The reason is that once an advanced-life-support/quick-response system is established and operational, opportunistic behavior by city officials might dissipate quasi-rents. For example, city officials might declare a medical emergency or simply abrogate the contract, or portions of it, or they might regulate rates. In light of the possible impact of ambulance service on the health and welfare of Kansas City residents, a promise by the city that its officials would refrain from such conduct would probably be unenforceable, if not unbelievable. The premium the owners would have demanded for bearing this risk of moral hazard would probably have amounted to a substantial fraction of the value of the service. The residents would have been reluctant to pay the service. They would have been particularly reluctant because they would have to bear the parallel moral hazard risk that the provider would reduce the level of service provided, or threaten to do so in order to obtain more revenues. That would be an acute risk if, to economize on monitoring and enforcement costs, the city had entered into a service agreement with only one provider. The effect of contracting with only one provider would make it much more difficult to replace the provider quickly.

Thus, it was quite reasonable for Kansas City officials to believe that no privately owned provider would supply the kind of service that could be produced with an advanced-life-support/quick-response system. The costs of capturing the quasi-rents generated by such a system would have been prohibitive. Thus, if the residents desired to obtain an advanced-life-support/quick-response system, they would have to obtain it from a publicly-owned provider. They could do so, without negotiating a risk-bearing agreement, by having the city acquire the necessary emergency vehicles to actually make the runs. That would mean, however, that the residents would bear the risk to expropriate the quasi-rent themselves. The quasi-rents generated by the system could be expropriated by residents who might welch on the implicit agreement

to purchase their requirement of ambulance transportation and care from the city-owned provider.

Many residents would have an incentive to welch on their agreement. By purchasing service from a noncity-owned provider, a resident could pocket any difference in rates. There would be a difference in rates because the city-owned provider's rates probably would reflect at least some capacity costs, while the rates of the alternative provider's would not. The city could have eliminated that potential gain by setting its provider's rates so that they did not reflect any capacity costs. If it had done so, residents might very well have to bear even more costs than they would otherwise have as a result of welching. They would have to bear additional taxes to cover those capacity costs, and they would have to bear the expense of inefficient behavior prompted by that taxation. Generally, residents would have been tempted to try to reap the gain from rate differences whenever they preferred the price/performance of the noncity-owned provider to that of the city-owned one. This preference would be especially prevalent at a time when there was no need of emergency service, and obtaining nonemergency service from a noncity-owned provider was convenient. The costs of making the purchase would be almost zero. The chances of being caught would also have been small, and it seems likely that if one were caught, the penalty would not have been harsh. Of course, whenever a resident purchased ambulance service from a noncity-owned provider, he would have also suffered a loss. The city-owned provider would have realized fewer revenues, and the value of his interest would have been diminished. Because he would have shared that revenue shortfall with many others, however, his gain would have likely exceeded his loss. Thus, the incentive to welch, at least when obtaining nonemergency service, would have been strong. Unless the city checked the response to this incentive, it is quite possible that collective risk-bearing, even through the city, would have been prohibitively expensive.

The agreement between Kansas City and ASI, and the complementary ordinance, made it much more costly for noncity-owned providers to operate in Kansas City. Thus, the challenged practice served an instrumental function in securing more nearly optimal ambulance service for the residents of Kansas City.¹³⁷ The

137. It enabled Kansas City to solve a problem of organizational design that confronts every firm: "the need to organize transactions in such a way as to economize on bounded rationality while simultaneously safeguarding the transactions in question against opportunism." Williamson, *supra* note 22, at 958.

court should have condemned it as an offense only if the court deemed that function undesirable according to the principles embodied in the antitrust statutes.

B. *Are Any of the Functions Objectionable?*

In *Pinehurst*, *Woolen*, *Hecht*, *Mason City* and *Gold Cross Ambulance*, the legal problems of the defendant local government grew out of its efforts to purchase a "service," broadly conceived, at the lowest possible price. Each tried to make the purchase by entering into a complex sales transaction, an integral part of which was a promise not to buy from any of the supplier's rivals. That practice, which is used by virtually every local government, is almost invariably intended to serve one or more of the four functions in the illustrative cases. Most of these functions are related to the avoidance of transaction costs. Individuals and groups generally enter into complex sales transactions instead of making spot market purchases for that very purpose.¹³⁸ The four functions are: (1) to help secure efficiently provided service by permitting the supplier to enjoy either economies of production or transaction; (2) to help reduce transaction costs, particularly monitoring and enforcement costs, of arranging for the service; (3) to help reduce the transaction costs of capturing quasi-rents; (4) and by reducing these costs, to help induce investment when providing the service requires an additional investment.

Serving those functions is consistent with the principle that it is good to maximize consumer welfare. That should not be surprising because local governments invariably use the practice of exclusivity as part of a sales transaction, and sales transactions generally tend to increase consumer welfare. In fact, as already noted,¹³⁹ the only sales transactions that do not are those which are largely transfer payments, and those that are strategic maneuvers designed to obtain market power. Only transactions that are strategic tend to reduce consumer welfare, and they are usually uncommon—especially among local governments. There is certainly no evidence that the defendant local governments engaged in such behavior.

When this most common local government practice is sup-

138. "The basic presumption of the transaction cost approach [which is the approach taken here] is that successive interfaces are organized in a manner that economizes on transaction costs." *Id.*

139. See *supra* notes 27-28 and accompanying text.

posed to serve functions one and two, it obviously tends to maximize consumer welfare. It tends to reduce the total costs incurred in making available a given output of a particular service. That cannot be said about the practice when it serves only function three. Viewed statically, the practice tends to maximize consumer welfare only in the sense that it may be the most cost-effective means by which investors can capture the quasi-rents generated by a service-related investment, an activity in which they are likely to engage in any event. Total costs will not vary with the identity of the individuals who can economically effectuate that capture. Viewed dynamically, however, total costs will vary. Unless potential investors can economically effectuate capture, they may not make the service-related investment, and without it, the total costs incurred in making available a given output of the service may be much greater than they would otherwise be. Indeed, they may be infinite. Thus, when the practice is supposed to induce investment, function four, it tends to promote efficiency. To restate this idea more technically, whichever function the practice is supposed to serve, it tends to lower the supply curve. In a sense, it thereby "liberates" resources for other uses, which may include the production of more of that particular service or of something else entirely. That means that as a result of using the practice of promising exclusivity, the total personal value of all goods and services produced will tend to be higher than it would otherwise be. Thus, the practice is unobjectionable on grounds related to the wealth of creation.

The practice could be objectionable, if at all, only on grounds related to the wealth of distribution. In any particular instance of its use, one could certainly identify those who appear to suffer a detriment as a result of taking part in a transaction. They are the rivals of the chosen supplier who would have liked to do business with the local government, or in the case of Johnny-come-latelies, those who would like the local government to welch on its promise. Presumably, they are the ones who should benefit by the application of any wealth-distribution principle, according to which the functions served by the practice are undesirable. It is easy enough, then, to describe the general characteristics of the wealth-distribution principle. There are two. First, the principle must be based on an intellectually acceptable distinction between a group that includes those who seem to be worse off, and another group that includes the chosen supplier and the local government, even if the latter is included only as a confederate. Second, it must provide

that it is good to prefer the first group to the second one. Finding a principle with these characteristics that will help resolve a specific dispute, however, is difficult at best.

For example, consider the problems one would have in finding this type of principle for the *Pinehurst* dispute. One could identify those who seem to be worse off as a result of the arrangements between the Moore County Board and Resort. They are fixed based operators, not including Resort, who upon reasonable notice could begin providing FBO service at Southern Pines Airport, and others, like Pinehurst, who could have done so without incurring heavy start-up costs even though they were not already established as fixed based operators. It is no simple task to distinguish in an intellectually acceptable way between that group and another one which includes Resort. Even if we suppose that a distinction could be made, one would still be confronted with an intractable problem in logic. The principle that it is good to prefer the first group to the second one will not help resolve the dispute because penalizing the Board for engaging in the practice would not give the preferred group any advantage. Penalizing the Board would deter fixed based operators from agreeing to provide FBO service in reliance on the kind of promise that the Board made to Resort. In the absence of this agreement, FBO service would seem more costly to the Board and to other airport-owning local governments. They could be expected to purchase less of it, or to offer less in exchange for it, than they otherwise would. In either event, the preferred group would not be better off, but worse off. The dynamics of markets will cause the search for a wealth-distribution principle to yield about as much as a snipe hunt.

One could willfully ignore these dynamics and search for the principle on the basis of analogy. The cases are legion where the court entertained similar challenges to the practice when private enterprises engaged in the practice of exclusivity.¹⁴⁰ Unfortunately, these cases may be bountiful, but not helpful. Most of the opinions do little more than affix one or more antitrust labels to the practice. Although the labels colorfully describe the obvious: the plaintiffs were made worse off as a result of a contract that restrained their trade; they do not expressly disclose the wealth distribution principle upon which the cases were actually decided.

140. For recent examples, see *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*, 676 F.2d 1291 (9th Cir.), *cert. denied*, 459 U.S. 1009 (1982); *Fishman v. Estate of Wirtz*, 47 ANTITRUST & TRADE REG. REP. 57 (N.D. Ill. 1984).

Analyzing the cases, it is possible to determine that the principle must have been that it is good to prefer private holdings of wealth which are "smaller" or "less advantaged" to those which are "larger" or "more advantaged." As suggested previously,¹⁴¹ that principle seems to be rooted in a two-part rationale. Recall that one part is the public choice theory that one may explain political behavior largely on the basis of the relative wealth of the private antagonists interested in influencing it, and the other part is populist ideology, which holds that behavior will be "better" the more wide and even the distribution of wealth.

Analyzing by the basis of analogy will yield a wealth-distribution principle, but that principle is inapplicable to disputes between the plaintiff, private enterprises, and defendant local governments. Even if we ignore the dynamics of markets, it is inapplicable on its own terms. It simply does not tell us that it is good to prefer some private holdings of wealth to any public holdings. One could try to expand the principle so that the nonpreferred group would include "larger" or "more advantaged" public holdings of wealth. That group could then include local governments using the practice if they arranged with a supplier for a "large" quantity of service, or if the court ipso facto deemed parties to the arrangements "more advantaged" than nonparties. Even if the court so extended the principle, and one would almost have to compromise one's intellectual honesty to do so, it would still be inapplicable in light of the rationale on which it is based. The crude public choice theory does not even purport to tell us what effect the distribution of wealth between private enterprises and local governments will have on political behavior. Certainly, populism does not even hint that political behavior will be better if wealth is redistributed from local governments, and the taxpayers they represent, to private enterprises. Indeed, local government is a populist-preferred institution.

No principle of wealth distribution or wealth creation suggests that the functions served by this practice are undesirable. The practice is, in and of itself,¹⁴² lawful when engaged in by local governments.

A reassessment of most of the other local government practices attacked as antitrust offenses would yield similar conclu-

141. See *supra* text accompanying note 5.

142. Of course, if nonimmune local governments somehow found a way to use it solely as a part of a strategic maneuver to become a monopolist or as part of the operations of a classic cartel, they would run afoul of the antitrust statutes.

sions.¹⁴³ Thus, local government may emerge unscathed from its battle with antitrust law, but antitrust law could undergo profound change.

IV. THE IMPACT OF REASSESSMENT ON ANTITRUST LAW

To understand why antitrust law could undergo profound change, one must understand that *Boulder* and *Lafayette* reflect local governments' enjoyment of rather limited immunity. In addition, the principles used in evaluating their conduct should be the same as those used in evaluating the conduct of private enterprises. In both cases, the court relegated local governments to the same treatment accorded private enterprises. Apparently, the Court reached those results purposefully. In *Lafayette* the Court explained, "[Our decision] means . . . that when the State itself has not directed or authorized an anticompetitive practice, the State's subdivisions in exercising their delegated power must obey the antitrust laws."¹⁴⁴ Unless the Court was employing double-speak, its language, quoted with approval in *Boulder*,¹⁴⁵ must mean that substantive antitrust principles apply with equal force to nonimmune local governments and private enterprises. Any other reading of that language would be inconsistent with the Court's rejection of the proposition that the applicability of the federal antitrust statutes turns on the status of the defendant.

The Court's analysis of the municipalities' arguments in *Lafayette* also reinforces the "same treatment" teaching. The Court rejected what it apparently understood to be the municipalities' first argument—that the Sherman and Clayton Acts must not apply to them because using, or threatening to use, the acts' sanctions against the cities would disrupt their essential operations, a result which those statutes were not designed to achieve. The Court seemed to recognize that pursuant to its decision, however, trial judges would be bound to apply the same substantive antitrust principles to all defendants.¹⁴⁶ Only the application of those

143. M. LEE, ANTITRUST LAW AND LOCAL GOVERNMENT (forthcoming from Greenwood Press). Cf. Lopatka, *State Action and Municipal Antitrust Immunity: An Economic Approach*, 53 FORDHAM L. REV. 23 (1984).

144. 435 U.S. 389, 416 (1978).

145. 455 U.S. 40, 57 (1982).

146. 435 U.S. 389, 400-01 (1978). In fact, the Court misconstrued the cities' first argument. "Regardless of whether their defense may ultimately succeed at trial," asserted the cities, "merely exposing city governments to injunctions, treble damage liability, and perhaps criminal prosecution under the federal antitrust statutes will produce enormous uncertainty and hesitancy among public officials and disserve the public interest Elected

principles would be likely to lead to such disruption. The Court merely suggested that the result might be avoided by limiting the remedies available to prevailing plaintiffs. The Court also rejected the municipalities' second argument—that applying the Sherman and Clayton Acts to municipalities would be inconsistent with the general purpose of the antitrust statutes. The municipalities erroneously claimed that the general purpose of the antitrust statutes was to check “private power derived from amassed capital or shrewd business practice,”¹⁴⁷ thus providing protection against abuses of that power.¹⁴⁸ Justice Brennan, writing for the majority of the Court, observed that local governments, like private enterprises, could bring about the precise harm that Congress designed the federal antitrust statutes to prevent.¹⁴⁹ Presumably, the courts should consider conduct that causes this economic harm a violation no matter whether it is engaged in by private enterprises or local governments. This result is obtained only if the courts apply the same substantive antitrust principles to all defendants. Finally, in accepting only an attenuated version of the municipalities' third argument—that the Sherman and Clayton Acts are inapplicable to them under *Parker* because they are merely subdivisions of a state and exercise only those powers granted by it¹⁵⁰—the Court ruled that local governments are entitled to no more immunity than that enjoyed by state agencies under *Goldfarb v. Virginia State Bar*.¹⁵¹ Surely, they are entitled to no more lenient treatment on the merits. On that point *Goldfarb* is instructive. In *Goldfarb*, the Court adjudged the conduct of the defendant bar association illegal *per se* under the same principles used to evaluate the conduct of a private enterprise.

Applying different substantive antitrust principles to local government defendants would mean, in effect, assessing the legality of challenged practices on the basis of not only the goal of the Sherman and Clayton Acts, as ordinarily conceived, but also on the basis of the conflicting goals purportedly being pursued by those defendants. It is difficult to believe the Court intended that judges

officials may be unwilling to accept the economic and political risks created by the Fifth Circuit's decision.” Brief for Petitioner at 20-21, *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389 (1978).

147. Brief for Petitioners at 22, *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389 (1978).

148. *Id.* at 22, 24.

149. *Id.* at 406-07.

150. *Id.* at 408.

151. *Id.* at 408-10 (discussing *Goldfarb v. Virginia State Bar*, 421 U.S. 773 (1975)).

use these differing analyses. In the first place, in *National Society of Professional Engineers v. United States*,¹⁵² the Court explicitly rejected such multiple goals analysis as improper under the anti-trust statutes. That opinion was rendered subsequent to *Lafayette* and it seems unlikely the Court intended to overrule it in *Boulder*, a case where the Court never raised the question of proper anti-trust analysis.¹⁵³ In the second place, if judges were to engage in multiple goals analysis, they would be put to the task of balancing noncomparable goals. They would find that task intellectually problematic at best, and because it would not be subject to systematic review, a large number of judges might refuse to apply it. Balancing goals might degenerate into giving one decisive weight. If that occurred, either local governments would be subject to the same substantive principles as private enterprises, or local governments would enjoy functional, although not nominal, immunity, contrary to court decisions. To reduce the risk of such degeneration, judges would have to evaluate both the wisdom of the conflicting goals purportedly being pursued by local government defendants, and the efficacy of the challenged practice in achieving them. The Court would then be judging the reasonableness of local government conduct much like it judged the reasonableness of state government conduct during the heyday of substantive due process.¹⁵⁴ It is unlikely that in deciding *Lafayette* and *Boulder* the Supreme Court intended to resurrect *Lochner*¹⁵⁵ and its progeny; it is even less likely that lower courts will so interpret them.

A court that had found a practice lawful when engaged in by a local government would as a practical matter be bound by *Boulder* and *Lafayette*'s "same treatment" teaching to disregard the status of the defendant, and to find the practice lawful when engaged in

152. 435 U.S. 679 (1978). In *National Society*, the Court held that a canon of the National Society of Professional Engineers prohibiting members from submitting bids for engineering services suppressed competition in violation of the Sherman Act, and affirmed the lower court's granting of an injunction against the canon. *Id.*

153. It seems especially unlikely that the Court meant to overrule, sub silentio, *National Society* in *Boulder* because Justice Rehnquist discussed that possibility explicitly in his dissent. 455 U.S. 40, 65-68 (1982) (Rehnquist, J., dissenting).

154. See Civiletti, *The Fallout from Community Communications Co. v. City of Boulder: Prospects for a Legislative Solution*, 32 CATH. U.L. REV. 379, 387 (1983); Comment, *Alternative Approaches to Municipal Antitrust Liability*, 11 FORDHAM URB. L.J. 63, 81-82 (1982); cf. Note, *Community Communications Co. v. City of Boulder: The Emasculation of Municipal Immunity from Sherman Act Liability*, 32 CATH. U.L. REV. 413, 433 (1983) ("Courts would be left to work with little or no guidance, attempting to give meaning to an overly flexible distinction.").

155. *Lochner v. New York*, 198 U.S. 45 (1905).

by a private enterprise.¹⁵⁶ Several such findings would work a major retrenchment in antitrust doctrine. That retrenchment would cause antitrust's internal war to intensify. Local government practices would be almost per se legal because they would rarely, if ever, function to reduce consumer welfare in restricting output and raising prices.¹⁵⁷ But other practices, such as a vertical acquisition, or licensing the use of a patented input solely on the basis of an end-product royalty,¹⁵⁸ would remain subject to expensive scrutiny and frequent condemnation because local governments would seldom, if ever, employ them. Such inconsistent treatment would be difficult for judges to justify. Some of them might attempt to alleviate the problem by eliminating the cause of the inconsistency. The cause represents the use of two quite different, and often conflicting, principles to determine the legality of practices under the same statutes—the antitrust statutes. Judges who wished to eliminate it in an intellectually respectable manner would simply choose one of the following: either the principle of maximizing consumer welfare, or the principle of distributing wealth in populist-preferred ways. To avert truly calamitous results, they would likely select the first option and discard the second (and populism generally) as inapplicable to the resolution of antitrust suits against both private enterprises and local governments. If the judiciary makes this choice, nonstrategic conduct that had an exclusionary effect, like the conduct challenged in the famous *Alcoa* case,¹⁵⁹ would be per se legal.¹⁶⁰ Franchisor-franchisee disputes would be relegated to the realm of ordinary contract law.¹⁶¹ Horizontal

156. This retrenchment would be largely consistent with Williamson's position on vertical restraints. Williamson, *supra* note 22, at 993.

157. A court could conceivably bar a local government's practice as inconsistent with some other federal statute under the supremacy clause, or as being unreasonably burdensome on interstate commerce, or even contrary to the first amendment as incorporated in the fourteenth. See *Bates v. State Bar of Ariz.*, 433 U.S. 350 (1977) (attorney's advertisement falls within scope of first amendment). Generally, those who are hurt by the practices of local government may pursue a host of federal, as well as state, judicial remedies.

158. The Supreme Court condemned this practice in *Zenith Radio Corp. v. Hazeltine Research, Inc.* and gave this case the "patent misuse" label. 395 U.S. 100 (1969).

159. *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 424 (2d Cir. 1945).

160. For example, the refusal by a sugar-beet processor to purchase beets from any grower who did not plant the processor's seeds would be legal, even though that conduct might exclude other seed sellers from the market, where such restraint has significant anticompetitive effects. See *Betaseed, Inc. v. U & I, Inc.*, 681 F.2d 1203, 1228-30 (9th Cir. 1982).

161. Presumably, cases like *Midwestern Waffles, Inc. v. Waffle House, Inc.* would generally not reach the summary judgment stage, as *Waffle House* did, and the court would promptly resolve those that did in favor of the franchisor. 734 F.2d 705 (11th Cir. 1984),

mergers similar to those in *Von's Grocery*¹⁶² and *Rome Cable*¹⁶³ would survive a motion for summary judgment based on minimal discovery.¹⁶⁴ Refusals by joint venturers to share the rewards of their enterprise with their rivals¹⁶⁵ would survive a motion to dismiss for failure to state a claim. Moreover, the focus of the inquiry in antitrust cases would shift to the challenged practice's economic function rather than the status of the parties. That situation would prompt even more changes. In short, this would completely reform the common law of antitrust and turn it into an engine for promoting economic efficiency.

aff'd, 1983-2 TRADE CAS. (CCH) ¶ 65,567 (N.D. Ga. 1982).

162. *United States v. Von's Grocery Co.*, 384 U.S. 270 (1966).

163. *United States v. Aluminum Co. of Am.*, 377 U.S. 271 (1964).

164. It appears from the 1982 Merger Guidelines of the Department of Justice that with respect to horizontal mergers, the Antitrust Division will focus on post merger concentration of the market and the market shares of the merging firms to determine whether the merger poses a significant threat to competition. *Justice Department Merger Guidelines*, ANTITRUST & TRADE REG. REP. (BNA) No. 1069, at 5-6 (June 17, 1972). Corporate executives contemplating a horizontal acquisition, however, must be concerned about not only the Antitrust Division but also private plaintiffs. See *Marathon Oil Co. v. Mobil Corp.*, 669 F.2d 384 (6th Cir. 1982), *cert. denied*, 455 U.S. 982 (1982). After the reformation suggested in the text of *Marathon Oil Co.*, presumably, companies like Marathon would be unable to invoke the antitrust statutes in order to block acquisition attempts from companies like Mobil. 669 F.2d at 380.

165. See, e.g., *Associated Press v. United States*, 326 U.S. 1 (1945).