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State Action and the Meaning of Agreement Under Sherman Act: An Approach to Hybrid Restraints

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State Action and the Meaning of Agreement Under the Sherman Act: An Approach to Hybrid Restraints

John E. Lopatka[†] and William H. Page^{††}

Antitrust observers are familiar with the two-part Midcal test for the immunity of state regulation from federal antitrust laws: the state must clearly articulate its policy to displace competition and must “actively supervise” any private conduct pursuant to the policy. But state action need not meet these requirements if it is “unilateral” and therefore does not conflict with Section 1. Only if a state-authorized restraint is “hybrid,” combining state and private action in a way that resembles a prohibited agreement, need the restraint satisfy Midcal.

In this article, John Lopatka and Bill Page examine the history and current importance of the distinction between unilateral and hybrid restraints. Although the Supreme Court’s precedents are not entirely consistent, the authors argue that a unilateral restraint is one in which governmental actors define the extent of consumer harm, while a hybrid restraint is one in which the government “empowers private actors to exercise discretion as to the nature or level of consumer injury in a way that closely resembles an antitrust violation.” They examine the emergence of this principle in the context of state restraints that are analogous to resale price maintenance. They then examine recent appellate decisions characterizing horizontal restraints as hybrid. In this part, the authors argue that antitrust law reaches “not only state authorized express collusion but state practices that significantly facilitate tacit collusion and serve no competitively benign purpose.”

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Introduction

Antitrust differs from most forms of economic regulation in its reliance on sporadic judicial intervention in markets to penalize conduct that reduces consumer welfare.¹ Over the past century, the Supreme Court has developed a complicated set of antitrust categories, prescribing forms and levels of scrutiny of various practices, based upon their likelihood of harming consumers by reducing economic efficiency.² The Court formulated these rules to address private practices—those that firms adopted without governmental support other than the market framework of contract and property law. But antitrust regulation often applies to markets that are subject to more continuous and pervasive regulation. Where the source of this regulation is state or local law, the question is whether antitrust and state regulation can coexist or whether one must yield to the other. The Supreme Court has developed yet another intricate body of doctrines to address this issue and its manifold variations. The most celebrated part of this doctrine is state action immunity,³ announced in the

1 On the purpose of antitrust law, see, for example, *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 458 (1993) (“The purpose of the [Sherman] Act is not to protect businesses from the working of the market; it is to protect the public from the failure of the market.”); *Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979) (“Congress designed the Sherman Act as a ‘consumer welfare prescription.’”) (citation omitted); ROBERT H. BORK, *THE ANTITRUST PARADOX* 427 (The Free Press 1993) (“By and large, with some ambiguity at times, the more recent cases have adopted a consumer welfare model [of antitrust].”).

2 See generally *Cal. Dental Ass’n v. FTC*, 526 U.S. 756, 769-71, 779-81 (1999) (discussing categories of antitrust scrutiny).

3 The terminology used to describe the state action doctrine can be confusing. One court recently observed: “‘State-action immunity’ is more accurately a strict standard for locating the reach of the Sherman Act than the judicial creation of a defense to liability for its violation. . . . Thus, what has come to be known as ‘state-action immunity’ is not really immunity but rather an exemption. . . . It does, however, function in certain respects much like an immunity.” *Apani Southwest, Inc. v. Coca-Cola Ents., Inc.*, 128 F. Supp. 2d 988, 997 (N.D. Tex. 2001). Justice Rehnquist, however, once complained about this issue: “I think it quite clear that questions involving the so-called ‘state action’ doctrine are more properly framed as being ones of pre-emption rather than exemption.” *Comty. Communications Co. v. City of Boulder*, 455 U.S. 40, 62 (1982) (Rehnquist, J., dissenting). The *Apani*

1943 case of *Parker v. Brown*⁴ and elaborated in numerous decisions since then.⁵ That doctrine protects the state from liability for its anticompetitive acts and protects private parties from liability for actions undertaken pursuant to a clearly articulated state policy and actively supervised by the state.

But there is another, less prominent, dimension of the Court's approach to state-supported restraints.⁶ The Court has rejected some antitrust challenges to state or local regulations on the grounds that they did not conflict with antitrust law and were therefore valid regardless of whether they met the requirements of immunity. State regulation does not conflict with antitrust law simply because it reduces competition. For a conflict to exist, the implementation of the regulation must amount to a violation of the substantive rules of antitrust. For example, in *Fisher v. City of Berkeley*,⁷ the Court held that a municipal rent control scheme, which all but eliminated price competition, did not conflict with antitrust law because it "unilaterally" imposed rents on landlords.⁸ Because there was no "contract, combination, . . . or conspiracy," there was no violation of Section 1 of the Sherman Act and, thus, no need to invoke *Parker* immunity.⁹ By contrast, in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*,¹⁰ a statute requiring distributors to charge resale prices dictated by their suppliers did conflict with antitrust; the Court condemned the restraint as tantamount to a per se illegal private resale price maintenance agreement. The Court has termed the kind of restraint in *Midcal* "hybrid," to indicate its inherent admixture of state assistance and private anticompetitive activity.¹¹ Such a restraint is valid only if it meets the requirements of state action immunity. The *Midcal* scheme was not immune, because the state did not actively supervise the prices dictated by the suppliers.

court relied on *Surgical Care Center, L.C. v. Hosp. Serv. Dist. No. 1*, 171 F.3d 231, 234 (5th Cir. 1999), where the court observed that the label "immunity" is only a "convenient shorthand" expression. We use the term immunity as a convenient way of referring to the state action doctrine in general, making no representations about its technical applicability.

4 317 U.S. 341, 350-51 (1943).

5 See *infra* Section I.A.

6 Throughout this Article, unless otherwise specifically indicated, we use the terms "state" and "government" to denote state and local governmental entities. The doctrine of state action immunity distinguishes between actions of the state as sovereign and those of subordinate bodies. See *infra* notes 21-24 and accompanying text. By contrast, no distinction is made between the state and subordinate governments for purposes of identifying unilateral restraints imposed by government. Of course, neither of these doctrines applies to anticompetitive federal actions.

7 475 U.S. 260 (1986).

8 *Id.* at 270.

9 *Id.* at 270 ("We therefore need not address whether, even if the controls were to mandate § 1 violations, they would be exempt under the state-action doctrine from antitrust scrutiny.")

10 445 U.S. 97, 103 (1980).

11 *Fisher*, 475 U.S. at 267-68.

Thus, the Court's state action jurisprudence recognizes both unilateral restraints imposed by government, which do not conflict with antitrust, and hybrid restraints, which do. Hybrid restraints, in turn, may or may not meet the requirements of state action immunity; the agricultural program in *Parker* was immune, but the resale price restraint in *Midcal* was not. In cases in which the requirements of immunity are not satisfied, therefore, the line between hybrid and unilateral restraints may determine the scheme's antitrust validity. As will become evident in the pages that follow, this line is extraordinarily elusive.

Although scholars have labored over the nuances of state action immunity,¹² they have largely ignored the separate issue of antitrust conflict.¹³ In this Article, we articulate a method of classifying state-supported restraints as unilateral or hybrid. We take as a jumping off point the statements of the Supreme Court. But the Court's guidance has been sparse. The full Court has only explicitly relied on the doctrine in one case, *Fisher*, and its teaching there was cryptic. Indeed, the Court seemed to discover the idea of a unilateral restraint rather late in its jurisprudence of state-supported anticompetitive actions; curiously, lower courts and litigants have often simply overlooked the doctrine. As a result, no principle has emerged full-blown from the cases. In any event, our objective is not to distill the doctrine from Supreme Court precedents on

12 See, e.g., Phillip Areeda, *Antitrust Immunity for "State Action" After Lafayette*, 95 HARV. L. REV. 435 (1981); John Cirace, *An Economic Analysis of the "State-Municipal Action" Antitrust Cases*, 61 TEX. L. REV. 481 (1982); Frank Easterbrook, *Antitrust and the Economics of Federalism*, 26 J.L. & ECON. 23 (1983); Einer R. Elhauge, *The Scope of Antitrust Process*, 104 HARV. L. REV. 667 (1991); Merrick B. Garland, *Antitrust and State Action: Economic Efficiency and the Political Process*, 96 YALE L.J. 486 (1987); Daniel J. Gifford, *The Antitrust State-Action Doctrine After Fisher v. Berkeley*, 39 VAND. L. REV. 1257 (1986); Robert P. Inman & Daniel L. Rubinfeld, *Making Sense of the Antitrust State-Action Doctrine: Balancing Political Participation and Economic Efficiency in Regulatory Federalism*, 75 TEX. L. REV. 1203 (1997); Thomas M. Jorde, *Antitrust and the New State Action Doctrine: A Return to Deferential Economic Federalism*, 75 CAL. L. REV. 227 (1987); John E. Lopatka, *State Action and Municipal Antitrust Immunity: An Economic Approach*, 53 FORDHAM L. REV. 23 (1984) [hereinafter Lopatka, *Municipal Immunity*]; John E. Lopatka, *The State of "State Action" Antitrust Immunity: A Progress Report*, 46 LA. L. REV. 941 (1986) [hereinafter Lopatka, *Progress Report*]; William H. Page, *Antitrust, Federalism, and the Regulatory Process: A Reconstruction and Critique of the State Action Exemption After Midcal Aluminum*, 61 B.U. L. REV. 1099 (1981) [hereinafter Page, *Federalism*]; William H. Page, *Interest Groups, Antitrust, and State Regulation: Parker v. Brown in the Economic Theory of Legislation*, 1987 DUKE L.J. 618 [hereinafter Page, *Interest Groups*]; William H. Page & John E. Lopatka, *State Regulation in the Shadow of Antitrust: FTC v. Tico Title Insurance Co.*, 3 SUP. CT. ECON. REV. 189, 191-92 (1993); Steven Semeraro, *Demystifying Antitrust State Action Doctrine*, 24 HARV. J.L. & PUB. POL'Y 203 (2000); Matthew Spitzer, *Antitrust Federalism and Rational Choice Political Economy: A Critique of Capture Theory*, 61 S. CAL. L. REV. 1293 (1988); John Shephard Wiley, *A Capture Theory of Antitrust Federalism*, 99 HARV. L. REV. 713 (1986).

13 For brief treatments of the topic, see, for example, 1 PHILLIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW*, ¶¶ 217b2-217d, at 306-19 (2d ed. 2000); Garland, *supra* note 12, at 502-08; Lopatka, *Progress Report*, *supra* note 12, at 1030-37; Page, *Interest Groups*, *supra* note 12, at 661-64. As a review of our previous articles would demonstrate, our own views on the issue have evolved.

the issue but to derive a sound doctrine from the substantive principles of antitrust law and the concerns that underlie the protection of state action from antitrust scrutiny.

We argue here that a unilateral governmental restraint is one in which public officials determine the nature and extent of the resulting consumer injury, even though the decision is effectuated through the actions of private parties in compliance with the government's mandates. A hybrid restraint, by contrast, is one in which the government specifically empowers private actors to exercise discretion as to the nature or level of consumer injury in a way that closely resembles an antitrust violation. The ingredients of a hybrid restraint, therefore, are focused government intervention, private discretion, and conduct analogous to a recognized antitrust offense. Determining whether a restraint is analogous to an antitrust offense requires an examination of the underlying goals of the relevant antitrust rules, which were designed to address private restraints, as well as the idiosyncrasies of the government action at issue. If state sponsorship implements or facilitates private discretion in a way that mimics a private restraint, the restraint is hybrid, and it must meet the requirements of state action immunity in order to avoid condemnation.

The tension between antitrust and state regulation does not end with a determination that a restraint is hybrid and not immune. It extends to the issue of antitrust remedies. A facially invalid government directive can be preempted in the abstract, implying that government officials cannot enforce it and private parties need not obey it. Non-immune hybrid restraints invalid only in particular circumstances need to be addressed through tailored injunctions, which may include an order from an antitrust court prohibiting a party from complying with a government mandate. We explain below that antitrust courts have the constitutional power to fashion injunctions that bind state actors and those subject to state control. But the assertion of federal power over state policy in the guise of a prospective antitrust remedy produces an undeniable tension. In addition, antitrust relief may include an award of treble damages for past harm. States and subordinate governments are shielded from damage liability, but private parties participating in hybrid restraints are not. The consequence is that a private party can incur treble damage liability for complying with a government directive. Again, the limits of federalism are tested.

In the next section, we locate the Supreme Court's hybrid restraint doctrine in relation to the state action antitrust immunity. We then set out our theory of a unified doctrine that separates state-supported arrangements that conflict with the antitrust laws from those that do not. Next, we examine state-mandated distributional restraints. We show how the Court has applied the rule against private resale price maintenance by somewhat strained analogy to state-endorsed restraints on distribution. We

dwelling particularly on the peculiarities in the Court's use of the idea of agreement. We then consider the application of the hybrid restraint concept to horizontal restraints, arguing that it reaches not only state authorized *express* collusion but state practices that significantly facilitate *tacit* collusion and serve no competitively benign purpose. We discuss in detail two important decisions of the courts of appeals that have reached this result. Finally, we address the application of our theory to state-created monopolies, demonstrating that unilateral governmental restraints granting monopolies to private firms generally do not violate Sections 1 or 2 of the Sherman Act.

I. Background: State Action Immunity and Hybrid Restraints

We have elsewhere examined in detail the Supreme Court's doctrines reconciling antitrust and state regulation.¹⁴ Here, we merely sketch the development of these doctrines in order to lay the groundwork for a more detailed exploration of the concept of hybrid restraints.

A. State Action Immunity

In *Parker v. Brown*,¹⁵ the Supreme Court refused to condemn a California regulatory scheme that allowed raisin growers to fix prices.¹⁶ The Court grounded its decision on federalism: "In a dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress."¹⁷ It reasoned that if Congress had wanted to apply the Sherman Act to sovereign states, it would have

¹⁴ See Lopatka, *Municipal Immunity*, *supra* note 12; Lopatka, *Progress Report*, *supra* note 12; Page, *Federalism*, *supra* note 12; Page, *Interest Groups*, *supra* note 12; Page & Lopatka, *supra* note 12, at 191-92.

¹⁵ 317 U.S. 341 (1943). The antecedent of the doctrine is *Olson v. Smith*, 195 U.S. 332 (1904), where the Court held that a state regulatory scheme limiting entry into and fixing rates in a marine pilot market was not preempted by the Sherman Act.

¹⁶ Although the Court clearly rejected the antitrust claim, precisely what the Court held is a matter of some dispute. Justice Stevens argued that the Court held merely that state officials, acting pursuant to express legislative command, do not violate the Sherman Act by engaging in conduct that would violate the Act if undertaken by private parties. See *Cantor v. Detroit Edison Co.*, 428 U.S. 579, 589-90 (1976) (plurality opinion). But Justice Stewart contended that the Court held that the California statute was not preempted by the Sherman Act, so that presumably no parties effecting the restraint, whether public or private, can be found to have committed an antitrust violation. *Id.* at 621-22 (Stewart, J., dissenting). The Court ultimately endorsed Justice Stewart's interpretation. See *S. Motor Carriers Rate Conf., Inc. v. United States*, 471 U.S. 48, 57 (1985) (citing Justice Stewart's dissenting opinion in *Cantor* and declining "to reduce *Parker's* holding to a formalism that would stand for little more than the proposition that Porter Brown sued the wrong parties").

¹⁷ *Parker*, 317 U.S. at 351.

expressed that intent more clearly.¹⁸ Yet the Court did not hold that federalism shelters all state-sponsored anticompetitive conduct from the antitrust laws. It observed, for example, that “a state does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful.”¹⁹ The Court, therefore, recognized the possibility that federal antitrust law would trump some state-supported restraints, but its guidance was minimal.

In later decisions, the Court clarified the reach of the state action immunity. It held that anticompetitive actions attributable to sovereign state actors are automatically immune from the antitrust laws.²⁰ But critically for present purposes, the Court held that municipalities,²¹ agencies composed of members of the profession they regulate,²² and independent state regulatory agencies²³ do *not* constitute the state as sovereign.²⁴ This latter cluster of decisions proved important to the emergence of the unilateral restraints doctrine. If acts of subordinate government units had been held automatically immune from antitrust exposure under the state action doctrine, an inquiry into whether a restraint escaped antitrust condemnation as one unilaterally imposed by government would have been largely superfluous: the validity of restraints adopted by these entities that contemplated private decision-making could have been assessed exclusively under the standards of *Midcal*.

In *Midcal*, the Court held that private parties are entitled to state action immunity when two requirements are satisfied: “First, the challenged restraint must be one clearly articulated and affirmatively

18 *Id.*

19 *Id.*

20 See *Hoover v. Ronwin*, 466 U.S. 558, 568 (1984); *Bates v. State Bar of Ariz.*, 433 U.S. 350, 361 (1977).

21 *City of Lafayette v. La. Power & Light Co.*, 435 U.S. 389, 412-13 (1978).

22 *Goldfarb v. Va. State Bar*, 421 U.S. 773, 791 (1975).

23 *S. Motor Carriers Rate Conf., Inc. v. United States*, 471 U.S. 48, 63 (1985). The issue before the Court was whether the agency could itself effectively authorize private parties to engage in a restraint or, in other words, the first prong of the *Midcal* test—“the challenged restraint must be one clearly articulated and affirmatively expressed as state policy,” *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980) (internal quotation marks omitted). But the determination of what constitutes the state for purposes of the antitrust status of its own restraint is identical to the determination of what constitutes the state for purposes of authorizing a private restraint.

24 At a minimum, a state legislature, when acting with the concurrence of the governor, is a sovereign actor. See *Hoover*, 466 U.S. at 567-68 (observing that “when a state legislature adopts legislation,” with the constitutionally required assent of the governor, “its actions constitute those of the State”). A state supreme court, when acting legislatively rather than judicially, is the state itself for purposes of an automatic antitrust exemption. See *id.* at 568; *Bates*, 433 U.S. at 360. The Court did not explain why it ostensibly limited automatic immunity to the legislative acts of a supreme court. The Court explicitly declined to decide “whether the Governor of a State stands in the same position as the state legislature and supreme court for purposes of the state-action doctrine.” *Hoover*, 466 U.S. at 568 n.17. A district court has held that the governor is indeed a sovereign actor. See *Astoria Entm’t, Inc. v. Edwards*, 159 F. Supp. 2d 303, 324 (E.D. La. 2001).

expressed as state policy; second, the policy must be actively supervised by the State itself.”²⁵ The implication is that a sovereign state actor—one that would enjoy automatic immunity for its own anticompetitive conduct—must express the policy. Immunity does not require that the state compel the actions of the private party; a permissive policy is enough.²⁶ Further, the policy, whether mandatory or permissive, need not in fact be as “clearly articulated and affirmatively expressed” as the *Midcal* formulation suggests.²⁷ The Court held that it is sufficient if “anticompetitive effects logically would result from”²⁸ or “foreseeably will result” from state pronouncements.²⁹ As for supervision, the Court held that active indeed means active. The state must exercise “sufficient independent judgment and control” to demonstrate “that the details of the rates or prices have been established as a product of deliberate state intervention, not simply by agreement among private parties.”³⁰

The Court also held that, though subordinate state bodies are not sovereign actors entitled to automatic immunity, they are not private actors subject to both prongs of the *Midcal* test either. Rather, municipalities and independent agencies need only satisfy the first prong of *Midcal*: They must act pursuant to a clear state policy, but their actions need not be actively supervised.³¹ Further, a grant of home rule power to a city does not satisfy the clear state policy prong of *Midcal*.³² This latter decision implied that a subordinate body could not effectively become the sovereign for state action purposes, thereby largely eliminating a role for a

25 *Midcal Aluminum, Inc.*, 445 U.S. at 105 (internal quotation marks omitted). Whatever uncertainty remained as to whether state action immunity includes private parties was put to rest in *Motor Carriers*, 471 U.S. at 57 (“*Parker* immunity is available to private parties . . .”).

26 *Motor Carriers*, 471 U.S. at 60.

27 As one court observed, “the ‘clear articulation’ label is not quite the hurdle that its language suggests, because it has always been construed as synonymous with the foreseeability test.” *Automated Salvage Transp., Inc. v. Wheelabrator Env’tl. Sys., Inc.*, 155 F.3d 59, 69 (2d Cir. 1998).

28 *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 42 (1985).

29 *Id.* at 43. In *City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365, 373 (1991), the Court found that “[i]t is enough . . . if suppression of competition is the ‘foreseeable result’ of what the statute authorizes.” Finding that a statute authorizing cities to regulate the location and size of structures through zoning ordinances was sufficiently specific to immunize an allegedly anticompetitive regulation of billboards, the Court indicated that rather general authorization suffices. It rejected the dissent’s contention that, for immunity, the state must “expressly authorize the municipality to engage (1) in specifically ‘economic regulation’ (2) of a specific industry,” declaring that the “dual specificities are without support in our precedents, for the good reason that they defy rational interpretation.” *Id.* at 373 n.4 (citations omitted).

30 *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 634-35 (1992). In *Patrick v. Burget*, 486 U.S. 94, 101 (1988), the Court explained that the state must “exercise ultimate control over the challenged anticompetitive conduct.” State officials must “have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy.” *Id.*

31 *Town of Hallie*, 471 U.S. at 46-47. The case involved a city, and the Court held that the active supervision requirement does not apply to such an entity. In dicta, it noted that “[i]n cases in which the state actor is a state agency, it is likely that active supervision would also not be required, although we do not here decide that issue.” *Id.* at 46 n.10.

32 *Cnty. Communications Co. v. City of Boulder*, 455 U.S. 40, 54-56 (1982).

separate unilateral restraint doctrine, through the simple expedient of a very broad delegation of power.

Oddly, the Court has never explained why federalism dictates the specific form of the doctrine that has taken shape over the years.³³ We have argued that the unspoken principle animating the doctrine is that antitrust should defer to state restraints that are ancillary to some positive regulatory program but not to naked repeals of federal statutory requirements.³⁴ A state may restrict competitive behavior in order to correct a market failure; if the failure is real, it is pursuing a policy congruent with antitrust policy. In such a case, there is no conflict between the objective of the antitrust law and the objective of the state program; consumer welfare in such an instance is ill-served through the process that normally protects consumers. But a state may also sacrifice the interests of consumers in order to serve some interest it deems more important.³⁵ Whatever the reason for state intervention in the market, so long as the state itself takes the operative action or both adopts its policy clearly and actively supervises private conduct to assure that the policy is implemented, the federal antitrust laws are inapplicable. A simple suspension of antitrust strictures without adequate state supervision, however, reflects a naked repeal of antitrust. It negates federal policy without substituting any coherent alternative policy, and it is vulnerable to antitrust attack unless it enjoys some separate federal protection, such as that provided by the Twenty-first Amendment.

B. *Unilateral and Hybrid Restraints in the Supreme Court*

While the Court was refining the principle behind the *Parker* doctrine, it held that even a governmental restraint that would not be immune under the doctrine just outlined might nevertheless be valid if it does not conflict with substantive antitrust prohibitions. The Court first relied on the notion that a unilateral government restraint simply does not conflict with Section 1 of the Sherman Act in the 1986 case of *Fisher v. City of Berkeley*,³⁶ though it found rudimentary antecedents of the idea in several earlier cases and returned to the doctrine a year later in *324 Liquor Corp. v. Duffy*.³⁷ But

33 The tension between the regulatory goals of states and the purpose of national antitrust policy is manifest, and obviously more than one resolution is possible. Richard Posner has observed, "A situation in which the benefits of government action are concentrated in one state and the costs in other states is a recipe for irresponsible state action. This is a genuine downside of federalism. The federal government . . . is . . . less subject to take-over by a faction. I am not myself inclined to make a fetish of federalism." RICHARD A. POSNER, *ANTITRUST LAW* 281 (2d ed. 2001).

34 See Page & Lopatka, *supra* note 12, at 191-92.

35 As the Court once observed, "[T]he function of government may often be to tamper with free markets, correcting their failures and aiding their victims . . ." *Fisher v. City of Berkeley*, 475 U.S. 260, 264 (1986).

36 *Id.*

37 479 U.S. 335 (1987).

in none of these cases did the Court lay out a coherent rationale that could guide the application of the doctrine to the myriad situations in which government and private conduct interact to produce anticompetitive results. Some of the discussion was misleading. But more important, the decisions tended to be highly specific to the peculiar restraint at issue. The Court declared that a particular restraint in the context of a specific regulatory regime was or was not a unilateral restraint but failed to articulate a principle of “concerted action” addressed generally to the unique nature of the interaction between the state and those subject to its control.

In *Fisher*, the city had adopted an ordinance freezing rents and creating a Rent Stabilization Board to make annual adjustments in rent levels. The Court might have decided *Fisher* on state action grounds,³⁸ as it had decided three earlier antitrust challenges to city regulatory programs.³⁹ Instead, the Court declined to reach the issue of immunity,⁴⁰ holding instead that the ordinance did not conflict with the antitrust laws because the rent control mechanism did not involve the element of agreement required by Section 1:⁴¹ “[T]he rent ceilings imposed by the

38 It could have held, for example, that the Berkeley ordinance was clearly authorized by state law and that active supervision was not required, either because the restraint was the ordinance itself as opposed to the actions of property owners in compliance with it or because the restraint was self-enforcing. Justice Powell concurred in the decision essentially on this basis, though he did not discuss the supervision issue at all. See *Fisher*, 475 U.S. at 273-74 (Powell, J., concurring). Or it could have held that the ordinance did not satisfy the clear state policy requirement because the rent control measures were not the foreseeable result of any statutory obligations. Justice Brennan dissented from the decision on this ground. See *id.* at 281 (Brennan, J., dissenting).

39 In *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389, 392-94 (1978), the Court held that the city was not automatically immune from antitrust liability by virtue of its status as a city for alleged anticompetitive actions directed against a competing electric utility. In *Community Communications Co. v. City of Boulder*, 455 U.S. 40, 47-48 (1982), the Court refused to find immunity for an emergency ordinance enacted under the city’s home rule power to prohibit temporarily the expansion of a cable television company’s service area. Finally, in *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 44, 47 (1985), the Court found that the city’s decision to condition the use of its sewage collection and transportation services on the use of its sewage treatment services was immune because the action was clearly authorized by state law and a city is not subject to the active supervision requirement.

40 See *Fisher*, 475 U.S. at 270.

41 *Id.* The plaintiff landlords alleged that the ordinance was unconstitutional because it was pre-empted by the federal antitrust laws, not that the city had violated those laws. A state or local law can be pre-empted in the abstract, but only if it “mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.” *Rice v. Norman Williams Co.*, 458 U.S. 654, 661 (1982). In other words, pre-emption is appropriate only if “the conduct contemplated by the statute is in all cases a *per se* violation” of the antitrust laws. *Id.* A law authorizing *per se* illegal conduct may nevertheless “be saved from invalidation under the doctrine of *Parker v. Brown*,” *id.* at 662 n.9, presumably by providing for active supervision of the private conduct. And in operation, the arrangements private parties make with each other “will be subject to Sherman Act analysis under the rule of reason,” *id.* at 662, so those private actors apparently could be held liable for antitrust violations unless their conduct is protected by the state action doctrine. Thus, whether a restraint is challenged as unconstitutional, and therefore pre-empted, or those involved in the restraint are alleged to have violated the antitrust laws, the issue of whether the restraint involves concerted action is the same.

[A] state statute, when considered in the abstract, may be condemned under the antitrust laws only if it mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.⁵¹

Thus, a state law could facially conflict with antitrust only if it authorized or mandated a per se violation, a label reserved for practices, such as price fixing, that the law condemns “without elaborate inquiry as to the precise harm they have caused or the business excuse for their use.”⁵² Because the statute in *Rice* only restored the distiller’s ability to limit the distribution of its product in California through a vertical nonprice restraint, which would be judged under the rule of reason in any event, the statute was not invalid on its face, and the legality of private conduct under its terms would be determined on a case-by-case basis.⁵³ Indeed, the Court noted the possibility that “particular *conduct* pursuant to the statute might be subject to a challenge under one or more of the established *per se* rules of illegality,”⁵⁴ even though the statute could not be condemned in the abstract.⁵⁵

The Court analogized the case to *Joseph E. Seagram & Sons, Inc. v. Hostetter*,⁵⁶ which also refused to find facially invalid a state regulation of liquor distribution. The regulation at issue in *Hostetter* required distributors to file price schedules with the State Liquor Authority along with an “affirmation” that prices listed were as low as prices charged anywhere else in the United States.⁵⁷ That regulation, according to the *Rice* Court, merely required the collection of price information to “support” the most-favored-nation affirmations and, as such, did not place “irresistible economic pressure” on distributors to violate Section 1; indeed, the regulation depended upon Section 1 to prevent conspiracies to raise the prices on which the affirmations were based. But the Court did not call the schemes in *Rice* or *Hostetter* hybrid restraints.

51 *Id.* at 661.

52 *N. Pac. R.R. v. United States*, 356 U.S. 1, 5 (1958).

53 *See Rice*, 458 U.S. at 662 (“The manner in which a distiller utilizes the designation statute and the arrangements a distiller makes with its wholesalers will be subject to Sherman Act analysis under the rule of reason.”).

54 *Id.* at 662 n.8. The Court must have been using the term “pursuant to” in a very loose sense. If a statute *authorized*, though did not compel, per se illegal behavior, it would be subject to facial pre-emption. The Court apparently has in mind per se illegal conduct that is not *prohibited* by the statute. To say that such conduct is “pursuant to” the statute is a linguistic stretch.

55 The Court also recognized that, because the facial antitrust challenge to the statute failed, “it is not necessary for us to consider whether the statute may be saved from invalidation under the doctrine of *Parker v. Brown*.” *Id.* at 662 n.9.

56 384 U.S. 35 (1966).

57 *Id.* at 39-40.

Ordinance and maintained by the Rent Stabilization Board have been unilaterally imposed by government upon landlords to the exclusion of private control.”⁴² The Court explained that neither a vertical nor a horizontal conspiracy arises when a governmental entity prescribes specific, uniform behavior and private competitors comply. Landlords who comply with “a restraint imposed unilaterally by government” because of the law’s “coercive effect” do not form individual agreements with the government, nor do they form a “conspiracy” among themselves: “There is no meeting of the minds here.”⁴³

But borrowing a term coined by Justice Stevens in *Rice v. Norman Williams Co.*,⁴⁴ the Court distinguished this sort of restraint from “hybrid” restraints, those in which “nonmarket mechanisms merely enforce private marketing decisions,”⁴⁵ so that “private actors are thus granted a degree of private regulatory power.”⁴⁶ For example, in two prior cases—*Midcal* and *Schwegmann*—the Court had condemned state statutes that mandated compliance with resale prices set by suppliers. These restraints, according to the *Fisher* Court, involved a significant “degree of free participation by private economic actors”⁴⁷ and were therefore “quite different from the pure regulatory scheme imposed by Berkeley’s Ordinance.”⁴⁸ They did satisfy the concerted action requirement of Section 1 and, thus, came into conflict with antitrust’s prohibition of resale price maintenance.⁴⁹ We examine some hidden complexities in this characterization more fully in the next section but shelve those questions temporarily in order to explore the history of the Court’s use of the hybrid restraints concept.

Because *Rice* was the origin of the critical term “hybrid restraint,” it warrants close attention. The Court there upheld against a facial attack California’s “designation” statute, which prohibited any state-licensed liquor dealer from importing a brand of liquor unless the distiller of that brand had specifically authorized the dealer to do so. The statute was enacted in response to Oklahoma’s liquor laws, which were understood to prohibit a distiller from limiting its sales to selected Oklahoma wholesalers.⁵⁰ As a result, a distiller’s normal ability to control the distribution of its product in California was thwarted, because a California wholesaler could obtain the liquor from an Oklahoma wholesaler. The majority in *Rice* announced the principle that:

42 *Fisher*, 475 U.S. at 266.

43 *Id.* at 267.

44 458 U.S. 654, 665 (1982) (Stevens, J., concurring).

45 *Fisher*, 475 U.S. at 268.

46 *Id.* at 268 (citing *Rice*, 458 U.S. at 665 (Stevens, J., concurring)).

47 *Id.* at 268.

48 *Id.* at 269.

49 *Id.*

50 *Rice*, 458 U.S. at 657.

In his concurrence, however, Justice Stevens did characterize the statute in *Rice* as a hybrid restraint, because it “contemplates a private market decision but provides a nonmarket mechanism for enforcing the decision.”⁵⁸ He thus distinguished the restraint both from a “public regulatory scheme,” such as a statute prohibiting oil companies from operating service stations in the state,⁵⁹ and from a “purely private restraint,” such as an ordinary resale price maintenance agreement.⁶⁰ Presaging the Court’s analysis in *Fisher*, he identified two earlier cases as involving hybrid restraints. In the first, *Schwegmann Bros. v. Calvert Distillers Corp.*,⁶¹ a state statute provided that an agreement on resale prices between a liquor supplier and a retailer would bind all other retailers, even if they did not sign a resale price agreement. At the time, simple resale price maintenance agreements permitted by a state were lawful under the Miller-Tydings Act. But the Court held invalid the non-signer provision, by which distillers were able to command dealers to comply with terms established in contracts with nonsigners. *Schwegmann*, according to Justice Stevens in *Rice*, stands for the proposition that:

[A] state statute that facilitates the manufacturer’s decision to impose a vertical restriction is not lawful simply because the Sherman Act permits the manufacturer, if it has sufficient power in the private market, to impose that same restriction without the aid of the statute. In other words, a statute that gives distributors additional power over the wholesale or retail market to impose an otherwise permissible restraint might not pass muster under the Sherman Act.⁶²

Justice Stevens’ other example of a hybrid restraint was *Midcal*, which struck down statutes that permitted wine suppliers to set resale prices of all wholesalers within each trading area. Stevens observed that “[e]ven though the State presumably could regulate the wine market by fixing retail prices itself, it could not empower private parties to undertake such regulation.”⁶³ By contrast, the statute in *Hostetter*, he opined, was not an example of a hybrid restraint but rather of a public regulatory scheme, because “it did not grant liquor distributors a degree of private regulatory power.”⁶⁴

58 *Rice*, 458 U.S. at 665. Justice Stevens’s description of a “hybrid” restraint was reminiscent of his observation in *Cantor v. Detroit Edison Co.*, 428 U.S. 579, 592 (1976), that restraints involving the government are typically “a blend of private and public decisionmaking.”

59 *See Exxon Corp. v. Governor of Maryland*, 437 U.S. 117 (1978).

60 *See Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911).

61 341 U.S. 384 (1951).

62 *Rice*, 458 U.S. at 667.

63 *Id.* at 667 n.2 (Stevens, J., concurring).

64 *Id.* at 665, 666 n.1.

Turning to the designation statute at issue in *Rice*, Stevens disagreed with the majority's assertion that the California statute merely restored a distiller's power to control distribution that was taken away by the Oklahoma laws because the statute might confer more power on the distiller than the Oklahoma law eliminated.⁶⁵ But he agreed with the majority that, on the record before the Court, the statute could not be condemned on its face, because it involved only a vertical nonprice restraint.⁶⁶ He maintained that the case should be remanded to determine "whether the statute's provision to distillers of an additional club over California importers affords distillers an unreasonable degree of unsupervised power to regulate their distribution practices that they would not otherwise enjoy under a free market."⁶⁷ Apparently Justice Stevens would have been willing to hold the statute facially invalid if the record demonstrated that the statute, though contemplating only vertical nonprice restraints, created "an unacceptable and unnecessary risk of anticompetitive effect."⁶⁸

Justice Stevens's definition of a hybrid restraint as one in which a "nonmarket mechanism" enforces a private market decision typifies the ambiguities in the Court's pronouncements on the issue.⁶⁹ If he meant his definition to be comprehensive, it falls short. By "nonmarket mechanism," Justice Stevens apparently had in mind something other than the legal enforcement of contracts, because he cited as a "purely private restraint"⁷⁰ the non-price distribution agreement at issue in *Continental T.V., Inc. v. GTE Sylvania Inc.*⁷¹ But the hybrid character of a restraint turns on the nature of the underlying arrangement, not on the kind of sanctions a state specifies for enforcing it. If, for example, a state legislature or even a state supreme court were to declare that price fixing agreements are judicially enforceable, the result would surely be a hybrid restraint.

Alluding to Justices Stevens's distinctions, the *Fisher* majority, which included Stevens, characterized *Schwegmann* and *Midcal* as hybrid restraint cases, because the statutes provided governmental enforcement of privately established prices. In *Fisher* itself, in contrast, government actors fixed the prices and compelled private actors to comply. The Berkeley ordinance was not a hybrid restraint because "it place[d] complete control over maximum rent levels exclusively in the hands of the Rent Stabilization Board. Not just the controls themselves but also the rent ceilings they mandate [had] been unilaterally imposed on the landlords by

65 *Id.* at 667-68.

66 *Id.* at 668.

67 *Id.* at 669.

68 *Id.* at 668.

69 *See id.* at 665, 668.

70 *Id.* at 665-66.

71 433 U.S. 36 (1977).

the city.”⁷² The involvement of the government at the stage of price-setting rendered the restraint one unilaterally imposed by government,⁷³ or apparently what Stevens would term a purely public regulatory scheme.

The year after deciding *Fisher*, the Court in *324 Liquor Corp. v. Duffy*⁷⁴ condemned as hybrid a liquor regulatory scheme that required liquor wholesalers to post price schedules and retailers to charge at least 112% of the wholesale prices posted at the time of retail sale. But the law allowed wholesalers to compel retailers to charge more than 112% of their wholesale cost, either by charging actual wholesale prices below posted prices or by selling large quantities of liquor and then raising posted wholesale prices before all of the liquor could be sold at retail.⁷⁵ The Court explicitly found that the scheme was a hybrid restraint because it granted private actors “a degree of private regulatory power.”⁷⁶ Moreover, it was not entitled to state action immunity because the state did not actively supervise the prices.⁷⁷

To summarize, the Court distinguishes among restraints unilaterally imposed by government, hybrid restraints, and private restraints. As we explain in more detail below, a restraint moves from the category of

72 *Fisher v. City of Berkeley*, 475 U.S. 260, 269 (1986).

73 Justice Brennan countered that “the lack of state supervision over price-fixing activities [in *Schwegmann and Midcal*] was only relevant to whether the challenged statutes were immune from antitrust liability under *Parker v. Brown*.” *Fisher*, 475 U.S. at 277 n.2 (Brennan, J., dissenting) (citations omitted). He noted that neither decision drew a distinction between “unilateral” and “hybrid” restraints and concluded that “regardless of whether Berkeley’s landlords have some role in setting the prices they must charge, the coercive effect of the city’s Ordinance results in concerted action violative of the Sherman Act.” *Id.*

74 479 U.S. 335 (1987).

75 *Id.* at 339-40. The enforcement agency allowed wholesalers to sell liquor by the case at a discount. As a result, the actual wholesale price per bottle could be lower than the posted bottle price. The retailer was required to charge 112% of the posted bottle price, so that the margin between actual wholesale cost and retail price could be greater than 12%, based on the discretion of the wholesaler in determining the amount of the case discount.

76 *Id.* at 345 n.8 (quoting *Fisher*, 475 U.S. at 268).

77 *Id.* at 344. Although the *Fisher* Court held that a unilateral government restraint cannot run afoul of Section 1, it also suggested in passing that an ostensibly unilateral restraint might be a hybrid one in disguise: “There may be cases in which what appears to be a state- or municipality-administered price stabilization scheme is really a private price-fixing conspiracy, concealed under a ‘gauzy cloak of state involvement.’” *Fisher*, 475 U.S. at 269. But what the Court meant is opaque. The Court went on to suggest that it had in mind a restraint disguised through corruption, noting, “However, we have been given no indication that *such corruption* has tainted the rent controls imposed by Berkeley’s Ordinance.” *Id.* (emphasis added). If this is what the Court meant, its teaching was undercut some years later in *City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 374 (1991), where the Court held that public corruption would not create a conspiracy between the city and the private firm sufficient to abrogate state action immunity. But the *Fisher* passage may mean that a court is entitled to scrutinize the degree of government involvement in the process of formulating a requirement in determining the character of the restraint. For example, if a Rent Stabilization Board did not actually review prices collusively established by landlords, and simply ratified and enforced them, the antitrust court might refuse to find the action unilateral. This principle would be similar to the Court’s holding in *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 635, 638 (1992), that mere nominal review of private conduct is insufficient to satisfy the active supervision requirement of state action immunity.

unilateral to hybrid restraint when private participation in a state-sponsored decision-making process crosses some critical threshold of similarity to established antitrust prohibitions. So understood, Justice Stevens's suggestion in *Rice* that the distinction is between hybrid restraints and "public regulation of the market"⁷⁸ is misleading; even the Court in *Fisher*, though it emphasizes our preferred language of unilateral restraints, at one point uses the term "pure regulatory scheme" as a synonym.⁷⁹ The reference to "regulation" seems to imply that a scheme under which private parties are allowed to fix prices under the supervision of the state—for example, the kind of system at issue in *Parker*—is not a hybrid restraint. And yet private participation in the decision-making process in such a case is undeniably sufficient to classify the resulting restraint as hybrid; the supervision of private conduct in *Parker* helped confer immunity on the arrangement but did not alter its status as a hybrid restraint.⁸⁰ Under this view, a similarity between unilateral and immune hybrid restraints becomes more apparent. If a restraint is unilateral, the state or local government excludes private discretion entirely; if it is hybrid and immune, there may be private discretion, but it is subject to ex post state supervision.

Finally, the Court's analysis implies the existence of a private restraint, one in which the government's participation is insignificant for purposes of the concerted action requirement of Section 1, but even this term can be misunderstood. At an elemental level, government involvement is necessary for any restraint of trade. The government creates property rights, enforces contracts, and gives legal identity to corporations.⁸¹ The Court could not have meant that governmental actions such as these suffice to make the government a party to concerted action whenever private actors rely upon the legal framework of the economy to accomplish an anticompetitive result. If these actions were sufficient, the category of hybrid restraints would be residual, containing any restraint that is not unilateral. Yet the *Fisher* Court was careful to limit the concept of a hybrid restraint. Indeed, Justice Stevens explicitly recognized a

78 *Rice v. Norman Williams Co.*, 458 U.S. 654, 665 n.1 (1982) (Stevens, J., concurring).

79 *Fisher*, 475 U.S. at 269.

80 The alternative to this typology is one that recognizes four categories of restraints—private, hybrid, unilateral, and regulatory. But the antitrust significance of hybrid and regulatory restraints would be identical, and so the four-category typology would be needlessly complicated.

81 An analogous issue arose in *Northern Securities Co. v. United States*, 193 U.S. 197 (1904). Railroads merging through the device of a holding company defended an antitrust attack in part on the ground that the holding company was not prohibited from acquiring the stock of the railroads by its charter, which was issued pursuant to state law. The federal government, the railroads contended, was forbidden by the Tenth Amendment from invading the rights of the states by prohibiting an act that was permissible under the state charter. The Court responded, "We cannot conceive how it is possible for anyone to seriously contend for such a proposition." *Id.* at 345. Similarly, the fact that the state created the legal entity of a corporation with the power to acquire stock did not make the state an accomplice in the corporation's anticompetitive acquisition.

category of “purely private restraint[s].”⁸² In a private restraint, therefore, the government does no more than to establish the preconditions for trade.

II. A Unified Theory of Hybrid Restraints

The foregoing sketch of Supreme Court law serves to highlight the problem of reconciling state economic regulation and the federal antitrust laws but not to resolve it. To be sure, certain principles emerge clearly. For example, as a matter of federalism, state regulation that represents a positive policy choice, rather than a naked repudiation of antitrust, is immune from antitrust attack regardless of its effect on consumers. But state regulation that does not conflict with the antitrust laws avoids condemnation whether or not it qualifies for state action immunity. Because a violation of Section 1 of the Sherman Act requires concerted action, a “unilateral” restraint of trade, whether state-supported or not, does not conflict with the statute. Compliance with a specific state mandate never creates an agreement between the government and the complying party. And the requisite agreement is not formed simply because multiple private parties comply with the same specific mandate, even if compliance has anticompetitive effects.

These principles, however, which have been announced piecemeal, do not provide an overarching theory to harmonize federal antitrust law and state economic regulation. They do not connect the idea of antitrust immunity for state action to the concept of antitrust indifference to restraints unilaterally imposed by government, even though both involve deliberate state intervention in the economy. They do not provide a coherent rationale to identify hybrid, and hence conflicting, restraints of trade across the wide spectrum of contexts in which the state and private parties interact. We attempt to offer that theory here, making no pretense that it is consistent with every judicial pronouncement on the issue. Rather, our theory springs from first principles of antitrust and state action immunity and is consistent with the most important and thoughtful opinions on the subject.

The doctrine of unilateral governmental restraints protects government regulation that neither enforces nor specifically facilitates private anticompetitive choices.⁸³ The antitrust laws were directed against

⁸² *Rice*, 458 U.S. at 665-66 (Stevens, J., concurring).

⁸³ The state may choose to adopt an anticompetitive policy suggested by private parties without creating a hybrid restraint. As long as the implementation of the restraint does not involve government support of anticompetitive private decisions made after the policy is adopted, the restraint is unilateral. And the private request for the anticompetitive state policy is separately protected from antitrust liability by the *Noerr-Pennington* doctrine. See *United Mine Workers v. Pennington*, 381 U.S. 657 (1965); *E. R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); see also *City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365, 379 (1991). In general, the *Noerr-*

the anticompetitive conduct of private market participants, not the exercise of coercive power by state and local governments that itself has anticompetitive consequences. Just as the “Sherman Act . . . gives no hint that it was intended to restrain state action or official action directed by a state,”⁸⁴ it gives no hint that it was intended to restrain any unilateral government exercise of coercive power that injures consumers.⁸⁵ A unilateral governmental restraint, therefore, is one in which public officials determine the nature and extent of the consumer injury, even though the decision is effectuated through the actions of private parties in compliance with the government’s mandates. These restraints need not be justified through the tests of state action immunity because they do not fundamentally conflict with antitrust. Tests developed to assure adequate controls on practices that do conflict with it are irrelevant. Thus, it does not matter whether the government is a sovereign actor or a subordinate body, and it does not matter whether the subordinate body has been specifically authorized by the sovereign to take the challenged action.⁸⁶

By contrast, a hybrid restraint is one in which the government empowers a private firm or firms to make choices, or to exercise discretion,⁸⁷ as to the nature or level of consumer injury. As the Court put it, the government in a hybrid restraint cedes to private actors “a degree of private regulatory power”⁸⁸ that results in a restraint of trade.⁸⁹ A

Pennington doctrine is a corollary to *Parker*. It would be “obviously peculiar in a democracy, and perhaps in derogation of the constitutional right ‘to petition the Government for a redress of grievances,’ to establish a category of lawful state action that citizens are not permitted to urge.” *Id.* at 370 (citation omitted). The *Noerr-Pennington* doctrine provides that the “federal antitrust laws . . . do not regulate the conduct of private individuals in seeking anticompetitive action from the government.” *Id.* at 379-80. Thus, it protects private combinations to obtain anticompetitive action from a governmental entity even if the entity refuses to take the action. Private actors, therefore, could be entitled to *Noerr-Pennington* immunity but not state action immunity.

84 *Parker v. Brown*, 317 U.S. 341, 351 (1943).

85 In a similar vein, the Court has held that a unilateral action of state government does not impose an impermissible burden on interstate commerce merely because it injures consumers. See *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 128 (1978).

86 Of course, it also does not matter whether private parties are actively supervised by the state. But when government action is properly classified as unilateral, the purpose of the supervision requirement would be fulfilled in any event. The fact that the relevant anticompetitive choices were made by the government would mean that supervision of private conduct is unnecessary.

87 See generally *Berkovitz v. United States*, 486 U.S. 531, 536 (1988) (“[C]onduct cannot be discretionary unless it involves an element of judgment or choice.”).

88 *Fisher v. City of Berkeley*, 475 U.S. 260, 268 (1986) (citing *Rice v. Norman Williams Co.*, 458 U.S. 654, 666 (1982) (Stevens, J., concurring)).

89 In a footnote in *Duffy*, the Court wrote that a “simple ‘minimum markup’ statute requiring retailers to charge 112 percent of their actual wholesale cost may satisfy the ‘active supervision’ requirement, and so be exempt from the antitrust laws under *Parker v. Brown*.” 324 *Liquor Corp. v. Duffy*, 479 U.S. 335, 344 n.6 (1987). Under our interpretation of *Fisher*, such a statute would involve a restraint unilaterally imposed by government, and so it would be beyond the reach of Section 1 without consideration of the state action doctrine. Most likely, the Court did not consider this basis for avoiding condemnation of the hypothetical statute. Some courts have suggested that, under the *Midcal* test, certain restraints are self-policing, so that the active supervision requirement is satisfied without continuing oversight. See, e.g., *Morgan v. Div. of Liquor Control*, 664 F.2d 353, 355

necessary condition for a hybrid restraint, therefore, is private discretion in the decision-making process that results in the anticompetitive effect. It is not a sufficient condition, however, for two reasons. First, private discretion is the hallmark of a private as well as a hybrid restraint. What separates the hybrid restraint is the participation of the government in a way that exceeds its normal role of establishing the preconditions for trade. Thus, private discretion and government participation are both necessary conditions for a hybrid restraint.⁹⁰

Second, the exercise of discretion by private parties must take the form of conduct closely analogous to a recognized antitrust offense. The antitrust laws were in general intended to promote consumer welfare by prohibiting private activities in the marketplace that reduce efficiency, or, stated otherwise, activities that reduce output and increase price. Practices are anticompetitive only if they are inefficient in this technical sense. Moreover, the laws recognize that efficiency in a dynamic sense increases through innovation. The catalyst for innovation is the prospect of monopoly profits; so antitrust does not oppose the acquisition of monopoly power through legitimate, efficient means.⁹¹ Nor does antitrust in general prohibit the full exploitation of monopoly power lawfully obtained; for the larger the expected reward from invention and hard competition, the greater the incentive to engage in practices that benefit consumers.⁹²

(2d Cir. 1981). The dicta in *Duffy* is consistent with this idea. In outcome, there is usually little difference between finding that a state restraint on competition is unilateral and finding that the restraint is clearly authorized by the state and self-enforcing. In both cases, the restraint avoids antitrust condemnation under Section 1. But the second approach ignores *Fisher*. Our definition of hybrid restraints is broadly consistent with the test one court suggested for determining when continuing supervision is required: “[A]ctive supervision is clearly necessary where private defendants are empowered with some type of discretionary authority in connection with anticompetitive acts (e.g., to determine price or rate structures).” *Zimomra v. Alamo Rent-A-Car, Inc.*, 111 F.3d 1495, 1499 (10th Cir. 1997).

⁹⁰ One could imagine a circumstance in which private parties would have successfully restrained trade without the assistance of government, but such assistance is provided anyway. We would call such a restraint hybrid, because it would be nearly impossible to determine that the government’s help was unnecessary. But even if the restraint were not termed hybrid, it would be private, and so the antitrust implications would be identical.

⁹¹ As the Court has noted:

It is not enough that a single firm appears to “restrain trade” unreasonably, for even a vigorous competitor may leave that impression. For instance, an efficient firm may capture unsatisfied customers from an inefficient rival, whose own ability to compete may suffer as a result. This is the rule of the marketplace and is precisely the sort of competition that promotes the consumer interests that the Sherman Act aims to foster. In part because it is sometimes difficult to distinguish robust competition from conduct with long-run anticompetitive effects, Congress authorized Sherman Act scrutiny of single firms only when they pose a danger of monopolization. Judging unilateral conduct in this manner reduces the risk that the antitrust laws will dampen the competitive zeal of a single aggressive competitor.

Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 767-68 (1984).

⁹² See *infra* Part V.

Further, as *Fisher* itself recognizes, Section 1 of the Sherman Act outlaws only “concerted” action, or agreements. The law recognizes that combinations among economic actors pose a special threat to consumer welfare, but the meaning of agreement, even in the context of purely private restraints, is notoriously complex. It is a term of art whose peculiar contours vary with the Court’s understanding of a particular restraint’s likely competitive effects.⁹³ In practice, antitrust analysis of private conduct has distinguished between horizontal agreements, or those among competitors, and vertical agreements, or those between firms at different distribution levels.⁹⁴ But a better way to understand the law is to distinguish between collusive and exclusionary anticompetitive arrangements.⁹⁵ Collusive arrangements produce anticompetitive effects solely through cooperation among the parties to them. The parties cooperate to limit competition among themselves, thereby reducing output, earning monopoly profits, and inflicting a deadweight loss on consumers.⁹⁶ By contrast, exclusionary practices work anticompetitive results through coercion of market participants outside the collusive group.⁹⁷ Such a practice forces a seller out of the market entirely or increases the costs of a seller that remains in the market. The loss or impairment of the seller has no antitrust significance in its own right, but it is important when consumers suffer because of a resulting reduction in output and increase in market price.⁹⁸ Moreover, antitrust law historically was prone to treat as exclusionary restraints that were neither exclusionary nor collusive, such as a tying arrangement in which a seller conditions the sale of one product on the purchase of another. These practices often did nothing more than

93 For example, the court in *Virginia Vermiculite, Ltd. v. Historic Green Springs, Inc.*, 307 F.3d 277 (4th Cir. 2002), observed that:

[C]ourts must treat the phrase “concerted action” as a term of art in the context of the Sherman Act; it cannot be understood as it might be in ordinary parlance, to reach any and all forms of joint activity by two or more persons. It must be defined consonant with its role in the antitrust analysis, as the basis for determining the unlawfulness of conduct prohibited by Section 1.

Id. at 281-82.

94 See *Bus. Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 730 (1988).

95 See BORK, *supra* note 1, at 134; POSNER, *supra* note 33, at 40.

96 See BORK, *supra* note 1, at 135-36.

97 POSNER, *supra* note 33, at 40.

98 The categories of collusive and exclusionary practices are not wholly separate. A boycott, for example, is both collusive, in that the participants cooperate with each other, and exclusionary, in that a non-participant is coerced. The arrangement is nevertheless an exclusionary practice at heart. See *id.* at 193. And a group of firms can contemporaneously engage in a collusive restraint and an exclusionary restraint, the latter serving to protect the former from erosion through the competition of a non-party. For example, the government alleged in *American Tobacco* that the major cigarette companies both needlessly bought cheap tobacco in order to exclude from the market the manufacturers of low-priced cigarettes and conspired to fix prices. See *Am. Tobacco Co. v. United States*, 328 U.S. 781, 803-04 (1946).

exploit the monopoly power that a single firm possessed without resort to exclusionary restraints.⁹⁹

Finally, antitrust law recognizes a domain of private exclusionary practices that involve neither horizontal nor vertical agreement. This is the apparent implication of Section 2 of the Sherman Act. Unless Section 2 is completely redundant,¹⁰⁰ it must outlaw acts of actual or attempted monopolization that do not constitute agreements within the meaning of Section 1. Legally, these are unilateral exclusionary acts used by a private monopolist to obtain or keep monopoly power. Of course, most practices a monopolist might use will in fact involve cooperation with another firm, albeit often a non-competitor. Monopolists do not often succeed by blowing up a rival's plant or committing fraud on the patent office, acts that could be called truly unilateral in that they involve no knowing cooperation between actors.¹⁰¹ Hence, important private exclusionary acts almost always involve some concert of action in the legal sense among private parties.

Although antitrust is broadly about preserving competition, therefore, it is more precisely about protecting competition from private practices that are demonstrably collusive or exclusionary. It is not a roving mandate to ferret out consumer injury from whatever source wherever it can be found. And historically, the law of antitrust developed in discrete doctrinal categories, such as exclusive dealing and tying, so that the practice at issue was slotted into the appropriate category and analyzed accordingly. Courts have attempted to identify hybrid restraints by comparing the arrangements at issue to recognized kinds of private anticompetitive practices, and with good reason. States frequently act in ways that arguably infringe on consumer interests; if consumer injury alone were enough to trigger state action immunity analysis, the scope of antitrust would be far broader than Congress ever imagined. Unless state or local government seeks to implement or facilitate private practices that restrict competition or practices much like them, there is no conflict with antitrust.

A review of the cases in which courts have addressed the issue indicate that two forms of hybrid restraints fall within the general definition: (1) the government enforces private arrangements that are

⁹⁹ See generally POSNER, *supra* note 33, at 197-202.

¹⁰⁰ Section 2 is unquestionably redundant to the extent that it prohibits conspiracies to monopolize, for a conspiracy to monopolize would almost always, if not always, constitute a conspiracy in restraint of trade prohibited by Section 1. See, e.g., *Fraser v. Major League Soccer, L.L.C.*, 284 F.3d 47, 67 (1st Cir. 2002) ("Conspiracy to monopolize claims are not often the subject of much attention, since almost any such claim could be proved more easily under section 1's ban on conspiracies in restraint of trade.")

¹⁰¹ See POSNER, *supra* note 33, at 259-60 (observing that most "exclusionary practices, though unilateral in the sense of not necessarily or typically involving cooperation between competitors, do require a contract, express or implied, with someone outside the firm engaging in the practice").

tantamount to antitrust violations; and (2) the government mandates or specifically authorizes particular, individual conduct by private firms that significantly facilitates the private exercise of market power, where the government directive serves no appreciable competitively-benign purpose. As we explain more fully below, the first category is typified by state mandates that permit sellers and buyers to agree on resale prices. The second category includes, for example, state law that purposely makes it easier for competitors to raise price above competitive levels without reaching an explicit agreement among themselves.

Our conception of the doctrine of hybrid and unilateral governmental restraints is consistent with most Supreme Court case law; but we make no claim that it is consistent with all of it. In particular, in *Community Communications Co. v. City of Boulder*,¹⁰² a case decided before *Fisher*, the city council enacted an emergency ordinance temporarily prohibiting an incumbent cable television operator from expanding service into new areas of the city while the council drafted a model ordinance to encourage competition in those areas.¹⁰³ The Court held that the city could be held liable for an antitrust violation because its action did not qualify for state action immunity; the home rule power granted the city under the state constitution was not a clear and affirmative state policy.¹⁰⁴ Though the Court never explicitly addressed the question of whether the restraint was hybrid, the Court's resolution implied that the moratorium ordinance conflicted with the antitrust laws. Under our analysis, however, it was a unilateral restraint imposed by government. We suspect that distinguishing clearly between the issue of antitrust conflict and immunity had not yet occurred to the Court.¹⁰⁵

102 455 U.S. 40 (1982).

103 *Id.* at 45-46.

104 *See id.* at 55.

105 Indeed, Judge Garland argues that *Fisher* represents the Court's effort to repudiate *Boulder* without explicitly overruling it. *See* Garland, *supra* note 12, at 503. But he goes on to criticize the rationale of *Fisher*, arguing that the existence of an agreement, which he recognizes is necessary for substantive Section 1 liability, was irrelevant because the plaintiffs did not allege an antitrust violation, but rather that the ordinance was preempted. *Id.* at 503-04. We disagree that a law can be preempted on its face when it does not mandate an arrangement that is tantamount to a violation. As we show below, *Midcal* and *Schwegmann*—cases Garland cites as involving statutes that were preempted despite the absence of illegal agreements—in fact involved arrangements that were analogous to per se illegal resale price maintenance. *See id.* at 505-06. Ultimately, Garland dismisses *Fisher*, concluding that it is exclusively “the two-pronged *Midcal* test that now effectively determines” whether a regulation is subject to Sherman Act attack. *Id.* at 507. But in the 15 years since he wrote, it has become clear that courts do indeed ask separately whether a restraint is hybrid. *See, e.g.*, A.D. Bedell Wholesale Co. v. Philip Morris Inc., 163 F.3d 239, 258 (3d Cir. 2001) (discussed *infra* at note 225 and accompanying text). And though we believe that the unilateral and hybrid restraints doctrine can be harmonized with the doctrine of state action immunity, the former is not superfluous. In particular, a unilateral act of a subordinate government body acting under general home rule authority would avoid preemption (and an adverse judgment on liability) under the unilateral restraint doctrine but would fail state action immunity for want of clear legislative authorization.

The Court understood the separate idea of antitrust conflict by the time it decided *City of Columbia v. Omni Outdoor Advertising, Inc.*,¹⁰⁶ however. This case was decided five years after *Fisher*, and centered on an ordinance that restricted “the size, location, and spacing of billboards.”¹⁰⁷ Under our approach and the logic of *Fisher*, the ordinance was a unilateral restraint imposed by government. Although the Court upheld the ordinance on the ground of state action immunity, it did not even consider whether it was a unilateral restraint.¹⁰⁸ While the Court’s failure to mention the unilateral restraint issue hints at a tension with our analysis, it seems most likely that the Court found the immunity issue easier to resolve or more important and so assumed that the restraint conflicted with antitrust.

Before turning to examples of hybrid restraints, we address in general terms the important issue of remedies. *Rice* holds that when a state or local government authorizes per se illegal anticompetitive conduct, the result is a hybrid restraint, and the government directive can be preempted in the abstract. If the government directive does not always result in anticompetitive conduct, the restraint can be condemned only on a case-by-case basis. In a given case, the private defendants could be enjoined from complying with a statute or ordinance that leads to anticompetitive conduct. Moreover, government officials could be enjoined from requiring the private defendants to comply with any mandatory directive. And they might even be enjoined from enforcing the mandate in a defined set of conditions where anticompetitive conduct would result, if that set of conditions can be identified. The Eleventh Amendment¹⁰⁹ would protect the state from damage liability,¹¹⁰ and the Local Government Antitrust Act¹¹¹ would shield subordinate governmental bodies from damages. But an injunction of the kind described, even if entered against a state as opposed to a local government official, would not run afoul of Eleventh Amendment.¹¹² Antitrust plaintiffs routinely obtain injunctive relief against state actors.¹¹³

106 499 U.S. 365 (1991).

107 *Id.* at 368.

108 The Court did consider whether an alleged conspiracy between the city council and a billboard company affected antitrust liability. But the conspiracy under the Court’s analysis related to state action immunity under *Parker*, not to the potential inference that the restraint was hybrid. *See id.* at 370-79.

109 U.S. CONST. amend. XI.

110 In *Seminole Tribe v. Florida*, 517 U.S. 44 (1996), the Court held that Congress acting under its Commerce Clause power cannot abrogate the sovereign immunity guaranteed a state by the Eleventh Amendment by authorizing private parties to bring suit against a state in federal court. This constraint on congressional power clearly applies to the federal antitrust laws, *see id.* at 72 n.16, and it would bar an action for damages that would be satisfied from a state treasury, *see, e.g., Earles v. State Bd. of Certified Pub. Accountants*, 139 F.3d 1033, 1038 (5th Cir. 1998).

111 15 U.S.C. § 34.

112 *See, e.g., Ex parte Young*, 209 U.S. 123 (1908). *Seminole Tribe* does not abrogate the rule of *Ex parte Young* that “an individual can bring suit against a state officer in order to ensure that

A more troubling prospect is holding private defendants liable for treble damages when they act with the assistance of the state. But the implication of state action analysis is that any hybrid restraint that violates the antitrust laws and fails the tests for immunity leaves private parties exposed to the whole panoply of antitrust remedies. The lesson is that private parties who restrain trade pursuant to government directives do so at their peril.

III. Hybrid Restraints and Vertical Restrictions

As we have explained, to characterize a government-supported restraint as hybrid, a court must analogize it to a private restraint. Private restraints have historically been classified as vertical or horizontal. Vertical restraints, in turn, have been divided between price and non-price restraints. Vertical minimum price agreements are per se illegal, whereas vertical non-price and maximum price agreements are judged under the rule of reason. As we explain below, the economic basis for the distinction between minimum price and other kinds of vertical restrictions is tenuous, but the per se illegality of minimum resale price maintenance has been a critical backdrop to the development of the hybrid restraint doctrine. The Supreme Court has explicitly applied the term hybrid restraint to state-supported resale price maintenance more than to any other recognized category of private antitrust offense.¹¹⁴ Where states have sponsored restraints that mimic private resale price maintenance, with an apparent intent to circumvent antitrust strictures, the Court could scarcely avoid the issue of whether a conflict existed.

We begin the elaboration of our theory of unilateral and hybrid restraints, therefore, with an examination of distributional restraints. We

the officer's conduct is in compliance with federal law." *Seminole Tribe*, 517 U.S. at 71 n.14; see also *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 204 (4th Cir. 2001) ("Although recent Supreme Court cases have added muscle to the constitutional principle of state immunity from litigation, the Court has not questioned the continuing validity of the *Young* exception."). The scope of *Ex parte Young* was questioned in *Idaho v. Coeur d'Alene Tribe*, 521 U.S. 261 (1997), but the Court explicitly noted that "where prospective relief is sought against individual state officers in a federal forum based on a federal right, the Eleventh Amendment, in most cases, is not a bar." *Id.* at 276-77. "Thus, if state officials were violating the Sherman Act, in principle the Eleventh Amendment would not bar injunctive relief against them." *Neo Gen Screening, Inc. v. New England Newborn Screening Program*, 187 F.3d 24, 28 (1st Cir. 1999).

113 See, e.g., *TFWS*, 242 F.3d at 204; *McNeilus Truck & Mfg., Inc. v. Ohio*, 226 F.3d 429, 437 (6th Cir. 2000); *Neo Gen Screening*, 187 F.3d at 28; *PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179, 1190-91 (C.D. Cal. 2000) (holding that a request for an injunction that would deprive the state of a continuing stream of income was nevertheless a claim for prospective relief and therefore permissible under *Ex parte Young*).

114 In *Fisher*, the Court cited as examples of hybrid restraints the resale price maintenance schemes at issue in *Schwegmann* and *Midcal*. *Fisher v. City of Berkeley*, 475 U.S. 260, 268 (1986). The Court later described as hybrid the resale price maintenance scheme under consideration in *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345 n.8 (1987).

first examine state-supported resale price maintenance—arrangements that would be illegal *per se* if they were private. Our conclusion is that courts are willing to declare a restraint hybrid so long as the arrangement bears some factual resemblance to its private counterpart, even if there is little economic justification for condemnation. Such is the power of the *per se* rule against vertical minimum price fixing. We then turn briefly to non-price distributional restraints. Few cases have raised the issue of hybrid versus unilateral restraints in this context, and so our discussion is general. Because antitrust has not displayed the same hostility toward non-price restraints that it has toward price restraints, courts have had an easier time reserving the hybrid designation for those non-price distributional restraints that do in fact constitute public support of private anticompetitive choices.

A. *Resale Price Maintenance*

Resale price maintenance is an antitrust puzzle. An agreement among competitors to impose resale price floors on their customers or an agreement among retailers to persuade their suppliers to impose price floors on them would constitute horizontal price fixing, which would be *per se* illegal regardless of the vertical aspects of the arrangement. The horizontal agreement in either context could be inferred from circumstantial evidence. But a minimum resale price agreement between a single supplier and retailer is also illegal,¹¹⁵ even though, by itself, it typically causes no demonstrable harm to competition.¹¹⁶ At one time, the Court believed that resale price restrictions imposed by a single manufacturer for its own interests had the same anticompetitive effects as a dealers' cartel¹¹⁷ and so merited *per se* treatment. Even though that view has long since been discredited, the *per se* illegality of resale price maintenance remains.¹¹⁸

Mitigating the overbreadth of the *per se* rule, however, the Court has narrowed the definition of the agreement necessary to find resale price maintenance. The *Colgate* doctrine states that when a supplier announces that it will sell only to retailers that adhere to specified minimum resale

115 See *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911). By contrast, a vertical agreement as to *maximum* resale prices is not illegal *per se*, though in theory it could violate the antitrust laws under the rule of reason. See *State Oil Co. v. Khan*, 522 U.S. 3, 22 (1997).

116 For a survey of theories of resale price maintenance and an empirical study of resale price maintenance cases, see Pauline M. Ippolito, *Resale Price Maintenance: Empirical Evidence from Litigation*, 34 J.L. & ECON. 263 (1991).

117 See *Dr. Miles Med. Co.*, 220 U.S. at 408.

118 Although vertical minimum price agreements are illegal *per se*, vertical non-price restrictions, even if agreed to explicitly by the parties, are illegal only if unreasonable. See *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 59 (1977). In cases of non-price distributional restraints, the issue is rarely whether an agreement exists, but whether the agreement is unreasonable.

prices, and a retailer thereafter buys the product and adheres to the price restriction, no antitrust agreement is formed, even though the arrangement could comfortably be called an agreement within the law of contracts.¹¹⁹ Yet the boundaries of the *Colgate* doctrine are notoriously hazy. An agreement is formed if a supplier announces that it will refuse to sell to any wholesaler that sells to retailers who fail to adhere to suggested minimum resale prices.¹²⁰ And one is formed if a supplier obtains acquiescence in a resale price maintenance system by persuading retailers to adhere to the suggested prices.¹²¹ But an agreement on resale prices cannot be inferred from an agreement between a supplier and a retailer that the supplier will cut off a price-cutting competitor of the retailer.¹²² Notably, nothing in the logic of *Colgate* turns on whether or not the supplier has economic leverage with respect to the retailer. A retailer may acquiesce in his supplier's announced resale price maintenance policy out of fear of the consequences of termination, but acquiescence does not create an agreement. As the Court later bluntly stated in *Monsanto*, "a distributor is free to acquiesce in the manufacturer's [resale price] demand in order to avoid termination" without thereby exceeding the bounds of *Colgate*.¹²³ This tortured history of the *Colgate* doctrine betrays an uneasiness with the per se treatment of resale price maintenance.

The *Monsanto* Court offered general guidance on the meaning of agreement in the context of vertical price fixing. It suggested that an agreement arises if "the manufacturer and others had a conscious commitment to a common scheme designed to achieve an unlawful objective."¹²⁴ The Court went on to explain that an agreement in a case alleging termination of a distributor pursuant to illegal vertical price fixing "includes more than a showing that the distributor conformed to the suggested price. It means as well that evidence must be presented both that the distributor communicated its acquiescence or agreement, and that this was sought by the manufacturer."¹²⁵ To establish an agreement, the plaintiff must offer evidence that tends to exclude the possibility that the parties acted independently.

In each of the cases in which the Court has invalidated a state-supported restraint as hybrid, it has done so at least partially on the ground that the restraint amounted to resale price maintenance. In *Midcal*, for example, the Court observed that "California's system for wine pricing plainly constitute[d] resale price maintenance in violation of the Sherman

119 See *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919).

120 See *United States v. Parke, Davis & Co.*, 362 U.S. 29, 45 (1960).

121 See *id.* at 46.

122 See *Bus. Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 731 (1988).

123 *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984).

124 *Id.* at 764 (internal quotation marks omitted).

125 *Id.* at 764 n.9.

State Action and Hybrid Restraints

Act.”¹²⁶ The Court characterized the restraint in *Schwegmann* as “blanketing a state with resale price fixing”¹²⁷ and the restraint in *Duffy* as “[m]andatory industrywide resale price fixing.”¹²⁸ As one court has recently observed:

[All three cases involve] schemes [that] were structured to allow one party (manufacturer or wholesaler) to set the resale prices to be charged by purchasers at the next [level]. The resemblance to traditional private resale price maintenance . . . was so close that the Supreme Court treated the arrangements as if they were nothing more than private resale price maintenance schemes licensed and abetted by the state.¹²⁹

In contrast, the regulations of liquor distribution that the Court has upheld were insufficiently analogous to resale price maintenance. The designation statute in *Rice* also gave distillers the power to control their purchasers, but only by limiting customers rather than by setting prices.¹³⁰ Vertical nonprice restraints are not per se illegal but are judged under the rule of reason.¹³¹ Similarly, the price filing and most-favored-nation affirmations in *Hostetter* bore only a “speculative” connection to possible antitrust violations, and so the scheme could not be condemned on its face.¹³²

On closer scrutiny, however, the nature of the analogy of the restraints in *Midcal*, *Schwegmann*, and *Duffy* to resale price maintenance is far from clear. Resale price maintenance is illegal only when the parties agree to it. The Court characterized the statutory scheme in *Midcal* as resale price maintenance because “[t]he wine producer holds the power to prevent price competition by *dictating* the prices charged by wholesalers.”¹³³ But under the *Colgate* doctrine, where a manufacturer dictates a price that a distributor must follow, there is no agreement. *Colgate* allows sellers to announce the conditions under which they will continue to deal with buyers; if the seller does so and the distributor merely complies, there is no agreement.¹³⁴ Nor does the fact that the state compels compliance supply the element of agreement. *Fisher* holds that compliance with a state-imposed price requirement does not entail an

126 Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc., 445 U.S. 97, 103 (1980).

127 *Schwegmann Bros. v. Distillers Corp.*, 341 U.S. 384, 390 (1990).

128 *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 342 (1987).

129 *Mass. Food Ass’n v. Mass. Alcoholic Beverages Control Comm’n*, 197 F.3d 560, 565 (1st Cir. 1999).

130 See *Rice v. Norman Williams*, 458 U.S. 654, 661-62 (1982).

131 *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 44 (1977).

132 See *Joseph E. Seagram & Sons, Inc. v. Hostetter*, 384 U.S. 35, 45-46 (1966).

133 *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 103 (1980) (emphasis added).

134 See *United States v. Colgate & Co.*, 250 U.S. 300, 300-07 (1919).

agreement with the entity that imposes it;¹³⁵ why legally mandated compliance with a privately determined price constitutes an agreement with a private entity is not obvious. There is no “meeting of the minds” in *Midcal* any more than in *Fisher*.

The scheme in *Schwegmann* involved an agreement between the distiller and at least one distributor. But that agreement by itself was valid (at the time) under the Miller-Tydings Act. What brought the arrangement into conflict with the Sherman Act was its application of the price to nonsigners, who by definition did not agree to the price. As the Court wrote:

[W]hen a state compels retailers to follow a parallel price policy, it demands private conduct which the Sherman Act forbids. Elimination of price competition at the retail level may, of course, lawfully result if a distributor successfully negotiates individual “vertical” agreements with all his retailers. But when retailers are *forced* to abandon price competition, they are driven into a compact in violation of the spirit of the proviso which forbids “horizontal” price fixing. A real sanction can be given the prohibitions of the proviso only if the price maintenance power granted a distributor is limited to voluntary engagements.¹³⁶

The Court went on to add that “[c]ontracts or agreements convey the idea of a cooperative arrangement, not a program whereby recalcitrants are dragged in by the heels and compelled to submit to price fixing.”¹³⁷ Thus, the Court understood that, from the nonsigners’ perspective, the arrangement was a legally imposed price. But it was a legally imposed price only in the sense that if the nonsigner remained a distributor, legal sanctions could be brought to bear on him if he did not adhere to the price. Under *Colgate*, a supplier can refuse to deal with a distributor that does not adhere to a specified resale price, and the law will support that decision.¹³⁸ Either way, the supplier has a lawful method of inducing the reluctant dealer to adhere to the set resale price, and it is not clear that the method approved of by the state in *Schwegmann* would have resulted in any greater compliance.¹³⁹ So the restraint was illegal in *Schwegmann*

135 See *Fisher v. City of Berkeley*, 475 U.S. 260, 267 (1986).

136 341 U.S. at 389 (citation omitted).

137 *Id.* at 390.

138 See *Colgate*, 250 U.S. at 307.

139 Justice Stevens addressed a similar point in *Rice*. Apart from the California designation statute, if a wholesaler refused to accept a customer restriction demanded by the distiller, the distiller could lawfully refuse to trade with the wholesaler. If the distiller has sufficient market power, the wholesaler will accede to the demand. But, according to Justice Stevens, it is “possible that, absent the state laws, the distillers would have insufficient market power to obtain and enforce such agreements. The designation statute therefore may give the distillers more power over California importers than was taken away by the Oklahoma laws.” *Rice v. Norman Williams Co.*, 458 U.S. 654, 668 (Stevens, J.,

precisely because it was not an agreement; yet under *Colgate*, resale price maintenance is illegal only when there is an agreement. The Court condemned the scheme anyway because it conflicted with “the spirit of” the Sherman Act.¹⁴⁰

It is still less clear what the relevant agreement was in *Duffy*. Recall that the state in that case prescribed a twelve percent markup for retailers over prices posted by wholesalers, but it effectively permitted wholesalers to increase the margin by selling below posted prices and by raising the posted prices to which retail prices were keyed after wholesale purchase but before resale.¹⁴¹ One federal appellate judge has suggested that this arrangement involved “a degree of private regulatory power” but not the power “independently to set prices *via an agreement*.”¹⁴² Consequently, he maintained, the Court “misunderstood its own precedents” in *Duffy*, because that case involved “classic unilateral state action.”¹⁴³ The judge was correct to point out that there was no conventional agreement in *Duffy*; but, as we have just seen, that feature of the scheme does not distinguish the case from the Supreme Court’s earlier hybrid restraint precedents.

Thus, if the arrangements in *Schwegmann*, *Midcal*, and *Duffy* are unlawful because of their similarity to resale price maintenance, it is not because they involve the sort of agreement a court would require in the context of private resale price maintenance. The presence of a government enforcement mechanism for a private choice of a price term was sufficient for the Court to find that the arrangement was functionally equivalent to the private offense of resale price maintenance. This result can only follow if the definition of agreement in the context of hybrid restraints differs from the definition of agreement in the contexts of private restraints and purely governmental restraints.

The Court’s adaptations of the definition of concerted action when applied to hybrid restraints are a testament to the strange antitrust status of private resale price maintenance. When viewed purely as a vertical

concurring). But again, it is not clear that the statutes change the outcome. If California importers would have had sufficient power to resist a demand for a distributional restraint, they presumably would have had sufficient power to insist that their preferred suppliers be “designated” pursuant to the California statute.

140 See *Colgate*, 250 U.S. at 307.

141 See *supra* note 74-75 and accompanying text.

142 *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 214 (4th Cir. 2001) (Luttig, J., concurring) (internal quotation marks omitted).

143 *Id.* at 213-14. In *TFWS*, discussed *infra* at notes 212-223 and accompanying text, the Fourth Circuit struck down under the Sherman Act a Maryland liquor control system that required liquor wholesalers to post their prices and adhere to them for at least a month and prohibited wholesalers from granting volume discounts. The court remanded for reconsideration of whether the Twenty-first Amendment barred application of the Sherman Act. *Id.* at 213. The court held that the regulatory scheme was a hybrid restraint. Judge Luttig found that the scheme was indistinguishable from the restraint in *Duffy*, and so he believed that the court was bound to follow *Duffy* and declare the system hybrid even though that case was wrongly decided.

phenomenon, that is, apart from horizontal competitive implications, resale price maintenance remains per se illegal despite the lack of a coherent economic basis for such treatment. In the private context, the *Colgate* doctrine, even with its limitations, serves as a check on the economic mischief that per se illegality can do. But it does so by blunting the impact of a rule that many want passionately to preserve.¹⁴⁴ State-supported vertical price restraints can be called concerted action, and hence subject to per se condemnation, because the logic of *Colgate* is so weak. To be sure, state-supported resale price maintenance schemes may authorize explicit vertical price *agreements*, which would not be protected under *Colgate* in any event. And the ability of a supplier to bring legal sanctions to bear on a dealer who does not adhere to set resale prices is not identical to the power a supplier has to enforce suggested resale prices by refusing to trade with a dealer. These are differences in form that provide a convenient basis for distinguishing hybrid resale price maintenance from unilateral private action. But they are not differences in economic substance. The designation of state-supported vertical price restraints as hybrid is the triumph of *Dr. Miles* over *Colgate*. Below, we suggest that state-supported resale price maintenance can appropriately be treated as hybrid because of its horizontal implications. But we are not convinced that the Court's treatment is based on those implications.

The upshot of the Supreme Court's cases drawing the elusive line between hybrid and unilateral restraints is that a restraint is hybrid if it is sufficiently analogous to an antitrust violation, even if it does not meet the technical requirements of the private offense. A state-supported restraint may even be invalid if it merely violates the spirit of the general prohibition. This process of analogy involves taking into account the policies of the substantive categories of antitrust themselves, even when they may be unconvincing from an economic perspective, and an awareness of the nature of governmental action. In light of those policies, state implementation of a private choice concerning resale prices is functionally equivalent to a private vertical agreement on price or price levels.¹⁴⁵

144 See, e.g., BORK, *supra* note 1, at xiii (noting that an influential political group favors the rule of per se illegality of resale price maintenance).

145 This view of hybrid restraints helps explain *Fisher's* characterization of state-imposed rent controls as unilateral or governmental and, therefore, valid. So long as the government itself determines the rents, the restraint cannot be hybrid, because it cannot plausibly be analogized to a private cartel. The separate motivations of regulators, whatever they may be, are different from those of self-interested landlords. Although we certainly cannot attribute a public-interest motivation to rent control, we can rule out any suggestion that it is enacted to provide enforcement of landlords' preferences. Whatever the goals of rent control, its mechanisms are in no way analogous to a private cartel.

B. *Non-price Distributional Restraints*

If a firm were to impose by contract a non-price distributional restriction, the restraint would be private. A state would remain free to enforce the contract, so long as the restraint did not overstep the requirements of the rule of reason in a particular case. But any attempt by a state to enforce a private restraint that violates the antitrust laws would render the restraint hybrid. As a practical matter, the state's effort, through its courts, to enforce an unreasonable restraint would be preempted.

The picture changes somewhat if a state specifically authorizes or mandates particular non-price distributional restraints. Unless these restraints will predictably have anticompetitive effects in nearly all applications by facilitating tacit collusion—a subject we consider below—they presumably could have anticompetitive effects in some circumstances but not others. As *Rice* teaches, such a governmental directive cannot be preempted in the abstract. But it could be preempted in its application, if the statutory authority is used to produce anticompetitive effects and does not qualify for state action immunity. Here, the discretion granted to private parties enforced by the government creates a hybrid restraint when the discretion is used to produce anticompetitive effects. In *Rice*, therefore, an antitrust court could appropriately strike down as hybrid a private implementation of the California designation statute that had anticompetitive consequences. Not every use of the discretion specifically contemplated by the statute to designate wholesalers will have anticompetitive effects. In fact, as the *Rice* Court pointed out, the statute did not *require* the distiller to impose vertical restraints of any kind; the distiller had the discretion *not* to impose restraints.¹⁴⁶

State law may, however, impose anticompetitive distributional restraints without enforcing private discretion. In *Massachusetts Food Association v. Massachusetts Alcoholic Beverages Control Commission*,¹⁴⁷ state law provided that “no one can own more than three retail liquor stores” in the state.¹⁴⁸ We consider below the possibility that the law might lead to anticompetitive effects through tacit collusion.¹⁴⁹ But to the extent that any anticompetitive effects were purely vertical, those effects were produced by compliance with the law itself, not by the exercise of private

¹⁴⁶ See *Rice v. Norman Williams Co.*, 458 U.S. 654, 662 (1982).

¹⁴⁷ 197 F.3d 560 (1st Cir. 1999).

¹⁴⁸ *Id.* at 562. Ironically, the Supreme Court in *Rice*, in an effort to emphasize the lack of anticompetitive potential of the California designation statute, noted that the law did not limit the “number of importers which may be designated by the distiller.” *Rice*, 458 U.S. at 662. The Massachusetts scheme did indeed limit the number of retail outlets a single dealer could own. But the dictum in *Rice* was intended to show that the restriction at issue was even less suspect than it might have been, not that a restriction on the number of distributors would be invalid under the antitrust laws.

¹⁴⁹ See *infra* Section IV.A.

discretion. Writing for the First Circuit, Judge Boudin aptly described hybrid restraints as “state licensing of arrangements between private parties that suppress competition—not state directives that *by themselves* limit or reduce competition.”¹⁵⁰ Private “arrangements” imply the kind of discretion to inflict consumer injury that is a necessary condition of a hybrid restraint, as we define it. The restraint at issue, according to the court, was unilateral action because “the state has not ordered or authorized private parties to engage in conduct that, absent immunity, would even arguably violate the antitrust laws; there is no private agreement or arrangement between retailers as to the number of retail outlets and therefore no violation to be shielded.”¹⁵¹ The court properly rejected the argument that the “statute is preempted because it produces an *effect* that could not be produced by agreement of private parties without violating the antitrust laws,”¹⁵² reasoning that “much [legitimate] direct government regulation prohibiting one form of economic activity or requiring another involves directives that private parties could not themselves implement without violating the antitrust laws.”¹⁵³

IV. Hybrid Restraints and Tacit Collusion

To this point, we have emphasized the Supreme Court’s decisions on hybrid restraints, which have (not coincidentally) involved state-imposed vertical restraints in the distribution of alcoholic beverages. The stage is now set for consideration of state-sponsored horizontal restraints. Some applications of the concept of hybrid restraints are straightforward. Express, horizontal price fixing has been per se illegal from the earliest years of the Sherman Act.¹⁵⁴ Under the logic of *Midcal*, a state regulatory scheme that authorizes insurers¹⁵⁵ or truckers¹⁵⁶ jointly to establish rates is a hybrid restraint because it gives private firms the power to exercise discretion in a way that reduces consumer welfare.¹⁵⁷ Such a restraint is

150 *Mass. Food Ass’n*, 197 F.3d at 565.

151 *Id.* at 562.

152 *Id.* at 564.

153 *Id.* at 564-65.

154 *See* *United States v. Joint Traffic Ass’n*, 171 U.S. 505 (1898); *United States v. Trans-Missouri Freight Ass’n*, 166 U.S. 290 (1897).

155 *See* *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621 (1992) (holding state regulatory program authorizing joint rate-making by title insurance companies was not immune under the state action doctrine because of a lack of active supervision).

156 *See* *S. Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48 (1985) (holding a state regulatory program authorizing joint rate-making by trucking companies immune under the state action doctrine).

157 *See also* *Patrick v. Burget*, 486 U.S. 94 (1988) (denying immunity to peer review system controlled by private physicians). Similarly, if a state allowed a single competitor to choose a price, and ordered all other competitors to charge the price selected, the regulation would amount to authorization of an explicit price fixing arrangement. *See* *Garland*, *supra* note 12, at 506 (posing a

invalid, unless the state as sovereign adopts the policy to restrict competition and reasserts its control by active supervision of the prices, thereby satisfying the requirements of state action immunity: “Actual state involvement, not deference to private price fixing arrangements under the general auspices of state law, is the precondition for immunity from federal law.”¹⁵⁸ Deference to private price fixing is thus a hybrid restraint.

Indeed, *Midcal* and *Schwegmann* both involved privately determined resale prices that were binding on all retailers. In both contexts, the Court characterized the arrangement as tantamount not only to resale price maintenance, as we saw in the last part, but to horizontal price fixing. In *Schwegmann*, for example, the Court wrote that “when retailers are forced to abandon price competition, they are driven into a compact in violation of the spirit of the proviso [of the Miller-Tydings Act] which forbids ‘horizontal’ price fixing.”¹⁵⁹ And *Duffy* interpreted *Midcal* as “involv[ing] horizontal as well as vertical price fixing,” because “the wholesalers . . . were required to adhere to a single fair trade contract or price schedule for each geographical area.”¹⁶⁰ A state law that is tantamount to express price fixing is invalid, unless it satisfies the requirements of state-action immunity, that is, clear articulation and active supervision.

But what if the law merely facilitates tacit collusion? Certainly, in that circumstance, any express collusion by firms subject to the statute would run afoul of Section 1 as a private restraint and, for want of state supervision, would not be immune.¹⁶¹ We argue, however, that in some circumstances, state-sponsored facilitating practices can amount to hybrid restraints that expose private actors to potential damages liability and are subject to an injunction against enforcement in a suit against the appropriate public officer. In these cases, private discretion, which lies at the heart of any hybrid restraint, is not the discretion to engage in the facilitating practice; the statute may unambiguously compel private actors

similar hypothetical). There is no question that the restraint would be hybrid.

158 *Ticor*, 504 U.S. at 633.

159 *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384, 389 (1951).

160 *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 342 (1987).

161 In *McNeilus Truck & Mfg., Inc. v. Ohio*, 226 F.3d 429 (6th Cir. 2000), the state enacted a statute that required an out-of-state truck remanufacturer selling from an office in Ohio to obtain agreements from nearby chassis dealers that they would provide warranty service to the customers of the remanufacturer. The dealers, who were competitors of the remanufacturer, refused to enter into such agreements, thereby allegedly excluding the remanufacturer from the market, but the remanufacturer sued state and county officials, not the dealers. In an obtuse opinion, the court correctly held that the statute was not preempted under *Rice* because it did not mandate conduct that in all cases would violate the Sherman Act. *Id.* at 441. The court also correctly observed that the statute may “facilitate[] . . . coordinated action . . . by dealers in refusing to enter binding agreements,” and the remanufacturer might then sue the dealers under the antitrust laws. *Id.* But in such a case, the statute would not “facilitate” joint exclusionary behavior in the way that post-and-hold regulations facilitate tacit collusion. The proper conclusion would be that a concerted refusal to deny the remanufacturer the agreements required by law is a *private* restraint, not a unilateral or a hybrid restraint.

to engage in the precise conduct that facilitates tacit collusion. Rather, private discretion inheres in the private collusion that compliance with the statute predictably enables. This collusion, not the conduct required by the statute, is the source of the anticompetitive injury.

This idea is also implicit, to some degree, in the Supreme Court's hybrid restraint cases that address resale price maintenance. As the Court in *Duffy* observed:

We have noted that industrywide resale price maintenance also may facilitate cartelization. Mandatory industrywide resale price fixing is virtually certain to reduce interbrand competition as well as intrabrand competition, because it prevents manufacturers and wholesalers from allowing or requiring retail price competition. The New York statute specifically forbids retailers to reduce the minimum prices set by wholesalers.¹⁶²

Thus, the Court has recognized that one reason for invalidating state law is that it facilitates cartelization. But resale price maintenance is only one of a range of possible facilitating practices. We begin by setting out the law's treatment of facilitating practices in the context of purely private restraints. We then examine how the lower federal courts have made use of the concept in analyzing hybrid restraints.

A. *Tacit Collusion in Antitrust Law*

As Judge Richard Posner recently noted:

[Section 1's language is] broad enough . . . to encompass a purely tacit agreement to fix prices, that is, an agreement made without any actual communication among the parties to the agreement. If a firm raises price in the expectation that its competitors will do likewise, and they do, the firm's behavior can be conceptualized as the offer of a unilateral contract that the offerees accept by raising their prices. Or as the creation of a contract implied in fact.¹⁶³

This observation echoes Posner's long-held belief, supported by elaborate argument, that the law should use economic evidence to challenge tacit

¹⁶² *Duffy*, 379 U.S. at 342 (citation omitted).

¹⁶³ *In re High Fructose Corn Syrup Antitrust Litig.*, 295 F.3d 651, 654 (7th Cir. 2002). The passage recognizes the standard principle of contract law that acceptance of an offer in proper circumstances may be inferred from performance. See E. ALLAN FARNSWORTH, *CONTRACTS* 148 (3d ed. 1999).

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collusion under Section 1.¹⁶⁴ But as Judge Posner himself recognizes, courts have not (yet) adopted this view, at least not universally.¹⁶⁵ The law does not, of course, require a formal agreement.¹⁶⁶ Rivals can agree by uniformly complying with an express proposal of an anticompetitive scheme.¹⁶⁷ Moreover, in many cases, an explicit agreement can be inferred from uniform behavior when the conduct of the parties almost certainly would have varied had the parties been acting independently.¹⁶⁸ For example, if sellers submit identical bids on specialized, complex products, an explicit agreement may be inferred, if other evidence does not explain the parallelism.¹⁶⁹ In some cases, an actual agreement might be inferred from circumstantial evidence even if the competitors never directly communicated with each other.¹⁷⁰ Though communication of some kind is indispensable to agreement, the parties can communicate through an intermediary.¹⁷¹ Cases in which explicit agreements can only be proven

164 Judge Posner has set out his views in a systematic way most recently in *Antitrust Law*, POSNER, *supra* note 33, at 51-100. But he offered a similar analysis as early as 1969 in Richard A. Posner, *Oligopoly and the Antitrust Laws: A Suggested Approach*, 21 STAN. L. REV. 1562 (1969) [hereinafter Posner, *Oligopoly*].

165 See *High Fructose Corn Syrup*, 295 F.3d at 654 (Posner, J.) (“[I]t is generally believed . . . that an express, manifested agreement, and thus an agreement involving actual, verbalized communication, must be proved in order for a price-fixing conspiracy to be actionable under the Sherman Act.”).

166 *American Tobacco Co. v. United States*, 328 U.S. 781, 809 (1946) (“No formal agreement is necessary to constitute an unlawful conspiracy.”).

167 In *Interstate Circuit, Inc. v. United States*, 306 U.S. 208 (1939), the Court observed: It is elementary that an unlawful conspiracy may be and often is formed without *simultaneous* action or agreement on the part of the conspirators. Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act.

Id. at 227 (citations omitted) (emphasis added). Though *Interstate Circuit* was a case of collusive exclusion, not pure collusion, the principal is general. A stark example of an invitation to collude is provided in *United States v. American Airlines, Inc.*, 743 F.2d 1114 (5th Cir. 1984). The president of American Airlines, one of the two major air carriers operating out of Dallas-Fort Worth, in a phone call with the president of Braniff, the other major carrier, said, “Raise your god-damn fares twenty percent. I’ll raise mine the next morning.” *Id.* at 1116. The Braniff president neither gave verbal assent nor raised his fares. But the court unquestionably would have found an agreement had the Braniff president done either.

168 An agreement among competitors to divide territories or customers could be inferred from conduct alone where economic conditions imply that the firms would be competing in the absence of an agreement.

169 See Donald F. Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 HARV. L. REV. 655, 660 (1962). Similarly, an actual agreement can be inferred if a large number of sellers in a market maintain the same price despite a decline in demand leaving them operating at sixty percent capacity. *Id.* at 659.

170 The Court once observed, “As is usual in cases of alleged unlawful agreements to restrain commerce, the Government is without the aid of direct testimony that the distributors entered into any agreement with each other In order to establish agreement it is compelled to rely on inferences drawn from the course of conduct of the alleged conspirators.” *Interstate Circuit*, 306 U.S. at 221.

171 *Interstate Circuit* may be a case in which mutual assent was communicated through an intermediary, though the case involved essentially an exclusionary practice, not a purely collusive restraint. The Court inferred an agreement among film distributors to accede to the demands of an

indirectly pose an evidentiary challenge for the law,¹⁷² but they do not strain the concept of agreement.

By contrast, if competitors are able to raise price to supra-competitive levels without overt communication or explicit agreement simply by taking each other's anticipated reactions into account in setting price, the nature of an antitrust agreement is called into question. If an agreement is found to exist, it will have to be inferred from circumstantial evidence, especially evidence of parallel pricing conduct. But the more difficult issue is whether the interaction of competitors in such a case constitutes an "agreement" at all. This situation is the now-familiar problem of tacit collusion, or oligopolistic interdependence, that has long vexed antitrust law.¹⁷³

The policy debate is illustrated by the divergent views of Posner and Donald Turner. Turner concluded years ago that, "while there are arguable grounds for saying there is no agreement" when oligopolists simply take into account the probable reactions of competitors in setting their basic prices, "there are far better grounds for saying that . . . it is not *unlawful* agreement."¹⁷⁴ Turner rests his position first on the premise that an oligopolist is acting rationally and in precisely the same way as a firm in a competitive market,¹⁷⁵ and it would simply be unjust to punish firms for acting rationally and in the same way that other firms act with impunity.¹⁷⁶ But Turner's second and decisive argument is that no court could impose a sensible and appropriate remedy on the oligopolists.¹⁷⁷ An injunction

exhibitor to impose restrictions on other exhibitors. The Court relied in part on evidence that the exhibitor made his demands in a letter that "named on its face as addressees the eight local representatives of the distributors, and so from the beginning each of the distributors knew that the proposals were under consideration by the others." *Id.* at 222. As the facts of this case suggest, the intermediary can be a supplier or customer, so a horizontal agreement can have a vertical aspect. *See also* *United States v. Masonite Corp.*, 316 U.S. 265, 275 (1942) (holding that a horizontal agreement can be formed through a series of vertical agreements where parties at one level are aware that their competitors are entering into the same kind of agreement).

172 *See* *Brown v. Pro Football, Inc.*, 518 U.S. 231, 241 (1996) ("Antitrust law . . . sometimes permits judges or juries to premise antitrust liability upon little more than uniform behavior among competitors, *preceded by conversations* implying that later uniformity might prove desirable or accompanied by *other conduct* that in context suggests that each competitor failed to make an independent decision.") (emphasis added) (citations omitted).

173 *See generally* John E. Lopatka, *Solving the Oligopoly Problem: Turner's Try*, 41 ANTITRUST BULL. 843 (1996).

174 Turner, *supra* note 169, at 671 (emphasis added).

175 *Id.* at 665 ("The rational oligopolist simply takes one more factor into account—the reactions of his competitors to any price change he makes.")

176 *Id.* at 666 (observing that "it seems questionable to call the behavior of oligopolists in setting their prices unlawful when the behavior in essence is identical to that of sellers in a competitive industry"). This interpretation is bolstered by Turner's further argument that the oligopolists are much like the lawful monopolist that merely charges a monopoly price. *See id.* at 667.

177 *See id.* at 669-70; *see also* *JTC Petroleum Co. v. Piasa Motor Fuels, Inc.*, 190 F.3d 775, 780 (7th Cir. 1999) (noting that "the most compelling objection" to holding that purely tacit collusion violates the Sherman Act "has nothing to do with the language of the Sherman Act but rather is the difficulty of formulating effective relief without transforming the district court into a regulatory

directed at the activity, a common Section 1 remedy, would be either “hopelessly vague,”¹⁷⁸ demand “irrational behavior,”¹⁷⁹ or result in something akin to undesirable “public-utility regulation.”¹⁸⁰ Significantly, Turner would allow a Section 1 challenge to interdependent pricing that is supported by facilitating practices, such as basing point pricing,¹⁸¹ because those practices could more readily be enjoined than simple interdependent pricing.¹⁸²

By contrast, Posner has insisted not only that “tacit collusion” is “a form of concerted action” but that it violates Section 1.¹⁸³ And though he concedes that “[r]emedy is a problem,”¹⁸⁴ he argues that tacit collusion can be addressed using the remedies of Section 1. He reasons that “[t]acit collusion is not an unconscious state” and that, therefore, a Section 1-type remedy would not imply “telling oligopolists to behave irrationally.”¹⁸⁵ Posner would allow a damages remedy¹⁸⁶ coupled with an injunction against any facilitating practices.¹⁸⁷ Of course, in the case of pure interdependent pricing, by definition, there are no facilitating practices. Turner is willing to condemn cases of oligopolistic interdependence supported by facilitating practices precisely because he, too, can envision a sensible injunction against such practices.¹⁸⁸ So the practical difference between Turner and Posner is that in the case of pure pricing interdependence—a case they both believe will be unusual¹⁸⁹—Turner

agency”); *Clamp-All Corp. v. Cast Iron Soil Pipe Inst.*, 851 F.2d 478, 484 (1st Cir. 1988) (observing that courts refuse to condemn interdependent pricing “not because such pricing is desirable (it is not), but because it is close to impossible to devise a judicially enforceable remedy for ‘interdependent pricing’”).

178 *Turner*, *supra* note 169, at 669.

179 *Id.*

180 *Id.*

181 *See id.* at 675-76.

182 *See id.* at 676 (“Finally, in sharp contrast to the basic-price case, here a perfectly understandable, plausible, and readily enforceable injunction can be written which would have excellent prospects, in most cases, of making price behavior substantially more competitive.”).

183 POSNER, *supra* note 33, at 94. He acknowledges that in this respect he “part[s] company with most other economically minded students of antitrust policy.” *Id.*

184 *Id.* at 98.

185 *Id.* at 97, 98.

186 Posner would prefer an action for damages brought by the Justice Department on behalf of the victims of antitrust violations, a form of suit that would require a statutory change, to a private treble-damages action. *Id.* at 99. But he is apparently willing to accept the private damages suit as a second-best alternative.

187 *Id.* at 98-99. This conception of an appropriate Section 1 remedy marks a slight change in thinking. Posner earlier advocated “a relatively simple and general injunction against express or tacit price-fixing,” together with a damages sanction. Posner, *Oligopoly*, *supra* note 164, at 1591 & n.76. He apparently no longer believes that such an injunction would be useful.

188 *See supra* notes 177-178 and accompanying text.

189 *See* POSNER, *supra* note 33, at 97 (“[T]here probably are few cases of purely tacit collusion.”); *Turner*, *supra* note 169, at 662 (noting that “it may well be that in reality a stable and firm pattern of noncompetitive prices is rarely achieved without some kind of [unlawful] agreement”). *See generally* Lopatka, *supra* note 173, at 879-80.

would find no unlawful agreement, whereas Posner would impose damages liability.

As noted above, courts generally have been unwilling to find unlawful agreements solely on the basis of interdependent pricing. To this extent, they have sided with Turner. They have required evidence of “plus factors,” such as the defendants’ use of practices that facilitate interdependent pricing.¹⁹⁰ But they have not made clear whether simple interdependent pricing behavior, devoid of plus factors, is not an agreement at all on the one hand or that it is a lawful agreement on the other.¹⁹¹

Courts have rarely condemned the merely parallel use of practices that have plausible efficiency justifications.¹⁹² But where competitors explicitly agree to adopt *practices* that serve little purpose other than to facilitate collusion,¹⁹³ courts are more willing to declare the agreement unlawful, even if no overt agreement on *prices* can be detected.¹⁹⁴ For

190 See, e.g., *Todd v. Exxon Corp.*, 275 F.3d 191, 198 (2d Cir. 2001) (noting that a price fixing agreement “may be inferred on the basis of conscious parallelism, when such interdependent conduct is accompanied by circumstantial evidence and plus factors such as defendants’ use of facilitating practices”); *Blomquist Fertilizer, Inc. v. Potash Corp.*, 203 F.3d 1028, 1032-34 (8th Cir. 2000) (finding insufficient evidence of “plus factors” to support an inference of agreement in a case based on a theory of conscious parallelism); *In re Baby Food Antitrust Litig.*, 166 F.3d 112, 122 (3d Cir. 1999) (noting that courts “require that evidence of a defendant’s parallel pricing be supplemented with ‘plus factors’” in order for a court to infer a conspiracy from circumstantial evidence). One court summarized the state of the law as follows: Courts “have almost uniformly held, at least in the pricing area, that . . . individual pricing decisions (even when each firm rests its decision upon its belief that competitors will do the same) do *not* constitute an unlawful agreement under section 1 of the Sherman Act.” *Clamp-All Corp. v. Cast Iron Soil Pipe Inst.*, 851 F.2d 478, 484 (1st Cir. 1988) (Breyer, J.).

191 Turner observes that, as a legal matter, the conclusion that firms engaged in simple pricing interdependence do not violate Section 1 can be stated in either of two ways: “(1) there is no violation because there is no ‘agreement’; or (2) there is no violation because, although there is ‘agreement,’ the agreement cannot properly be called an unlawful agreement.” Turner, *supra* note 169, at 671. Though Turner prefers the latter formulation, he notes that “either way of formulating the result is supportable.” *Id.* In most cases, because the legal effect is the same, the formulation does not matter, and this may be why courts have devoted little attention to distinguishing between the formulations.

192 See, e.g., *E.I. DuPont de Nemours & Co. v. FTC*, 729 F.2d 128 (2d Cir. 1984). *But see Triangle Conduit & Cable Co. v. FTC*, 168 F.2d 175 (7th Cir. 1948), *aff’d by an equally divided court sub nom. Clayton Mark & Co. v. FTC*, 336 U.S. 956 (1949) (upholding a finding that a basing-point system was unlawful without insisting on evidence of an agreement, though such evidence in fact existed).

193 For a fascinating study of the use of facilitating practices by a cartel, see David Genesove & Wallace P. Mullin, *Rules, Communication, and Collusion: Narrative Evidence from the Sugar Institute Case*, 91 AM. ECON. REV. 379 (2001). The authors observe that the sugar cartel never directly fixed prices nor allocated market shares. “Instead, it fixed rules. These rules . . . covered every conceivable aspect of the distribution and marketing of sugar other than the basis price itself. In this way, the refiners eliminated the differential treatment of customers and harmonized contractual practices, thus facilitating the detection of secret price cuts.” *Id.* at 380. On rule-fixing generally, see Robert H. Lande & Howard P. Marvel, *Three Types of Collusion: Fixing Prices, Rivals, and Rules*, 2000 WIS. L. REV. 941.

194 See, e.g., *In re Brand Name Prescription Drugs Antitrust Litig.*, 288 F.3d 1028, 1033 (7th Cir. 2002) (“There is authority for prohibiting as a violation of the Sherman Act or of Section 5 of the Federal Trade Commission Act an agreement that facilitates collusive activity . . .”).

example, *Catalano v. Target Sales*¹⁹⁵ holds that an agreement to eliminate discounts is per se illegal, even though competitors remain free to compete on the ultimate price. Eliminating discounting facilitates tacit collusion by instantly exposing price cutters when basic prices are readily observable.¹⁹⁶ Similarly, an agreement to adopt a basing point pricing system is unlawful because it reduces the number of variables rivals must accommodate in reaching an agreement on the ultimate price.¹⁹⁷ And courts would summarily condemn an agreement among competitors to impose resale price maintenance even if the agreement did not specify the prices, because, as the Court noted in the passage from *Duffy* quoted earlier, industry-wide resale price maintenance is often a device that facilitates collusion by reducing the incentive to cheat on the cartel.¹⁹⁸ But explicit agreements to engage in ambiguous practices—practices that may facilitate collusion but may instead increase efficiency—are generally treated less harshly, though they may be condemned. For example, agreements to exchange price information are judged under the rule of reason and may or may not be found unlawful;¹⁹⁹ alternatively, such agreements may be used as circumstantial evidence of per se illegal price fixing.²⁰⁰

The more difficult case concerns the parallel adoption of facilitating practices without direct proof of explicit agreement. When the practice seems to facilitate collusion unambiguously, there is good reason to condemn it, and courts have been on occasion willing to do so.²⁰¹ Turner,

195 446 U.S. 643 (1980) (holding an agreement among competitors not to extend trade credit illegal per se).

196 Selective discounting tends to imply price discrimination, and this kind of price discrimination can be an indication that sellers are cheating on a tacit cartel arrangement. If so, an agreement to eliminate discounting may shore up the cartel. See generally POSNER, *supra* note 33, at 79-86.

197 See, e.g., *FTC v. Cement Inst.*, 333 U.S. 683, 696-700, 709-17 (1948); POSNER, *supra* note 33, at 91-93.

198 See POSNER, *supra* note 33, at 88-89; Lester G. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86 (1960).

199 See, e.g., *United States v. United States Gypsum Co.*, 438 U.S. 422, 441 n.16 (1978) (“[E]xchanges of [price data and other] information do not constitute a *per se* violation of the Sherman Act.”); *Todd v. Exxon Corp.*, 275 F.3d 191, 198 (2d Cir. 2001) (stating that an agreement to exchange price information “is not illegal *per se*, but can be found unlawful under a rule of reason analysis). See generally Dennis W. Carlton et al., *Communication Among Competitors: Game Theory and Antitrust*, 5 GEO. MASON L. REV. 423, 424 (1997) (arguing that “in the absence of direct evidence to form a ‘naked’ cartel to restrict output or to raise price, the appropriate legal standard to judge the flow of information among competitors is the rule of reason”).

200 See *Todd*, 275 F.3d at 198 (observing that an information exchange is a facilitating practice “that can help support an inference of a price-fixing agreement,” but noting the “closely related but analytically distinct type of claim” that the information exchange itself is unlawful under the rule of reason).

201 See, e.g., *Triangle Conduit & Cable Co. v. FTC*, 168 F.2d 175 (7th Cir. 1948), *aff’d by an equally divided court sub nom. Clayton Mark & Co. v. FTC*, 336 U.S. 956 (1949) (upholding a finding that a basing-point system was unlawful under the Federal Trade Commission Act without insisting on evidence of an agreement, though such evidence in fact existed).

for example, is willing to condemn parallel adoption of a basing-point price system, though he would not outlaw pure interdependent pricing.²⁰² He observes that parallel adoption of a delivered-price system can be “somewhat more readily characterized as ‘agreement’ than parallel basic pricing.”²⁰³ But he would accord different legal treatment to the practices not for that reason, but largely because a sensible remedy can be applied only in the price system case.²⁰⁴ Posner would allow illegal tacit collusion to be inferred from all evidence, including the use of a basing point system.²⁰⁵ But courts have been reluctant to condemn the parallel use of practices they deem competitively ambiguous, including delivered price systems.²⁰⁶

B. *State Regulation and Tacit Collusion*

The law of hybrid restraints has striking implications for the concept of tacit collusion, particularly in the context of facilitating practices. We argue here that, where the government mandates or specifically authorizes individual conduct by private firms that significantly facilitates noncompetitive pricing, the arrangement should be considered a hybrid restraint unless the government directive serves another appreciable and plausible purpose. Because governmental restraints are at issue, the plausibility of the purpose should be evaluated deferentially. The domain of justifications for government regulation is far broader than the domain of justifications for private horizontal agreements. But if the evidence establishes that the government intended to promote noncompetitive pricing by ordering or explicitly tolerating facilitating practices, the restraint should be considered hybrid. This result should follow even if the government seeks to achieve some public goal by lessening price competition. A state cannot, for example, justify an arrangement that amounts to price fixing on the ground that it wants to inhibit consumption of the product by increasing prices.

A restraint should not be deemed hybrid, thereby subjecting the parties to further antitrust scrutiny and possibly the entry of an injunction against compliance with or enforcement of the government directive, merely because conduct contemplated by the state has some remote

202 Turner, *supra* note 169, at 675-76.

203 *Id.* at 676.

204 See *id.* at 676 (“Finally, in sharp contrast to the basic-price case, here a perfectly understandable, plausible, and readily enforceable injunction can be written which would have excellent prospects, in most cases, of making price behavior substantially more competitive.”).

205 See POSNER, *supra* note 33, at 92 (arguing that evidence that the sellers agreed to establish a basing-point system should be “unnecessary to establish a violation of the Sherman Act”).

206 See, e.g., *E.I. DuPont de Nemours & Co. v. FTC*, 729 F.2d 128 (2d Cir. 1984).

potential of leading to tacit collusion.²⁰⁷ Facilitating practices tend to be competitively ambiguous, especially when compelled by a government entity. We have mentioned a number of facilitating practices already: basing-point pricing, the exchange of price information, and particularly industry-wide resale price maintenance. But the list of facilitating practices is not fixed; it expands as economic models and actual experience demonstrate that particular conduct can be conducive to collusion. An anticompetitive explanation could be offered for a wide variety of government-imposed restraints, even some for which the competitively benign justification seems compelling. Conversely, when a government acts to bring about noncompetitive conduct and no significant and plausible competitively-neutral explanation can be offered for the action, the resulting restraint should be subjected to antitrust review. In such a case, because the government at most is only mandating conduct that facilitates collusion, the hybrid restraint will fail the requirements of state action immunity for want of active supervision.

1. Facilitating Practices and the Definition of Agreement

Our suggested definition of hybrid restraints applies to circumstances in which there is no private agreement in the usual sense, only tacit collusion. But, as we saw in the last section, the Supreme Court has already extended the doctrine to reach conduct that is, at best, only analogous to a private agreement. *Fisher* holds that competitors do not conspire with each other just because they uniformly comply with a specific legal requirement. Yet in *Midcal* and *Duffy*, the Court characterized the restraint as resale price maintenance, even though the dealers subject to the resale price mandates were merely complying with a legal requirement. Moreover, the Court analogized the restraints in both *Schwegmann* and *Midcal* to horizontal price fixing, even though competing dealers charged identical prices only because the state required them to charge the price determined by the supplier. Where a private actor determines a price that the state enforces, the restraint is sufficiently analogous to price fixing to justify invalidation.

It is no great extension of this reasoning to apply the concept of hybrid restraints to state directives that facilitate tacit collusion, despite the concept's problematic relationship to the law's standard definitions of agreement. As we noted earlier, one of the reasons the Court condemned the restraint in *Duffy* was that it increased the probability of collusion among wholesalers by deterring cheating. Industry-wide resale price

²⁰⁷ Of course, if *illegal* collusion in fact takes place against the backdrop of the government mandate, that collusion would be a private restraint, subject to antitrust liability.

maintenance is thought to facilitate collusion among suppliers because it reduces the incentive to shade the wholesale cartel price; as long as the dealers adhere to the stipulated resale price, most of the gain from a supplier cheating on the cartel price would inure to the dealer.²⁰⁸ The regulatory structure in *Duffy* not only encouraged suppliers to publicize their prices, but it discouraged them from offering any secret discounts off the wholesale prices they might have agreed to charge. In fact, because government-mandated resale price restrictions typically apply industry wide, there is a stronger economic objection to government-imposed resale price restraints than to purely private resale price maintenance. Such a law would increase the likelihood that competitors will make choices to raise prices above the level that would otherwise prevail. But this interaction among competitors, by itself, might not be considered concerted action under the dominant approach to oligopolistic interdependence. As we have seen in the last section, most courts hold that pure interdependent pricing does not offend Section 1,²⁰⁹ so the statute does not necessarily facilitate conduct that would otherwise be illegal. Nevertheless, as *Duffy* suggests, the result may be a hybrid restraint because the non-competitive pricing behavior may have been impossible absent the assistance of the state. The state context alters the meaning of a horizontal agreement, just as it alters the meaning of a vertical agreement, in identifying state-sponsored restraints that conflict with antitrust rules.

2. Anticompetitive Regulation with Facilitating Practices

We turn now to examples of state regulatory actions that were, we believe, properly condemned as hybrid restraints on the ground that they facilitated noncompetitive pricing. First, in a noteworthy group of cases again arising in alcoholic beverage markets, courts have addressed state “post and hold” statutes, which require liquor distributors to announce price lists and to charge only those prices for as long as the list is in effect.²¹⁰ With one exception, the courts have invalidated the restraints.²¹¹

208 See generally POSNER, *supra* note 33, at 88.

209 See, e.g., *Clamp-All Corp. v. Cast Iron Soil Pipe Inst.*, 851 F.2d 478, 484 (1st Cir. 1988) (noting that courts “have almost uniformly held, at least in the pricing area, that . . . individual pricing decisions (even when each firm rests its decision upon its belief that competitors will do the same) do not constitute an unlawful agreement under section 1 of the Sherman Act”).

210 See *Battipaglia v. N.Y. State Liquor Auth.*, 745 F.2d 166 (2d Cir. 1984). *But see id.* at 179 (Winter, J., dissenting). Without offering much analysis, Professors Areeda and Hovenkamp endorse the dissent’s position on the ground that it is “more consistent with *Midcal*,” given “the great danger that agreements to post and adhere will facilitate horizontal collusion.” I AREEDA & HOVENKAMP, *supra* note 13, at 308-09, ¶ 217b2.

211 See *TFWS, Inc. v. Schaefer*, 242 F.3d 198 (4th Cir. 2001); *Miller v. Hedlund*, 813 F.2d 1344, 1350 (9th Cir. 1986); *Beer & Pop Warehouse v. Jones*, 41 F. Supp. 2d 552, 560-62 (M.D. Pa. 1999); *Canterbury Liquors & Pantry v. Sullivan*, 16 F. Supp. 2d 41, 47-48 (D. Mass. 1998); *Anheuser-Busch, Inc. v. Goodman*, 745 F. Supp. 1048, 1056 (M.D. Pa. 1990). The *Jones* case did not discuss

In the most recent case in the series, *TFWS, Inc. v. Schaefer*,²¹² the Fourth Circuit characterized Maryland's post-and-hold system, which also prohibited volume discounts,²¹³ as "a hybrid restraint that amounts to a per se violation of § 1."²¹⁴ The court reasoned that the post-and-hold and volume discount restrictions were illegal per se, because, under *Catalano, Inc. v. Target Sales, Inc.*,²¹⁵ the retailers would commit per se Section 1 violations by agreeing among themselves on similar restrictions.²¹⁶

This reasoning is striking because nothing in the state's "post-and-hold" scheme purported to authorize liquor wholesalers to agree on prices. Nor did it impose resale prices set by wholesalers on dealers. The arrangement, therefore, did not impose a price chosen by one firm on another firm, like the state-mandated resale price maintenance schemes in *Midcal* and *Schwegmann*. Instead, the law required each wholesaler to adhere to *its own* prices. Nevertheless, the result is a sensible adaptation of the law of facilitating practices to the context of state regulation. Under conventional models of oligopoly behavior, the dissemination of information about prices and a credible commitment to maintain those prices reduce a firm's uncertainty about its rivals' pricing behavior and thereby predictably foster a non-competitive outcome.²¹⁷ And whatever criticisms can be leveled against the theory of oligopolistic interdependence,²¹⁸ the evidence in the case arguably showed that the restrictions in fact increased prices.²¹⁹ Equally important, the Maryland

hybrid restraints directly.

212 242 F.3d 198 (4th Cir. 2001).

213 *Id.* at 202-03. The court remanded for reconsideration of whether the Twenty-first Amendment barred application of the Sherman Act. *Id.* at 213. The protection afforded anticompetitive state regulation by the Twenty-first Amendment is beyond the scope of this Article.

214 *Id.* at 206.

215 446 U.S. 643 (1980) (holding an agreement among competitors not to extend trade credit illegal per se).

216 *TFWS*, 242 F.3d at 209, 210.

217 For example, in his classic article on the subject, Donald Turner emphasizes that an imperfect oligopoly pricing pattern is converted into a perfect one "by eliminating uncertainties." Turner, *supra* note 169, at 673; see also Carlton et al., *supra* note 199 (describing information-sharing practices that can be anticompetitive in certain situations).

218 See, e.g., POSNER, *supra* note 33, at 69 ("There is no sound basis in economic theory for thinking that if there are just a few sellers in a market, competition will disappear *automatically*.") (emphasis in original); Posner, *Oligopoly*, *supra* note 164, at 1566-71. See generally Lopatka, *supra* note 173.

219 On remand for reconsideration of the defendant's Twenty-first Amendment defense, the district court credited the testimony of one of the defendant's expert witnesses that the restrictions "result in higher and more stable prices" than would otherwise exist. *TFWS, Inc. v. Schaefer*, 183 F. Supp. 2d 789, 792 (D. Md. 2002), *vacated*, No. 02-1199, 2003 WL 1689528 (4th Cir. Mar. 31, 2003). The expert testified that the anti-discrimination, or volume-discount, provision leads to higher prices in two ways:

(1) by depriving a manufacturer or wholesaler of one important form of price competition, i.e., the selective price reduction to a favored, usually larger, retailer, which is used as a means of increasing market share; and (2) by reducing incentive for retailers to conduct promotions and advertising, especially price-based

legislature *intended* to induce non-competitive pricing.²²⁰ It apparently believed that the obligations imposed on sellers would “promote[] temperance by eliminating price wars among liquor wholesalers and by maintaining wholesale prices at stable (and higher) levels.”²²¹ The state *expected* the scheme to have anticompetitive effects through unconstrained choices of private parties, and outcomes are more likely to occur when they are intended than when they are inadvertent.²²²

By prohibiting certain unilateral conduct in which private parties might otherwise have engaged, post-and-hold regulations limit the domain of rivalry and thus increase the likelihood of an anticompetitive outcome that private parties could not legally achieve by actual agreement. They may facilitate tacit collusion, even though they do not explicitly authorize any kind of collusion. Thus, federal courts could enjoin the appropriate state officials from enforcing the regulations against private firms that rely on the requirements to collude tacitly. Of course, if the sellers *expressly* colluded after implementation of the regulatory scheme, then the relevant restraint would be the subsequent agreement, a wholly private restraint, and because it was not immune under *Midcal* for want of active supervision, the actors would be liable for violating Section 1.²²³

promotions, since the wholesaler or manufacturer is precluded by law from offering a rebate or allowance to reward or spur the higher volume that such a promotion would bring.

Id. The expert concluded that the price filing requirement results in higher prices because it tends (1) to reduce the opportunity for price competition by requiring that each firm maintain its filed price list for a thirty-day period, and (2) to reduce the incentive for price competition by revealing price cuts to competitors, since in the absence of price filing, one of the incentives to a price reduction is the acquisition of new customers during the period before competitors discover the price cut and adjust their prices.

Id. at 792-93. The plaintiff's expert did not dispute the conclusion that the restrictions increase the price of liquor, but argued that the price increase would not result in reduced consumption. *See id.* at 793-94. On appeal, the circuit court vacated summary judgment for the state, holding that the district court was required to conduct a trial on the disputed question of whether the regulations in fact reduce consumption. *TFWS*, 2003 WL 1689528, at *7.

220 The plaintiff on first remand argued that “Maryland’s true purpose in enacting and defending its statutory scheme is the protection of small retailers.” *Id.* at 791 n.1. Its expert argued that, as a result, the system increased the number of retail outlets. *Id.* at 793. But the district court found that the state’s “avowed” purpose of promoting temperance controlled and that, in any event, the state might have been motivated by both purposes. *Id.* at 791 n.1. Further, the scheme would not necessarily result in more outlets because the state controlled the number of outlets through its licensing system. *Id.* at 793.

221 *TFWS*, 242 F.3d at 203.

222 *See Olympia Equip. Leasing Co. v. W. Union Tel. Co.*, 797 F.2d 370, 379 (7th Cir. 1986).

223 A finding of a hybrid restraint in *TFWS* is consistent with Posner’s view of tacit collusion and can even be reconciled with Turner’s. The government orders the firms to engage in conduct—posting and adhering to prices—that *encourages* collusion, but the individual decisions to set supra-competitive prices are still not inevitable, and if the firms do set these prices, that coordination can be called an unlawful agreement. The government effectively participates in a private anticompetitive agreement. The restraint is hybrid, and punishing it as an antitrust violation will discourage conduct that can be avoided. Under Turner’s view, pure interdependent pricing is beyond the reach of Section 1

In some situations, a government may facilitate collusion not by dictating the conduct of the colluding parties but by creating market conditions that are propitious for tacit collusion.²²⁴ Though either kind of government action may lead to an anticompetitive outcome, the critical practical difference is that laws creating a hospitable climate for collusion are more likely to be economically ambiguous than are directives to engage in facilitating practices. It is one thing to thwart a mandate that has little purpose other than to facilitate collusion, but it is another to inhibit a government from taking action that may sensibly serve a legitimate public interest, even if it may also create an environment favorable to tacit collusion.

A particularly troublesome case along these lines is *A.D. Bedell Wholesale Co. v. Philip Morris, Inc.*,²²⁵ which reviewed the multi-state settlement of the massive tobacco litigation. To settle states' suits to recoup healthcare costs and reduce smoking by minors,²²⁶ the four major tobacco companies ("Majors"), accounting for ninety-eight percent of cigarette sales in the United States, agreed to pay the states about \$200 billion over twenty-five years.²²⁷ Not only did the forty-six states signing on to the Multistate Settlement Agreement ("MSA") promise to drop their suits in exchange,²²⁸ but the MSA contemplated financial penalties for any participating fringe firm that increased its market share,²²⁹ non-participating fringe firms, and new entrants.²³⁰ Twenty fringe firms, accounting for about two percent of the market, became Subsequent Participating Manufacturers ("SPMs").²³¹ An SPM owed nothing to the settlement fund if it maintained its 1998 market share but owed a substantial amount per pack if it increased its share.²³² States were given an incentive to enact "Qualifying Statutes," which impose obligations on any non-signatory tobacco company, including by definition all new entrants, either to become a SPM, with the attendant financial obligations,

and when the government mandates facilitating practices, the firms' subsequent, interdependent pricing can be called pure. But the primary reason for Turner's hesitance to condemn pure tacit collusion is the absence of an effective remedy. In the hybrid restraint context, this concern disappears, because a court can order a public official not to enforce a state mandate to engage in a facilitating practice.

224 In *In re High Fructose Corn Syrup Antitrust Litig.*, 295 F.3d 651, 655 (7th Cir. 2002), the court observed that economic evidence of *explicit* collusion generally includes "evidence that the structure of the market was such as to make secret price fixing feasible (almost any market can be cartelized if the law permits sellers to establish formal, overt mechanisms for colluding . . .)." Structural conditions are equally relevant to the prospects of *tacit* collusion.

225 263 F.3d 239 (3d Cir. 2001).

226 *Id.* at 241.

227 *Id.* at 241-42.

228 *Id.* at 241 n.1.

229 *See id.* at 244.

230 *See id.* at 245.

231 *Id.* at 243.

232 *Id.* at 244.

or to pay a “tax” into an escrow fund.²³³ The payments the Majors agreed to make into the settlement fund in part reflected compensation for past harm suffered by the states, and so prices set to cover those payments would inevitably exceed the unregulated prices of an equally efficient new entrant, which caused no past harm.²³⁴ If new entrants took sales from the Majors, the Majors would suffer financial injury, which might jeopardize their payments to the states.²³⁵ The provisions of the MSA and the Qualifying Statutes were designed to “effectively and fully neutralize[] the cost disadvantages that the Participating Manufacturers [would] experience vis-a-vis Non-Participating Manufacturers.”²³⁶ Plaintiff wholesalers claimed that the restrictions on expansion and new entry “permitted the Majors to raise their prices to near monopoly levels,” levels “allegedly above those necessary to fund the settlement payments.”²³⁷

233 *Id.* at 246. Under the terms of the agreement, if a state does not enact a qualifying statute and non-participating manufacturers gain market share, the Majors are permitted to reduce their payments to the settlement fund by more than a proportionate amount. *Id.* at 244. The agreement provides that a state’s payment “shall not be subject to” such an adjustment if the state enacts a qualifying statute. *id.* at 244 n.19. For a description of the provisions of the MSA designed to impede new entry, see Hanoch Dagan & James J. White, *Governments, Citizens, and Injurious Industries*, 75 N.Y.U. L. REV. 354, 381-82 (2000) (observing that the “agreement with the states contains a diabolically clever set of provisions to insulate cigarette manufacturers” from competition from new entrants).

234 One court explained that the amounts paid in settlement by the participating manufacturers were intended to redress “past and future damages.” *Star Scientific, Inc. v. Beales*, 278 F.3d 339, 351 (4th Cir. 2002) (holding in a challenge to the MSA and the Virginia qualifying statute that the settlement does not violate due process, equal protection, the Commerce Clause, or the Compact Clause). By contrast, “nonparticipating members are required to put money into escrow which is held only for assuring that the nonparticipating manufacturers’ future liability is satisfied.” *Id.* (emphasis added). The court apparently accepted the plaintiff’s assertion that, “while all of the payments made by nonparticipating manufacturers under the [Virginia] qualifying statute are used to pay for future harms caused to the Commonwealth, only five percent of the payments made by participating manufacturers go to addressing future harms.” *Id.* at 353 (emphasis in original).

235 As one court explained:

Because of a concern that manufacturers participating in the Master Settlement Agreement might suffer a competitive disadvantage when compared to nonparticipating manufacturers and that this disadvantage could affect the participating manufacturers’ ability to make the settlement payments, the Master Settlement Agreement includes provisions to protect the market shares and profitability of the participating manufacturers.

Id. at 345-46.

236 *Bedell*, 263 F.3d at 246 (quotation marks omitted). As the court explained:

Together, the Renegade Clause, the Qualifying Statutes and the Enforcement Fund allegedly create severe obstacles to market entry, or to increasing production and market share. This is not accidental. The Multistate Settlement Agreement explicitly proclaims its purpose to reduce the ability of non-signatory cigarette manufacturers to seize market share because of the competitive advantage accruing from not contributing to the settlement.

Id. (citation omitted).

237 *Id.* The plaintiffs alleged that the Majors could have funded the settlement by a price increase of \$0.19 per pack, but the Majors instituted two price increases totaling \$0.76 per pack. *Id.*

State Action and Hybrid Restraints

The Third Circuit held that the “case resembles a hybrid restraint.”²³⁸ It then applied the *Midcal* analysis, concluding that, though the MSA represented a clear state policy to displace competition,²³⁹ it failed to provide for adequate supervision.²⁴⁰ The court, however, did find the defendants’ activities in reaching the settlement immune under the *Noerr-Pennington* doctrine,²⁴¹ which protects from antitrust liability good faith efforts by private actors to secure anticompetitive government actions.²⁴²

Nothing in the MSA or the Qualifying Statutes explicitly authorized the Majors to set prices jointly. If a state had authorized express collusion, the restraint would certainly have been hybrid and subject to *Midcal*. Indeed, though the plaintiffs alleged that the Majors violated Section 1, they apparently did not claim that the Majors explicitly colluded on prices.²⁴³ Rather, they based their allegation of an agreement on the MSA itself, which obviously is an agreement but did not authorize any further express collaboration.²⁴⁴ The best anticompetitive story that can be told is that the states intentionally created a zone of pricing freedom that the Majors could exploit through pricing interdependence. Hence, the scheme allegedly allowed the Majors to increase the market price of cigarettes by \$.76 per pack, when an increase of \$.19 per pack would have been enough to satisfy their obligation to the states.²⁴⁵ Unlike post-and-hold statutes, the state restrictions fostered tacit collusion by constraining the conduct of fringe and potential competitors, or stated otherwise, by limiting entry and expansion. But in both contexts, the resulting market prices were expected to be non-competitive, allegedly the result of unconstrained private decisions.²⁴⁶

238 *Id.* at 258 (internal quotation marks omitted).

239 *Id.* at 260 (“[I]t is evident that the Multistate Settlement Agreement was backed by clearly articulated state policy.”).

240 *Id.* at 262. The court noted, “[W]e are not convinced that the States satisfy *Midcal*’s ‘active supervision’ prong. This is because the States’ supervision does not reach the parts of the Multistate Settlement Agreement that are the source of the antitrust injury.” *Id.* The provisions of the MSA providing for regulation “have no effect on pricing or production and thus do not regulate the challenged anticompetitive conduct.” *Id.* at 264.

241 *Id.* at 254.

242 For a description of the *Noerr-Pennington* doctrine, see *supra* note 83.

243 Tellingly, the court did not find that the MSA authorized the manufacturers to collude, but rather that it “empowers the tobacco companies to make anticompetitive decisions with no regulatory oversight by the States.” *Bedell*, 263 F.3d at 260 (emphasis added).

244 *Id.* at 241.

245 *Id.* at 246.

246 Interestingly, the Court in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), rejected the argument that cigarette manufacturers could use tacit collusion to recoup the losses incurred in a campaign of predatory pricing. The Court described tacit collusion as a process “not in itself unlawful,” *id.* at 227, thereby endorsing the Turner view. Nor did the Court find tacit collusion a sufficient basis for inferring that oligopolists will be able to recoup losses from a predatory pricing campaign. See *id.* at 227-28. *Bedell*, however, implicitly relied on the prospect of enhanced tacit collusion to condemn an unsupervised, state-sponsored arrangement. The difference between the two cases lies in the government context. However unlikely tacit collusion is in the

Cases like *TFWS* and *Bedell* hint at the danger of extending the concept of a hybrid restraint to government-mandated facilitating practices. If any government directive that facilitates non-competitive behavior is called a hybrid restraint, states may be unduly constrained in their regulatory choices. A wide range of common government regulations could potentially be termed hybrid under this definition and thus trigger antitrust liability unless protected by the state action doctrine. Immunity would require not only active supervision but a clear policy articulated by the state as sovereign authorizing the regulatory scheme.

Of course, a successful antitrust challenge based on government-supported facilitating practices requires a theory as to how the conduct in question does indeed facilitate collusion. Sometimes, a restraint can be deemed unilateral for want of a plausible theory. For example, reconsider *Massachusetts Food Association v. Massachusetts Alcoholic Beverages Control Commission*,²⁴⁷ where the state law provided that “no one can own more than three retail liquor stores” in the state.²⁴⁸ It is difficult to construct a theory as to how the three-store limit facilitates collusion, unless the state severely restricts the number of *owners* as well as the number of outlets; indeed, the law may hinder collusion by reducing concentration.

In other cases, the theory explaining the anticompetitive potential of a restraint may be tenuous. Recall that in *Hostetter*, for example, the restraint included a requirement that liquor dealers charge prices in New York no higher than the lowest price at which they made sales anywhere else in the country during the preceding month.²⁴⁹ As a matter of theory, most-favored-nation clauses may indicate collusion,²⁵⁰ but they may also increase efficiency.²⁵¹ Thus, the arrangement would fail our standard. Also, under this reasoning, the Second Circuit erred in *Hertz Corp. v. City*

unregulated context following a predatory campaign, it is far more likely where the state intrudes to inhibit rivalry. The *Brooke Group* Court identified the threat of expansion by fringe firms and new entrants as sources of instability for tacit arrangements, but these are precisely the activities the states sought to inhibit in *Bedell*.

247 197 F.3d 560 (1st Cir. 1999).

248 *Id.* at 562. Ironically, the Supreme Court in *Rice*, in emphasizing the lack of anticompetitive potential of the California designation statute, noted that the statute did not limit the “number of importers which may be designated by the distiller.” *Rice v. Norman Williams Co.*, 458 U.S. 654, 662 (1982). The Massachusetts scheme did indeed limit the number of retail outlets a single dealer could own. But the observation in *Rice* was intended to show that the restriction at issue was even less suspect than it might have been, not that a restriction on the number of distributors would be invalid under the antitrust laws.

249 *Joseph E. Seagram & Sons, Inc. v. Hostetter*, 384 U.S. 35, 39-40 (1966).

250 See George A. Hay, *Facilitating Practices: The Ethyl Case*, in *THE ANTITRUST REVOLUTION: ECONOMICS, COMPETITION, AND POLICY* 194-95 (John E. Kwoka, Jr. & Lawrence J. White eds., 3d ed. 1999).

251 See, e.g., Keith J. Crocker & Thomas P. Lyon, *What Do “Facilitating Practices” Facilitate? An Empirical Investigation of Most-Favored-Nation Clauses in Natural Gas Contracts*, 37 *J.L. & ECON.* 297 (1994).

of *New York*,²⁵² when it held that a New York City ordinance prohibiting rental car companies from imposing fees based on a person's residence "merits hybrid treatment."²⁵³ The restraint unilaterally limited firms' ability to make differential charges and did not, by any theory now recognized, encourage collusive behavior. But so long as a plausible theory can be articulated predicting a risk of tacit collusion, the restraint will be suspect.

More importantly, though, the theory supporting the anticompetitive potential of some restraints is robust. For example, because pricing interdependence requires that a market have no more than a few sellers,²⁵⁴ any government-imposed scheme restricting the right to operate to a small number of suppliers, without a concomitant specification of price, could easily be termed hybrid. Thus, a state might permit only six firms to provide limousine service at an airport without setting rates.²⁵⁵ The potentially enormous scope of the facilitation approach to defining hybrid restraints, therefore, is troublesome. The concern, however, should not be overstated. First, a court can derive some information on the capacity of a restraint to facilitate collusion from the identity of the complainants. If the sellers who pose the risk of collusion object to the restraint, as the landlords did in *Fisher*, the restraint is almost certainly not facilitating collusion, and it can be adjudged unilateral. Second, a restraint is hybrid only if it results in private collusion; *Fisher* makes clear that states are free to dictate prices. For this reason, a state or municipal agency limiting the number of limousine service providers at an airport may typically specify rates as well, and the result would be a unilateral restraint. We have no empirical estimate of the number of governmental restraints that in fact facilitate collusion.

More significantly, states have the full range of police powers and can act to advance health, safety, and welfare in ways that have an ancillary effect on competition. They have a greater range of justifications for regulations that limit competition than would private competitors in regulating their own behavior. Our approach is deferential: where the government mandates or specifically authorizes individual conduct that significantly facilitates collusive pricing by private competitors, the arrangement should be considered a hybrid restraint *unless* the government

252 1 F.3d 121 (2d Cir. 1993).

253 *Id.* at 127. The court concluded that the "law is not a 'unilateral' restraint," though it does not "easily fit the fact pattern of the cases held to involve 'hybrid' restraints" either. *Id.*

254 See, e.g., POSNER, *supra* note 33, at 68-69 (noting that "concentration is a necessary condition of tacit collusion"); Turner, *supra* note 169, at 661 (noting that interdependent behavior "might well arise in an 'oligopoly' situation (*i.e.*, where sellers are 'few')").

255 In *Commuter Transportation System, Inc. v. Hillsborough County Aviation Authority*, 801 F.2d 1286, 1288 (11th Cir. 1986), the state agency restricted the number of limousine service providers to six, but it had contracts with them that presumably contained price terms.

directive serves an appreciable and plausible competitively-benign purpose. Thus, a law limiting the number of limousine companies serving an airport might plausibly be justified by concerns about congestion or safety of passengers. Similarly, a state law requiring stores to close at a certain time each day would not be a hybrid restraint, even though the stores themselves could not legally agree on a fixed closing time.²⁵⁶ A statutory closing time might reduce competition along one dimension and, conceivably, could affect price or output; but it would be difficult to characterize the restraint as primarily aimed at facilitating noncompetitive behavior, because the state's justifications are likely to be plausible and appreciable (under a properly deferential standard). Although some laws limiting entry or expansion, like the one in *Bedell*, may be primarily designed to facilitate noncompetitive pricing, that kind of law is bound to be unusual.

Moreover, intent evidence is useful in identifying hybrid restraints. In both *Bedell* and *TFWS*, for example, the state *intended* to permit private parties to price less competitively. Usually, evidence of intent is of limited utility in antitrust cases.²⁵⁷ Firms are not adept at expressing their intentions artfully, and vigorous competition implies an intent to injure a rival anyway. But when the government intends to permit firms to behave non-competitively, one inference is that, all else equal, non-competitive behavior is more likely to result. Another inference is that the law is not designed to achieve public purposes unrelated to collusion. Stated otherwise, government directives that are intended to facilitate collusion are likely to be unambiguous. This is not to say, however, that a government's statement of intent should be taken as irrefutable evidence of the regulation's purpose. Legislators commonly express a benign purpose in order to mask its real desire to transfer wealth. In an appropriate case, if the explicit statement of intent is demonstrably specious, it ought to be disregarded. By contrast, absent any demonstrable intent on the part of government to facilitate collusion, a restriction on the number of firms in a market that can be explained as an attempt to reduce traffic congestion or pollution might be deemed unilateral, even if higher prices result.

²⁵⁶ See *Mass. Food Ass'n v. Mass. Alcoholic Beverages Control Comm'n*, 197 F.3d 560, 565 (1st Cir. 1999).

²⁵⁷ See, e.g., *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d 1396, 1401-03 (7th Cir. 1989); *Ball Mem'l Hosp., Inc. v. Mut. Hosp. Ins., Inc.*, 784 F.2d 1325, 1338-39 (7th Cir. 1986); *Olympia Equip. Leasing Co. v. W. Union Tel. Co.*, 797 F.2d 370, 379-80 (7th Cir. 1986); *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 232 (1st Cir. 1983).

V. Private Monopolies and Hybrid Restraints

.. In the preceding part, we focused on the prospect of collusive behavior. The private discretion that is required for a hybrid restraint in that context pertains to the ability of competitors to price interdependently. But suppose a state confers a monopoly on a firm and allows it to price without regulatory constraints. Would the entry restrictions inherent in the creation of the monopoly suffice to render the scheme a hybrid restraint? Under our analysis, the answer is no. The government-protected monopolist has the requisite discretion for a hybrid restraint, but its conduct is not closely analogous to behavior that violates Section 1. For a monopolist simply to charge monopoly prices resembles no recognized Section 1 offense.

For example, in *Arsberry v. Illinois*,²⁵⁸ state correctional authorities granted telephone companies exclusive rights to provide telephone service in each prison and jail in return for fifty percent of the revenues generated.²⁵⁹ According to Judge Posner, because the state is a monopolist with “iron control over access to the inmate market,” it does not violate the antitrust laws by renting “pieces of the market to different phone companies.”²⁶⁰ The court concluded that “[s]tates and other public agencies do not violate the antitrust laws by charging fees or taxes that exploit the monopoly of force that is the definition of government.”²⁶¹ Furthermore, “the persons with whom the states contract [do not] violate the antitrust laws by becoming state concessionaires, provided those persons do not collude among themselves or engage in other anticompetitive behavior, of which charging high prices as a state concessionaire is not a recognized species.” The rates charged by the phone companies were apparently not specified in the contracts conferring exclusive rights. The rates were contained in tariffs filed with federal and state regulatory agencies,²⁶² but conceivably the agency’s supervision of those rates was not sufficiently active to pass muster under *Ticor*. Nevertheless, the presence or absence of state action immunity is beside the point. Even if each telephone company had been granted a degree of pricing discretion, the arrangement would not conflict with the antitrust laws as a hybrid restraint because the conduct does not resemble an antitrust violation.

258 244 F.3d 558 (7th Cir. 2001) (Posner, J.).

259 *Id.* at 566.

260 *Id.*

261 *Id.*

262 *See id.* at 561.

Now consider *Electrical Inspectors, Inc. v. Village of East Hills*.²⁶³ Pursuant to state authority, municipalities gave a private, not-for-profit firm the exclusive right to conduct inspections of new buildings for compliance with the electrical code but did not regulate the fees the firm charged to homeowners and electricians.²⁶⁴ A for-profit competitor challenged the scheme, seeking damages against the firm and equitable relief against the cities. The district court held that the cities and the exclusive inspector were entitled to state action immunity, concluding that the cities satisfied the clear state policy requirement, that the cities' immunity extended to the inspector, and that active supervision was not required.²⁶⁵ The circuit court reversed on the ground that active supervision of the inspector was required for the inspector's own immunity²⁶⁶ and perhaps for the cities' immunity as well,²⁶⁷ and it remanded for an inquiry into supervision.²⁶⁸ Though neither court considered it, the unilateral restraint doctrine, in our view, could have disposed of the bulk of the claim, rendering consideration of the state action doctrine unnecessary. To the extent the plaintiff challenged the inspector's monopoly pricing, the restraint was not hybrid, both because the conduct was not analogous to an antitrust violation and because the justification for the restraint was plausible and appreciable.²⁶⁹ One town asserted that "it would not be in the best interests of the village (and its residents) or building owners to have more than one qualified agency performing services because additional inspectors 'would result in loss of control . . . over the electrical inspection process and the quality of the end result.'"²⁷⁰ The argument that competition in the electrical inspection services market would be inefficient—and here threaten public safety—is

263 320 F.3d 110 (2d Cir. 2003).

264 *Elec. Inspectors, Inc. v. New York Bd. of Fire Underwriters*, 145 F. Supp. 2d 271, 275 (E.D.N.Y. 2001), *vacated sub nom. Elec. Inspectors, Inc. v. Village of East Hills*, 320 F.3d 110 (2d Cir. 2003).

265 *Elec. Inspectors*, 145 F. Supp. 2d at 278-279.

266 *Elec. Inspectors*, 320 F.3d at 128.

267 *Id.* at 129.

268 *Id.*

269 The plaintiff seemingly tried to avoid alleging that the charging of a monopoly price alone exposed the inspector to antitrust liability, *see id.* at 127, but its allegation that the firm abused its monopoly "by providing low-quality service," *id.* at 116, amounted to the same thing. The relevant economic concept is *quality-adjusted* price, here a monopoly quality-adjusted price. The mere exploitation of monopoly power is not an antitrust violation. But the plaintiff also asserted that the inspector violated the antitrust laws by "threatening to retaliate in those locations where it has exclusivity against customers who use the plaintiff's services where competition is allowed." *Id.* at 116. Such conduct may even have been sufficiently remote from the municipal regulatory scheme as to be a private restraint. Otherwise, it was hybrid and subject to state action immunity analysis. The plaintiff's final claim, that the inspector "attempted to monopolize inspections services by seeking government-issued exclusivity," *id.* at 128, clearly alleged private conduct, but conduct that almost certainly enjoyed *Noerr-Pennington* immunity.

270 *Elec. Inspectors*, 145 F. Supp. 2d at 276 (quoting Affidavit of Frank B. Falco ¶¶ 11, 17).

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not compelling, though this kind of argument has stronger legs when made by a municipality with no financial interest in limiting competition than when asserted by private competitors who agree to limit rivalry.²⁷¹ And the justification does not directly explain why the villages did not set the price. But under a deferential standard of review, the restraint is unilateral.²⁷²

We have been arguing that a state-granted monopoly coupled with pricing discretion does not constitute a hybrid restraint and, for that reason, does not conflict with Section 1 of the Sherman Act. But the *Fisher* Court alluded to the possibility that a unilateral restraint imposed by government may violate Section 2. In a footnote, the Court wrote:

Though they have not pressed the point with any vigor in this Court, appellants have suggested that Berkeley's rent controls constitute attempted monopolization because the city 'is clearly engaged in the provision of housing in the public sector' and using the controls to depress the prices of residential properties as a prelude to taking them over. As to this claim, we note only that the inquiry demanded by appellants' allegations goes beyond the scope of the facial challenge presented here.²⁷³

A violation of Section 2 of the Sherman Act, of course, does not require concerted action. Therefore, the fact that a restraint is unilaterally imposed by government does not imply a lack of conflict with this statutory provision. But the logic that drives the distinction between hybrid and unilateral restraints for purposes of identifying a conflict with Section 1 applies equally here. A state mandate does not conflict with antitrust unless it authorizes or facilitates conduct analogous to an antitrust violation, regardless of its effect on consumer welfare.

Section 2 outlaws exclusionary conduct—conduct that injures competition and does not increase efficiency—that either results in monopoly power or poses a dangerous probability of resulting in such

271 Cf. *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 693 (1978) (rejecting a justification for an agreement by engineers not to engage in competitive bidding that competition "would lead to deceptively low bids, and would thereby tempt individual engineers to do inferior work with consequent risk to public safety and health").

272 In *In re Massachusetts Bd. of Registration in Optometry*, 110 F.T.C. 549 (1988), the FTC suggested a somewhat related interpretation of *Fisher*: If the governmental body imposing the restraint consists of individuals with separate economic identities and a financial interest in the regulation, then any restraint imposed by it cannot be unilateral. The FTC concluded that members of the state optometry board engaged in a combination when they acted together to impose a restriction on truthful advertising. We doubt that the status under *Fisher* of an otherwise unilateral restraint depends on the composition of the government agency. The principle in any event would have limited applicability. It would not apply, for instance, to a typical public utilities commission, whose members by law must be disinterested. Further, the FTC would be hard pressed to extend the principle to a city council, even if its part-time members economically benefitted from an ordinance as commercial actors.

273 *Fisher v. City of Berkeley*, 475 U.S. 260, 270 n.2 (1986) (citations omitted).

power. For the completed offense of monopolization, for example, the plaintiff must show “(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.”²⁷⁴ To prove attempted monopolization, the plaintiff must show “that (1) the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize.”²⁷⁵ The law does not prohibit the mere possession and use of monopoly power,²⁷⁶ and with good reason. The prospect of monopoly profits can be the carrot that prompts firms to innovate and thereby improve the lot of consumers. Section 2 is premised on the assumption that the benefits flowing from this dynamic process outweigh the static inefficiency caused by monopoly pricing.

In general, government-granted monopolies are not acquired through exclusionary conduct within the meaning of the law. Petitioning government for the monopoly may not be socially productive, but it is separately protected under the *Noerr-Pennington* doctrine.²⁷⁷ The government’s action in granting the monopoly may or may not be socially productive, and if it is, the reason may have little to do with encouraging innovation. But, in any case, it has no counterpart in the law of exclusionary conduct developed under Section 2. Similarly, the exploitation of the monopoly by charging higher prices does not satisfy the conduct element of Section 2. For example, in *Endsley v. City of Chicago*,²⁷⁸ the court rejected the claim that a city violated Section 2 by raising tolls on a highway, noting that simply raising prices is not itself anticompetitive. Similar logic would apply in the context of a simple grant of a state monopoly to a private firm—the firm’s action in raising prices would not be exclusionary. Thus, to the extent the complaint in *Electrical Inspectors* alleged that monopoly pricing by the government-designated exclusive inspector violated Section 2,²⁷⁹ it should fail for want of exclusionary conduct. In short, a unilateral restraint imposed by government that results in the exploitation of monopoly power by a private

274 *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966).

275 *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 447 (1993).

276 As noted in *Marshfield Clinic*,

A natural monopolist that acquired and maintained its monopoly without excluding competitors by improper means is not guilty of “monopolizing” in violation of the Sherman Act and can therefore charge any price that it wants for the antitrust laws are not a price-control statute or a public-utility or common-carrier rate-regulation statute.

Blue Cross & Blue Shield United v. Marshfield Clinic, 65 F.3d 1406, 1412-13 (7th Cir. 1995) (citations omitted).

277 See *supra* note 83 and accompanying text.

278 230 F.3d 276, 283 (7th Cir. 2000).

279 See *Elec. Inspectors, Inc. v. Village of East Hills*, 320 F.3d 110, 128 (2d Cir. 2003) (referring to a Section 2 allegation).

firm lacks the close analogy to a Section 2 violation necessary for a conflict between the government action and the antitrust statute.²⁸⁰ Such a restraint avoids antitrust condemnation regardless of state action immunity.

Conclusion

Because state and local governments regulate economic activity in myriad ways, tension with federal antitrust policy is inevitable. The Court has developed a sophisticated doctrine of state action immunity to resolve conflicts between the federal antitrust laws and state policies. But state action immunity need be considered only when there is a real conflict. The Court has attempted to identify conflicts by distinguishing between hybrid restraints, which do conflict with antitrust law, and restraints unilaterally imposed by government, which do not. But its guidance has been cryptic.

We have offered a more comprehensive approach to unilateral governmental and hybrid restraints. Under our approach, a unilateral governmental restraint is one in which public officials determine the nature and extent of the resulting consumer injury, even though the decision is effectuated through the actions of private parties in compliance with the government's mandates; a hybrid restraint is one in which the government specifically empowers private actors to exercise discretion as to the nature or level of consumer injury in a way that is closely analogous to an antitrust violation. Properly applied, this doctrine works in tandem with the doctrine of state action immunity to isolate and remove from further antitrust scrutiny governmental actions that do not reflect a naked repudiation of antitrust.

²⁸⁰ We confine our comments to situations in which the government merely regulates the conduct of private parties. State and local governments instead may function as market participants. As a matter of substantive law, a defendant cannot violate Section 2 unless it competes in the market that it is monopolizing or attempting to monopolize. E.g., *Discon, Inc. v. NYNEX Corp.*, 93 F.3d 1055, 1062 (2d Cir. 1996), *rev'd on other grounds*, 525 U.S. 128 (1998); *Official Airline Guides, Inc. v. FTC*, 630 F.2d 920, 925-27 (2d Cir. 1980). To conflict with Section 2, therefore, a state or local government must at a minimum be engaged in a commercial enterprise. If a governmental entity acting in a proprietary capacity engages in exclusionary conduct that is *commercial* in nature, the analogy to private Section 2 violations is much closer than when the government merely regulates, and the argument that the government's action conflicts with the antitrust laws is therefore much stronger. If the entity protects its proprietary interests through exclusionary conduct that is *governmental* in nature, the analogy is tenuous, but there is an arguable conflict with Section 2. We note the issue here, but a full exploration of it is beyond the scope of this Article.

