

Spring 2007

Reconciling the Harvard and Chicago Schools: A New Antitrust Approach for the 21st Century

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Reconciling the Harvard and Chicago Schools: A New Antitrust Approach for the 21st Century

THOMAS A. PIRAINO, JR.*

INTRODUCTION: A NEW APPROACH TO ANTITRUST ANALYSIS.....	346
I. THE BATTLE FOR THE SOUL OF ANTITRUST	348
A. <i>The Harvard School</i>	348
B. <i>The Chicago School</i>	350
II. THE PRINCIPAL CASES REFLECTING THE HARVARD/CHICAGO SCHOOL CONFLICT	352
A. <i>The Restraint of Trade Cases</i>	352
B. <i>Merger and Joint Venture Cases</i>	356
C. <i>Monopoly Cases</i>	359
D. <i>The Need for a Harvard/Chicago School Synthesis for Antitrust Regulation</i>	362
III. MOVING BEYOND THE HARVARD/CHICAGO DICHOTOMY TO A NEW ANTITRUST APPROACH.....	364
A. <i>Post-Chicago Scholarship</i>	364
B. <i>The Lower Federal Courts' and Agencies' Movement Toward a New Approach</i>	365
C. <i>The Supreme Court's New Approach in California Dental</i>	366
IV. A NEW APPROACH TO ANTITRUST REGULATION.....	367
A. <i>Classifying Competitive Conduct on a California Dental Continuum</i> 367	
B. <i>Presumptively Legal or Illegal Conduct</i>	368
C. <i>Conduct Requiring a Prioritized Market Analysis</i>	370
V. PRESUMPTIVELY LEGAL CONDUCT	371
A. <i>Vertical Restraints of Trade</i>	371
B. <i>Vertical Mergers and Joint Ventures</i>	374
VI. PRESUMPTIVELY ILLEGAL CONDUCT.....	378
A. <i>The Presumption of Illegality</i>	378
B. <i>The Plaintiff's Initial Burden of Proof</i>	381
C. <i>The Defendant's Rebuttal Case: Proving Restraints Ancillary to Joint Ventures</i>	383
VII. CONDUCT REQUIRING A PRIORITIZED MARKET ANALYSIS	390
A. <i>Tying and Exclusive Dealing Arrangements</i>	391
B. <i>Monopoly Cases</i>	394
C. <i>Horizontal Mergers</i>	399
D. <i>Horizontal Joint Ventures</i>	405
CONCLUSION	409

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INTRODUCTION: A NEW APPROACH TO ANTITRUST ANALYSIS

The principal federal antitrust laws, the Sherman Act of 1890 and the Clayton Act of 1914, are broadly worded, and they give the federal courts and antitrust enforcement agencies wide leeway to develop a federal “common law” of antitrust regulation.¹ Over the 115 years since the adoption of the Sherman Act, the courts and enforcement agencies have altered their interpretation of the antitrust laws to match prevailing economic assumptions. Two opposing economic theories have battled for dominance during the modern antitrust era.

In the 1960s and 1970s, the courts and agencies adopted the economic theories of a group of Harvard scholars who assumed that firms with market power would act in an anticompetitive manner.² Under the “Harvard School” approach, the courts and agencies presumed the illegality of any mergers, joint ventures, or agreements that allowed firms to obtain, enhance, or exercise market power, regardless of whether the conduct had the potential to benefit consumers by lowering prices or increasing output.

However, beginning in the late 1970s, the courts and agencies began to adopt the theories of a group of University of Chicago academics,³ who taught that the only legitimate goal of the antitrust laws was to promote consumer welfare.⁴ Under the “Chicago School” approach, the courts and agencies became much less willing to prohibit competitive conduct on its face. Instead, they felt compelled to engage in an extensive factual inquiry to confirm the effects of particular conduct on consumers before finding it illegal.

The presumptions of illegality afforded by the Harvard School and the empirical economic approach of the Chicago School represented opposite poles of antitrust enforcement. Plaintiffs usually could prevail under a Harvard School approach because they were excused from proving complex economic facts, while defendants usually could win under the Chicago School approach because plaintiffs were unable to meet their burden of proving the adverse economic effects of particular types of conduct.⁵

1. Section 1 of the Sherman Act prohibits “every contract, combination . . . or conspiracy, in restraint of trade,” 15 U.S.C. § 1 (2004); section 2 of the Sherman Act makes it illegal for a firm to “monopolize, or attempt to monopolize” interstate commerce, *id.* § 2; and section 7 of the Clayton Act prohibits any mergers the effect of which “may be substantially to lessen competition, or to tend to create a monopoly,” *id.* § 18. Because of the broad wording of these statutes, “[p]erhaps uniquely, American antitrust law is a creature of judicial, as opposed to legislative, creation.” Motion for Leave to File and Brief of Visa U.S.A., Inc. et al. as Amici Curiae Supporting Petitioners on Petition for Writ of Certiorari at 8, *Texaco, Inc. v. Dagher*, 126 S. Ct. 1276 (2006) (Nos. 04-805 & 04-814).

2. The Harvard scholars included Donald F. Turner and Philip Areeda, who were influenced by earlier Harvard economists such as Edward Chamberlain, Edward Mason, and Joe Bain. Herbert Hovenkamp, *The Rationalization of Antitrust*, 116 HARV. L. REV. 917, 920 (2003) (reviewing RICHARD A. POSNER, *ANTITRUST LAW* (2d ed. 2001)).

3. The Chicago School scholars included Robert Bork, Richard Posner, and Frank Easterbrook. See ROBERT H. BORK, *THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF* (1978); RICHARD A. POSNER, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* (1976); Frank Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. 135 (1984).

4. See *infra* notes 21–35 and accompanying text.

5. See *infra* note 39 and accompanying text.

As the courts and agencies moved between the divergent approaches of the Chicago and Harvard Schools, business executives became confused as to the applicable rules of competitive conduct.

This author argues in a series of articles, published between 1991 and 2001, that antitrust analysis need not be viewed as a choice between the extremes of the Harvard and Chicago Schools. Instead of viewing antitrust analysis through either a Harvard or Chicago School lens, the courts and agencies should adopt a “third way” that builds upon the insights of both Schools. Neither the Harvard School’s presumptions nor the Chicago School’s empiricism are appropriate in all cases. The courts and agencies should construe antitrust analysis as a continuum, under which they can vary their degree of inquiry depending upon the likely competitive effects of the particular conduct at issue.⁶

In 1999, in *California Dental Ass’n v. FTC*,⁷ the United States Supreme Court, citing the work of this author and other antitrust commentators, endorsed a similar type of analysis. *California Dental* made it clear that antitrust analysis should be conducted under a sliding scale, allowing for different levels of scrutiny depending upon the type of restraint at issue.⁸ However, *California Dental* did not explain how to apply its sliding scale analysis to specific types of competitive conduct, and the lower federal courts have not yet been able to use *California Dental* to reconcile the antitrust divide between the Harvard and Chicago Schools.⁹

This Article sets forth a comprehensive means of analyzing all types of competitive conduct in a manner consistent with *California Dental*. The proposed approach would

6. See Thomas A. Piraino, Jr., *A Proposed Antitrust Approach to Collaborations Among Competitors*, 86 IOWA L. REV. 1137 (2001) [hereinafter Piraino, Jr., *Antitrust Approach to Collaborations*]; Thomas A. Piraino, Jr., *Making Sense of the Rule of Reason: A New Standard for Section 1 of the Sherman Act*, 47 VAND. L. REV. 1753 (1994); [hereinafter Piraino, Jr., *Rule of Reason*]; Thomas A. Piraino, Jr., *Reconciling the Per Se and Rule of Reason Approaches to Antitrust Analysis*, 64 S. CAL. L. REV. 685 (1991) [hereinafter Piraino, Jr., *Reconciling*].

7. 526 U.S. 759 (1999). *California Dental* has been called a “major antitrust event” and may constitute a watershed in the Court’s approach to antitrust analysis. See Charles P. Weller, *A “New” Rule of Reason from Justice Brandeis’ “Concentric Circles” and Other Changes in Law*, 44 ANTITRUST BULL. 881, 949 (1999).

8. *California Dental*, 526 U.S. at 780 (citing PHILLIP AREEDA, ANTITRUST LAW ¶ 1507 (1986); William Kolasky, *Counterpoint: The Department of Justice’s “Stepwise” Approach Imposes Too Heavy a Burden on Parties to Horizontal Agreements*, ANTITRUST, Spring 1998, at 41, 43; Piraino, Jr., *Rule of Reason*, *supra* note 6, at 1771).

9. The divide between the Harvard and Chicago approaches was evident in the differing reactions to the Supreme Court’s recent decision in *Verizon Communications, Inc. v. Trinko*, 540 U.S. 398 (2004), which found that a monopoly telephone company should not be liable for refusing to allow access to its telephone network. A prominent follower of the Chicago School applauded the Court’s conclusion that fact finders are ill-equipped to regulate access to monopolists’ facilities, see John Thorne, *A Categorical Rule Limiting Section 2 of the Sherman Act: Verizon v. Trinko*, 72 U. CHI. L. REV. 289, 296 (2005), while a strong Harvard School supporter called the decision a “child in a china shop of Section 2” which elevated “business freedom” above the interests of “competition and competitive opportunity.” Eleanor M. Fox, *The Trouble with Trinko*, 52 ANNUAL SPRING MEETING OF THE ANTITRUST SECTION OF THE AMERICAN BAR ASSOCIATION: GENERAL SESSION PROGRAM COURSE MATERIALS 1365, 1369–70 (2004).

resolve the conflicts between the Harvard and Chicago Schools and establish a more balanced theory of antitrust regulation. By adopting this unified approach, the courts and agencies can avoid their confusing swing between the extremes of the Harvard and Chicago Schools. The new approach proposed in this Article will encourage American firms to engage in aggressive competitive conduct beneficial to consumers, while deterring firms from behavior that harms consumers. The approach should also conserve judicial resources and give business executives and practitioners better notice of the types of competitive conduct that will be permitted or precluded.

I. THE BATTLE FOR THE SOUL OF ANTITRUST

Antitrust analysis is now poised at a critical tipping point between the Harvard and Chicago Schools. Neither approach has proven to be effective in regulating competitive conduct. The Harvard School prohibited innovative forms of competition that could have enhanced economic efficiency, while the Chicago School allowed competitors to engage in certain conduct that harmed consumers in many domestic markets. The courts and agencies need to move beyond these two theories and adopt a new approach to antitrust analysis tailored to the competitive landscape of the twenty-first century.

The Harvard School dominated antitrust analysis during the activist era of antitrust enforcement that extended from the middle of the twentieth century to the 1970s. By the late 1980s, however, the Chicago School revolutionized the approach to antitrust in the federal courts and enforcement agencies. Under the Chicago School's hegemony, the courts and agencies now must engage in an empirical analysis of actual competitive effects before ruling on the legality of specific competitive conduct.

A. The Harvard School

In the middle of the twentieth century, Harvard economists such as Edward Chamberlain,¹⁰ Edward Mason,¹¹ and Joe Bain¹² argued that an industry's structure, that is, the number of firms in the market and their relative sizes, determines how effectively firms will perform in that market.¹³ Beginning in the 1960s, Harvard professors applied the structural approach of the Harvard economists to antitrust

10. See EDWARD CHAMBERLAIN, *THE THEORY OF MONOPOLISTIC COMPETITION* (1933).

11. See EDWARD S. MASON, *ECONOMIC CONCENTRATION AND THE OLIGOPOLY PROBLEM* (1964).

12. See JOE S. BAIN, *INDUSTRIAL ORGANIZATION* (2d ed. 1959); JOE S. BAIN, *BARRIERS TO NEW COMPETITION: THEIR CHARACTER AND CONSEQUENCES IN MANUFACTURING INDUSTRIES* (1956).

13. The Harvard economists were heavily influenced by the classic theory of structuralism set forth by Augustin Cournot in 1838. AUGUSTIN COURNOT, *RESEARCHES INTO THE MATHEMATICAL PRINCIPLES OF THE THEORY OF WEALTH* (Nathaniel T. Bacon trans., Macmillan Publishers 1897) (1838). Cournot hypothesized that oligopolists would calculate their output so that, together, they would be able to achieve a profit-maximizing price approaching the monopoly level. John E. Lopatka, *Solving the Monopoly Problem: Turner's Try*, 41 *ANTITRUST BULL.* 843, 862 (1996). For a current theory of structuralism, see F.M. SCHERER & DAVID ROSS, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* (3d ed. 1990).

theory. These scholars argued that, when markets are concentrated, firms are more likely to engage in anticompetitive conduct.¹⁴ Harvard School academics pointed out that, when Congress enacted the Sherman and Clayton Acts, it was concerned with the growing economic and political power of trusts such as the Standard Oil Company and United States Steel Corporation. In construing the broad language of the Sherman and Clayton Acts, the courts should be guided by Congress's desire to protect individual competitors from the market power wielded by large firms.¹⁵

Harvard scholars opposed market concentration, even when it might lower costs and prices, thereby benefiting consumers.¹⁶ Harvard scholarship convinced many judges to presume the illegality of any conduct by firms with market power, regardless of its effect on consumers. For example, in 1945, in *United States v. Aluminum Co. of America*,¹⁷ Judge Learned Hand found Alcoa liable for monopolizing the aluminum manufacturing market.¹⁸ Taking advantage of economies of scale by expanding its manufacturing capacity to meet increasing demand, Alcoa was able to deliver quality products to customers at low prices.¹⁹ Judge Hand's decision penalized Alcoa simply for engaging in aggressive competition that benefitted consumers.

The Harvard School approach had a similar effect in deterring consumer-friendly mergers. In 1963, the government persuaded the Supreme Court to preclude a merger between two banks in the Philadelphia area that together held only thirty percent of the relevant market. The Court deemed irrelevant the defendants' arguments that the merger might have enhanced their ability to provide better services to their Philadelphia customers.²⁰

The Harvard School approach had many advantages. If antitrust analysis under the Harvard School was not perfect, at least it was certain. The courts were able to indulge in a presumption of illegality for many types of conduct without engaging in a complicated analysis of the economic circumstances in the relevant market. Since the

14. See Hovenkamp, *supra* note 2, at 920 (“[T]he Harvard School historically tend[ed] to emphasize a strong relationship between structure and performance . . .”).

15. See Thomas J. DiLorenzo, *The Origins of Antitrust: An Interest-Group Perspective*, 5 INT'L REV. L. & ECON. 73, 74–76 (1985) (arguing that the Sherman Act was designed to transfer wealth from big business to small merchants and farmers); Herbert Hovenkamp, *Distributive Justice and the Antitrust Laws*, 51 GEO. WASH. L. REV. 1, 16–17 (1982) (stating that Congress was concerned with distributing economic and political power more widely); David Millon, *The Sherman Act and the Balance of Power*, 61 S. CAL. L. REV. 1219, 1287–92 (1988) (viewing the original purpose of the Sherman Act as the protection of democratic institutions from concentrated economic power).

16. For example, Donald Turner argued in a 1962 article in the *Harvard Law Review* that, since concentrated markets were so inefficient, Congress should pass legislation allowing the courts to dismember large firms, despite their ability to achieve economies of scale and lower producers' costs. Donald F. Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 HARV. L. REV. 655, 663–73 (1962).

17. 148 F.2d 416 (2d Cir. 1945).

18. *Id.*

19. Donald I. Baker, *Government Enforcement of Section 2*, 61 NOTRE DAME L. REV. 898, 905 (1986).

20. *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 371 (1963) (“[A] merger the effect of which ‘may be substantially to lessen competition’ is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial.”).

outcomes of trials were so predictable, business executives understood the type of conduct they should avoid. Firms in concentrated industries were effectively deterred from transactions that increased concentration levels in the relevant market. The Harvard School approach, however, also had serious disadvantages. Harvard School jurists were too quick to find fault with aggressive competition. The courts and agencies prevented large firms from engaging in competitive conduct that could have benefited consumers and would have been perfectly permissible for firms with lower market shares.

B. The Chicago School

By the late 1960s, a group of scholars at the University of Chicago had set forth an opposing theory of antitrust analysis in a series of articles and treatises. These scholars found no evidence that Congress's intent under the antitrust laws was to protect individual competitors against large firms' exercise of market power. In a 1966 law review article, Robert Bork argued that the antitrust laws were designed simply to increase the efficiency of the American economy.²¹ Bork defined economic efficiency in terms of conditions that maximized wealth, and he equated wealth enhancement with "consumer welfare," meaning lower costs, reduced prices, and increased output of products and services desired by customers.²² Bork believed that "[t]he only legitimate goal of American antitrust is the maximization of consumer welfare."²³ All other possible goals of the antitrust laws, including the protection of small business from the power of large firms, were irrelevant.²⁴

Chicago School academics argued that the Harvard School misjudged the ways in which firms continue to compete, even when they have relatively few rivals.²⁵ Chicago School scholars believed that markets were likely to correct against any competitive imbalances on their own, without intervention by antitrust regulators.²⁶ Indeed, the courts and government agencies usually made poor decisions in attempting to regulate economic conduct; they were simply not capable of devising regulatory solutions that were more effective than the natural workings of the marketplace. Since markets are self-correcting in any event, the courts and enforcement agencies should only intervene in the competitive process when it was clear, after thorough study, that anticompetitive conduct was threatening consumer welfare.²⁷

21. See Robert Bork, *Legislative Intent and the Policy of the Sherman Act*, 9 J.L. & ECON. 7 (1966).

22. *Id.*

23. BORK, *supra* note 3, at 51; see also Frank H. Easterbrook, *Workable Antitrust Policy*, 84 MICH. L. REV. 1696, 1703 (1986) ("However you slice the legislative history, the dominant theme is the protection of consumers from overcharges.").

24. Bork, *supra* note 21, at 7.

25. See Hovenkamp, *supra* note 2, at 921 (stating that the Chicago School assumes that "[e]ven in concentrated markets, firms will naturally try to find ways of competing with each other").

26. The Chicago School scholars asserted that markets should be given a free rein because the greatest good comes from "the natural tendency of firms . . . to be efficient." Eleanor Fox, *The Battle for the Soul of Antitrust*, 75 CAL. L. REV. 917, 917 (1987).

27. See Herbert Hovenkamp, *Post-Chicago Antitrust: A Review and Critique*, 2001 COLUM.

The Chicago School began to impact antitrust case law in the late 1970s, when several Chicago School scholars, including Robert Bork, Frank Easterbrook, and Richard Posner, were appointed to the federal bench.²⁸ By the early 1990s, the Chicago School had completed a revolution in antitrust analysis. No longer willing to indulge a presumption of illegality for many types of competitive conduct, the courts and agencies insisted on proof of specific anticompetitive effects before finding defendants' conduct illegal. It was insufficient for a plaintiff to prove that an individual firm or a group of competitors possessed significant market power. In addition, plaintiffs would have to demonstrate, through empirical evidence, that the conduct at issue harmed consumers by increasing prices or decreasing output.

This approach led the courts and agencies to become more lenient in allowing firms to acquire and exercise market power. In 1979, the Supreme Court refused to presume the illegality of a price-fixing agreement among a group of musical composers;²⁹ in 1997, the Federal Trade Commission (FTC) permitted the Boeing Company to acquire the McDonnell Douglas Corporation in a transaction that gave Boeing and Airbus a duopoly in the worldwide market for the manufacture of commercial airliners;³⁰ and in 2002, the Bush Administration settled the Department of Justice's long-standing monopolization case against Microsoft by consenting to a final judgment that allowed the company to continue to leverage its monopoly in the computer operating system market into related markets for word processing, Internet access, video and audio services, and instant messaging.³¹

Ultimately, the Chicago School overreacted to the shortcomings of the Harvard School, and in so doing created its own problems. Chicago School adherents never acknowledged an inherent conflict in their approach to antitrust regulation. Chicago School economists believed that the courts and agencies were ineffective in regulating competitive conduct.³² Yet in denying the presumptions of illegality used by the Harvard School, the Chicago School left judges, juries, and administrative agencies with even more responsibility in antitrust cases. Henceforth, fact finders would have to confirm the specific economic effects of competitive conduct on consumers. Such decisions ultimately proved to be beyond the competence of judicial and administrative fact finders. Most judges, juries, and government regulators are simply not capable of deciding complex economic issues. Indeed, even economists disagree about how such decisions should be made.³³ If such decision making is difficult for economists, it is

BUS. L. REV. 257, 269 ("Chicago School antitrust writers developed well-reasoned arguments that in the long run markets tend to correct their own imperfections . . . and that tribunals would be well advised to study practices much more thoroughly before deciding that intervention is appropriate.").

28. See *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210 (D.C. Cir. 1986) (Bork, J.); *Polk Bros. v. Forest City Enters.*, 776 F.2d 185 (7th Cir. 1985) (Easterbrook, J.); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742 (7th Cir. 1982) (Posner, J.).

29. *Broad. Music, Inc. v. CBS*, 441 U.S. 1 (1979) (refusing to apply the per se rule to agreement by musical composers to license their copyrighted compositions at identical prices).

30. See *In re Boeing Co.*, [1997–2001 FTC Complaints & Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 24,295 (July 1, 1997).

31. See Thomas A. Piraino, Jr., *A Proposed Antitrust Approach to High Technology Competition*, 44 WM. & MARY L. REV. 65, 119–23 (2002) [hereinafter Piraino, Jr., *High Technology Competition*] (describing deficiencies in Microsoft Final Judgment).

32. See *supra* notes 25–26 and accompanying text.

33. See Easterbrook, *supra* note 3, at 153 ("If you assembled [twelve] economists and gave

almost impossible for lay juries, administrators, and judges who are not trained in economics.³⁴

By the late 1980s, the Chicago School had destroyed the old antitrust verities. No longer could business executives be sure of the types of transactions that might lead to antitrust liability. Faced with the impossibility of making the empirical economic decisions required by the Chicago School, fact finders rendered a series of conflicting decisions in antitrust cases. These decisions confused antitrust practitioners and business executives as to the applicable standards of conduct under the antitrust laws. As a result, the antitrust laws lost their deterrent effect. Firms miscalculated by engaging in harmful conduct whose illegality would have been clear under the Harvard School approach.³⁵

II. THE PRINCIPAL CASES REFLECTING THE HARVARD/CHICAGO SCHOOL CONFLICT

The next three Parts describe how the Harvard/Chicago School conflict has played out in the courts' and agencies' approach to the most significant antitrust issues of the last forty years: restraints of trade, mergers and joint ventures, and monopoly conduct. As the Chicago School has triumphed over the Harvard School approach in each of those areas, the courts' and agencies' analysis of competitive conduct has inevitably become more complex, antitrust decisions have become more confusing, and business executives have found it increasingly difficult to understand how to tailor their conduct to comply with the antitrust laws.

A. *The Restraint of Trade Cases*

Section 1 of the Sherman Act prohibits any "conspiracy, in restraint of trade."³⁶ For most of the twentieth century, the federal courts have assumed that they must choose between two opposite methods of analyzing restraints of trade under section 1: a "per se rule" that deems certain conduct illegal on its face,³⁷ or a "rule of reason" that

them all available data about a business practice, plus an unlimited computer budget, you would not soon (or ever) get unanimous agreement about whether the practice promoted consumers' welfare or economic efficiency more broadly defined.").

34. See *Arizona v. Maricopa County Med. Soc'y*, 457 U.S. 332, 343 (1982) ("Judges often lack the expert understanding of industrial market structures and behavior to determine with any confidence a practice's effect on competition."); *United States v. Topco Assocs.*, 405 U.S. 596, 609–12 (1972) ("[C]ourts are of limited utility in examining difficult economic problems. . . . [They are] ill-equipped for such decision making [and cannot] analyze, interpret, and evaluate the myriad of competing interests and the endless data that would surely be brought to bear on such decisions."). As Professor Sullivan has concluded, "economics does not comprehend enough and law, without extreme transformations in its own structure, cannot adequately deal with all that economics does comprehend." LAWRENCE A. SULLIVAN, *HANDBOOK OF THE LAW OF ANTITRUST* § 2, at 10 (1977).

35. See Piraino, Jr., *Reconciling*, *supra* note 6, at 709 ("[D]efendants continue to engage in questionable competitive practices.").

36. 15 U.S.C. § 1 (2000 & Supp. IV 2004).

37. The per se rule constitutes an irrebutable presumption of illegality. Herbert Hovenkamp has concluded that the conduct is considered per se illegal "because no one has made a plausible argument that the action is competitive, and its anticompetitive potential seems fairly obvious." Herbert Hovenkamp, *Antitrust Policy, Restricted Distribution, and the Market for Exclusionary*

inquires into all conceivable circumstances before determining the legality of a particular restraint.³⁸ The per se and rule of reason approaches are so divergent that a court's choice of one analysis over another has usually determined the outcome of an antitrust case. Traditionally, the rule of reason meant a decision for the defendant and the per se rule a victory for the plaintiff.³⁹ Because the dividing line between per se and rule of reason analysis is so critical, a debate has raged for decades over the proper scope of each approach. The Harvard and Chicago Schools have been aligned on opposite sides of the per se/rule of reason divide.

1. Ascendancy of the Per Se Rule

Courts and agencies following the Harvard School found a per se approach attractive because it greatly enhanced the effectiveness of antitrust enforcement. Per se standards reduced the time and expense of antitrust cases, provided clear guidance to businesses, and effectively deterred anticompetitive conduct.⁴⁰ The Supreme Court first used a per se approach early in the twentieth century in price-fixing cases, where the anticompetitive potential of the arrangements was so obvious that the Court could easily dispense with inquiries into market conditions or the defendants' justifications.⁴¹

No new per se classifications were established until the late 1950s, when the Harvard School first began to influence the Supreme Court. By the late 1960s, the Court had applied the per se rule to tying arrangements,⁴² horizontal territorial or

Rights, 71 MINN. L. REV. 1293, 1294–95 n.8 (1987).

38. See *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918) (listing several factors a court should consider before invoking antitrust sanctions). In *Continental T.V., Inc. v. GTE Sylvania, Inc.*, the Supreme Court stated that “[u]nder this rule [of reason], the factfinder weighs all the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition.” 433 U.S. 36, 49 (1977) (citing *Chicago Bd. of Trade*, 246 U.S. at 238).

39. Donald L. Beschle, “*What Never? Well, Hardly Ever*”: *Strict Antitrust Scrutiny as an Alternative to Per Se Antitrust Illegality*, 38 HASTINGS L.J. 471, 501–02 (1987); Joe Sims, *Developments in Agreements Among Competitors*, 58 ANTITRUST L.J. 433, 435 (1989). The rule of reason has been viewed as “a euphemism for an endless economic inquiry ending in a defense verdict.” Thomas C. Arthur, *A Workable Rule of Reason: A Less Ambitious Antitrust Role for the Federal Courts*, 68 ANTITRUST L.J. 337, 337 (2000) (quoting Maxwell M. Blecher, *The Schwinn Case—An Example of a Genuine Commitment to Antitrust Law*, 44 ANTITRUST L.J. 550, 553 (1975)). Indeed, plaintiffs have so rarely prevailed in rule of reason cases that the approach has been equated with a rule of per se legality. See William F. Baxter, *The Viability of Vertical Restraints Doctrine*, 75 CAL. L. REV. 933, 949 (1987) (“As a practical matter, current case law treats all . . . [nonprice] vertical restraints as lawful per se [under the rule of reason].”).

40. The courts have concluded that the litigation efficiencies provided by the per se rule justify its occasional overbreadth. For example, in *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 344 (1982), the Supreme Court stated: “As in every rule of general application, the match between the presumed and the actual is imperfect. For the sake of business certainty and litigation efficiency, we have tolerated the invalidation of some agreements that a fullblown inquiry might have proved to be reasonable.”

41. See *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) (horizontal price fixing); *United States v. Trenton Potteries Co.*, 273 U.S. 392 (1927) (horizontal price fixing); *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911) (resale price fixing).

42. See *N. Pac. Ry. v. United States*, 356 U.S. 1 (1958).

customer allocations,⁴³ and group boycotts.⁴⁴ The Harvard School “never reached its peak”⁴⁵ in 1967 with *United States v. Arnold, Schwinn & Co.*,⁴⁶ which extended the per se rule to nonprice vertical restrictions imposed by a supplier on its distributors.

By making so many restraints illegal on their face, the activist per se approach insured that American firms would avoid conduct that could harm consumers.⁴⁷ The dominance of the per se rule, however, also caused significant problems. The per se approach was rigid and formalistic. By mechanically precluding certain conduct without any consideration of its economic effects, the rule deterred beneficial, as well as pernicious, business practices. For example, the nonprice vertical restraints condemned by the Supreme Court in *Schwinn* arguably promoted competition between retail brands.⁴⁸ During the 1970s, Chicago School scholars began to criticize the per se rule for its failure to consider the potential beneficial effects of such restraints.⁴⁹

2. Increased Use of the Rule of Reason

After the high watermark of per se analysis in the *Schwinn* case, the federal judiciary began to take notice of the Chicago School’s criticism of the approach. The most dramatic retreat from per se analysis occurred in 1977 when, in *Continental T.V., Inc. v. GTE Sylvania Inc.*,⁵⁰ the Supreme Court reversed its decision in *Schwinn* and decided that nonprice vertical restrictions should be judged by the rule of reason.

At issue in *Sylvania* was a contractual requirement that distributors sell Sylvania television sets only from authorized locations.⁵¹ The Court recognized that, although this requirement limited competition among the distributors in the resale of Sylvania televisions (“intra-brand competition”), it also promoted competition with other brands of television sets (“inter-brand competition”) by inducing Sylvania distributors to make the investments necessary to provide more services to customers.⁵² Drawing heavily upon the scholarship of Richard Posner,⁵³ the Court concluded that a rule of reason,

43. See *United States v. Topco Assocs.*, 405 U.S. 596 (1972); *United States v. Sealy, Inc.*, 388 U.S. 350 (1967).

44. See *Klor’s, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959).

45. Earl L. Pollock, *The “New Antitrust”—Its Implications for the Practitioner*, 54 ANTITRUST L.J. 51, 52 (1985).

46. 388 U.S. 365 (1967), *overruled by* *Cont’l T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

47. See *Topco*, 405 U.S. at 609 n.10 (“Without the *per se* rules, businessmen would be left with little to aid them in predicting in any particular case what courts will find to be legal and illegal under the Sherman Act.”).

48. See Richard A. Posner, *Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions*, 75 COLUM. L. REV. 282, 297 (1975) (noting that *Schwinn*’s application of the per se rule to vertical restraints prevents the consideration of beneficial effects on interbrand competition, such as improved point-of-sale services).

49. See, e.g., *id.* (criticizing application of per se rule to resale restraints).

50. 433 U.S. 36 (1977).

51. *Id.* at 40–41.

52. *Id.* at 54–55.

53. *Id.* at 36, 50–57 (citing RICHARD A. POSNER, ANTITRUST: CASES, ECONOMIC NOTES, AND OTHER MATERIALS 134 (1974); Posner, *supra* note 48, at 283, 285, 287–88).

rather than a per se, approach was appropriate in light of the potential economic benefits of the location clause imposed by *Sylvania*.⁵⁴

Sylvania established the foundation for modern antitrust's reliance on empirical economic evidence. After *Sylvania*, the federal courts had to confront a new paradigm: henceforth, they could not indulge in any presumptions of illegality under the antitrust laws that were not supported by economic facts. Other decisions favoring the rule of reason followed on the heels of *Sylvania*. Indeed, the history of antitrust analysis since *Sylvania* has been, with only a few exceptions, a steady erosion of the per se approach and an expanded use of the rule of reason.

In 1979 the Supreme Court indicated for the first time that it would be willing to apply a rule of reason analysis to a price-fixing arrangement. The Court held in *Broadcast Music, Inc. v. CBS*⁵⁵ ("*BMP*") that a group of copyright holders did not commit a per se violation of the Sherman Act when they fixed a common price for the licensing of their musical compositions.⁵⁶ The Court pointed out that, instead of engaging in a rigid per se analysis, fact finders should initially consider whether a restraint "appears to be one that would always or almost always tend to restrict competition and decrease output."⁵⁷ The Court concluded that the common license allowed the copyright holders to market their compositions more efficiently and therefore should be analyzed under the rule of reason.⁵⁸

During the 1980s, the Supreme Court extended the rule of reason to other horizontal agreements with potential efficiency justifications.⁵⁹ The lower federal courts have followed the Supreme Court's lead in limiting applications of the per se rule and expanding the use of the rule of reason. Convinced by the Chicago School of the dangers of an absolute approach, federal judges have shown an increased willingness to consider defendants' justifications for practices formerly considered illegal on their face.⁶⁰

3. Deficiencies in Rule of Reason Analysis

As a result of the revolution in antitrust economics that occurred within the federal judiciary in the 1980s, the rule of reason is now the dominant form of analysis in Sherman Act cases. However, the Chicago School has been unable to construct a

54. *Sylvania*, 433 U.S. at 54–57.

55. 441 U.S. 1 (1979).

56. *Id.* at 24–25.

57. *Id.* at 19–20.

58. *Id.* at 20.

59. *See* *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447 (1986) (using the rule of reason to analyze refusal by an association of dentists to supply patient x-rays to insurance companies seeking to evaluate benefit claims); *NCAA v. Bd. of Regents*, 468 U.S. 85 (1984) (using the rule of reason to analyze the NCAA's limitations on the number of times its member college sports teams could appear on television).

60. *See, e.g.,* *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210 (D.C. Cir. 1986) (allowing requirement that van lines not deal with other moving companies); *Nat'l Bancard Corp. v. VISA U.S.A., Inc.*, 779 F.2d 592 (11th Cir. 1986) (upholding interchange fee among members of Visa credit card system); *Polk Bros. v. Forest City Enters.*, 776 F.2d 185 (7th Cir. 1985) (upholding noncompetition covenant).

formulation of the rule of reason that allows for effective decision making. Most judicial discussion of the rule of reason standard has occurred in the Supreme Court and federal appellate courts, where the analysis has been confined to the issue of whether a rule of reason or per se standard should apply.⁶¹ Once the courts have decided that the rule of reason is appropriate, they have usually neglected to explain how it should be applied on remand. Most courts' definitions of the rule have not progressed beyond a requirement that the trier of fact consider all the circumstances surrounding a restraint before condemning it.⁶² The courts simply quote "a long list of factors without any indication of priority or weight to be accorded each factor."⁶³

The current rule of reason standard provides little guidance to litigants, judges, or juries.⁶⁴ Antitrust enforcement relies primarily on self-policing by the business community, but voluntary compliance is impossible when antitrust standards are unclear. These uncertain standards can lead both to under-deterrence and over-deterrence. Not only will firms miscalculate and risk anticompetitive conduct that they believe to be lawful; they may also avoid procompetitive behavior under the mistaken assumption that it can be attacked successfully.⁶⁵ Since the outcome of cases is so difficult to predict, both plaintiffs and defendants miscalculate. Plaintiffs bring unjustified suits that waste judicial and private resources, and defendants continue to engage in questionable competitive practices. Under the courts' current approach, the antitrust laws are capable of neither encouraging beneficial conduct nor deterring anticompetitive practices. In order to insure an effective antitrust policy, the federal courts must adopt a clearer method of analyzing restraints of trade under section 1 of the Sherman Act.

B. Merger and Joint Venture Cases

Mergers and joint ventures are evaluated under section 7 of the Clayton Act, which prohibits any such transactions that may "substantially lessen competition or tend to create a monopoly."⁶⁶ Until the mid-1970s, the federal courts and agencies followed a Harvard School approach to mergers and joint ventures. This approach caused the courts and agencies to presume illegality of any mergers or joint ventures among firms that held substantial shares of the relevant market. Currently, however, the courts and agencies follow a Chicago School approach that allows them to consider factors other

61. See *supra* notes 50–60 and accompanying text.

62. Mark Crane, *The Future Direction of Antitrust*, 56 ANTITRUST L.J. 3, 14 (1987).

63. Robert Pitofsky, *The Sylvania Case: Antitrust Analysis of Non-Price Vertical Restrictions*, 78 COLUM. L. REV. 1, 34 (1978).

64. See Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1, 12–13 (1984) ("When everything is relevant, nothing is dispositive. Any one factor might or might not outweigh another, or all of the others, in the factfinder's contemplation. The formulation offers no help to businesses planning their conduct.").

65. *Id.*

66. 15 U.S.C. § 18 (2002). Because the parties to the joint venture retain their independent existence and continue to compete with each other outside the scope of the venture, joint ventures may also be evaluated under the "restraint of trade" provisions of section 1 of the Sherman Act.

than the parties' market shares before determining the legality of a merger or joint venture.

1. The Harvard School Approach

Harvard School scholars believed that mergers and joint ventures which substantially increased concentration levels in the relevant market made it easier for the remaining firms to engage in anticompetitive conduct.⁶⁷ Either the merged entity acting alone (defined as "unilateral effects") or the merged entity collaborating with the remaining firms in the market (defined as "coordinated effects") could limit competition by charging higher prices, lowering output, reducing product quality, or slowing innovation.⁶⁸ Under the Harvard School approach, the courts and enforcement agencies defined a relevant market, assigned market shares to each of the competitors in the market, and presumed the illegality of transactions that increased market concentration levels beyond particular thresholds. As the Supreme Court noted, "market definition generally determine[d] the result of the case."⁶⁹

Under the Harvard School approach, the courts and agencies applied the market share presumption of illegality regardless of whether the transaction at issue had the potential to lower costs or prices or otherwise benefit consumers. For example, in *Brown Shoe Co. v. United States*,⁷⁰ the Supreme Court considered the legality of a merger between two shoe manufacturers. The Court conceded that the merger would allow the integrated companies to "market their own brands at prices below those of competing independent retailers."⁷¹ Despite this advantage to consumers, the Court

67. The Harvard School antitrust treatise supported prima facie illegality for mergers in which the parties had an aggregate share of thirteen to fourteen percent of the relevant market. See 4 PHILLIP AREEDA & DONALD F. TURNER, ANTITRUST LAW ¶ 915, at 83 (1980).

68. For a unilateral effects case, see *United States v. Mercy Health Services*, 902 F. Supp. 968, 975 (N.D. Iowa 1995), *vacated as moot*, 107 F.3d 632 (8th Cir. 1997), stating that "courts have focused on whether the merger will cause the merged entity to have enough market power such that it could profitably increase prices." For a coordinated effects case, see *Hospital Corp. of America v. FTC*, 807 F.2d 1381, 1386 (7th Cir. 1986), stating that "the worry is that [the merger] may enable the acquiring firm to cooperate (or cooperate better) with other leading competitors on reducing or limiting output, thereby pushing up the market price."

69. *Eastman Kodak Co. v. Image Technical Servs.*, 504 U.S. 451, 469 n.15 (1992). The Supreme Court has followed this highly structured approach to the analysis of mergers since the early 1960s. See *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 363 (1963) (establishing the principle that the illegality of a merger can be presumed from a substantial market share concentration level); *Brown Shoe Co. v. United States*, 370 U.S. 294, 335 (1962) ("[T]he proper definition of the market is a 'necessary predicate' to an examination of the competition that may be affected by the . . . merger."). Beginning in 1968, the U. S. Department of Justice (DOJ) and the FTC published guidelines for merger enforcement that followed the Supreme Court's lead and adopted presumptions of illegality based on the market shares of the parties to a merger. Merger Guidelines, 4 Trade Reg. Rep. (CCH) ¶¶ 13,101–103 (Mar. 18, 1968). The most recent guidelines ("Merger Guidelines"), issued by the DOJ and FTC in 1992, establish a formula called the Herfindahl-Hirschman Index (HHI) to calculate the specific market share concentration levels at which mergers should be presumed illegal.

70. 370 U.S. 294 (1962).

71. *Id.* at 344.

invalidated the merger, pointing out that it was more important to promote Congress's objective of protecting small business against potential abuses of power by larger firms: "[W]e cannot fail to recognize Congress'[s] desire to promote competition through the protection of viable, small, locally owned businesses. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets."⁷²

2. The Chicago School Approach

By the mid-1970s, Chicago School scholars began to criticize the federal courts' market share presumption of illegality for mergers and joint ventures. The presumption, these scholars asserted, precluded many efficiency-enhancing transactions.⁷³

Responding to the concerns of the Chicago School, the Supreme Court, in the mid-1970s, began to open up merger and joint venture analysis to a consideration of factors other than market share concentration statistics. In 1974, in *United States v. General Dynamics Corp.*,⁷⁴ the Court, in a marked departure from its earlier antitrust jurisprudence, held that a merger could not be deemed illegal simply because the defendants held high market shares. The Court expressed a willingness to consider conditions that might affect the future market shares of the merging parties.⁷⁵ *General Dynamics* paved the way to a more sophisticated approach to merger and joint venture analysis. After *General Dynamics*, the courts and agencies became willing to consider defendants' arguments that their current market shares inaccurately predicted a transaction's probable effect on future competition.⁷⁶

In a few recent cases, the courts and agencies have relied on *General Dynamics* to discount the future market share of financially troubled companies.⁷⁷ As the District of

72. *Id.* See also *Standard Oil Co. v. United States*, 337 U.S. 293, 318–19 (1949) (Douglas, J., dissenting) (showing concern for “growth in bigness”).

73. For example, Richard Posner argued that there was no basis for automatic judicial intervention against a merger where the combined market share of the four largest firms in the market was less than sixty percent. POSNER, *supra* note 3, at 112.

74. 415 U.S. 486 (1974).

75. *General Dynamics* involved a merger between two coal companies. The Court pointed out that most of the coal companies' production was committed under long-term supply contracts. *Id.* at 501–02. The defendants' past market shares did “not . . . necessarily give a proper picture of [their] future ability to compete” because other companies with large supplies of coal not already under contract would likely be able to obtain a greater market share in future negotiations. *Id.* at 501.

76. See *Merger Guidelines*, *supra* note 69, at 20,573–76 (“Market share concentration data provide only the starting point for analyzing the competitive impact of a merger. Before determining whether to challenge a merger, the Agency also will assess the other market factors that pertain to competitive effects, as well as entry, efficiencies and failure.”).

77. See *United States v. Int'l Harvester Co.*, 564 F.2d 769, 773–75 (7th Cir. 1977) (allowing merger between International Harvester and tractor manufacturer on grounds that manufacturer would not have sufficient financial resources to compete effectively in future); *In re Boeing Co.*, [1997–2001 FTC Complaints & Orders Transfer Binder] Trade Reg. Rep. (CCH) ¶ 24,295, at 24,123–24 (July 1, 1997) (allowing merger of Boeing and McDonnell Douglas on grounds that, due to its financial distress, McDonnell Douglas would “no longer constitute a

Columbia Circuit recognized in *United States v. Baker Hughes, Inc.*,⁷⁸ “evidence of market concentration simply provides a convenient starting point for a broader inquiry into future competitiveness.”⁷⁹

Despite the courts’ and agencies’ willingness to consider economic factors that may reduce merging parties’ future market shares, the Chicago School has not been able to convince antitrust regulators to fully recognize economic efficiencies as a mitigating factor in merger cases. Economists have recognized that mergers may achieve economies of scale, synergies, or cost savings that will allow the parties to offer lower prices to consumers after the completion of the transaction. The courts and agencies, however, have not yet been willing to consider such efficiencies as a defense to an otherwise illegal merger.⁸⁰ Some commentators have ascribed the courts’ and agencies’ reluctance to recognize an efficiencies defense to the difficulty of confirming the legitimacy of defendants’ efficiency claims.⁸¹

C. Monopoly Cases

Under the Harvard School approach, the courts and agencies were willing to preclude rather benign conduct by firms that were only attempting to obtain or maintain a monopoly position in the relevant market. However, as the courts and agencies began to adopt the empirical approach of the Chicago School, they recognized that firms should not be punished simply for obtaining monopoly power. Indeed, firms often obtained such power because they were the most successful in delivering the types of products and services desired by consumers. Thus, under the Chicago School, the courts and agencies became unwilling to find monopolists liable

meaningful competitive force” in the relevant market). *See also* *FTC v. Univ. Health, Inc.*, 938 F.2d 1206, 1221 (11th Cir. 1991) (“[W]e view *General Dynamics* as standing for the unremarkable proposition that a defendant may rebut the government’s prima facie case by showing that the government’s market share statistics overstate the acquired firm’s ability to compete in the future . . .”).

78. 908 F.2d 981 (D.C. Cir. 1990).

79. *Id.* at 984.

80. The Supreme Court has consistently refused to recognize an efficiencies defense for mergers that substantially increase concentration levels in a relevant market. *See* *FTC v. Proctor & Gamble Co.*, 386 U.S. 568, 580 (1967) (stating that “possible economies cannot be used as a defense to illegality” in section 7 merger cases); *United States v. Philadelphia Nat’l Bank*, 374 U.S. 321, 371 (1963) (“[A] merger the effect of which ‘may be substantially to lessen competition’ is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial.”). For their part, the lower federal courts have never found that efficiencies should save a merger that otherwise would have been deemed anticompetitive. *See* *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 720 (D.C. Cir. 2001) (discussing the history of the efficiencies defense). The Merger Guidelines of the FTC and DOJ have provided for an efficiencies defense since 1997, Merger Guidelines, *supra* note 69, ¶ 13,104, at 20,573-11 to-13, but the provision has not caused the agencies to recognize an efficiencies defense in their enforcement actions. *See* David Balto, *The Efficiency Defense in Merger Review: Progress or Stagnation?*, ANTITRUST, Fall 2001, at 74, 79 (describing the FTC’s neglect of efficiency issues).

81. *See, e.g.*, Robert Pitofsky, *Antitrust Policy in a Clinton Administration*, 62 ANTITRUST L.J. 217, 221 (1993).

under the Sherman Act unless they had engaged in some type of improper competitive conduct.

1. The Harvard School Approach

Section 2 of the Sherman Act precludes monopolization, or attempts to monopolize, by individual firms.⁸² Harvard School scholars have assumed that poor economic performance is inevitable in monopoly markets.⁸³ Until the late 1960s, the federal courts and enforcement agencies followed a Harvard School approach in section 2 cases, and they became willing to find monopolists liable, even if they had not engaged in any exclusionary behavior.⁸⁴

Once a defendant was found to possess monopoly power, the courts and agencies precluded any conduct having the purpose or effect of protecting or increasing that power. “It was sufficient that a defendant evidenced a general intent to obtain or maintain its monopoly power, [that is], that it chose to do the acts that led to the establishment or perpetuation of its monopoly.”⁸⁵ Commentators have pointed out that such a standard “is hardly a requirement at all It is almost inconceivable that [a monopolist] can possess [monopoly] power . . . without taking some volitional act that may fairly be characterized as an exercise of its power.”⁸⁶

2. The Chicago School Approach

Chicago School scholars believe that monopolists should not be liable simply for engaging in conduct that is a natural consequence of their market power. The Chicago School assumes that firms usually acquire monopoly power because of their ability to provide consumers with superior products at low prices. Punishing monopolists simply

82. 15 U.S.C. § 2 (2000).

83. See *supra* notes 10–19 and accompanying text.

84. The 1978 version of the Harvard antitrust treatise argued that monopolies should be dismembered, even if they had not engaged in identifiable anticompetitive conduct. See 3 PHILLIP AREEDA & DONALD F. TURNER, *ANTITRUST LAW* ¶ 620c, at 45–47 (1978).

85. Thomas A. Piraino, Jr., *Identifying Monopolists' Illegal Conduct Under the Sherman Act*, 75 N.Y.U. L. Rev. 809, 829 (2000) [hereinafter Piraino, Jr., *Identifying Monopolists*].

86. Maxwell M. Blecher & Consuelo S. Woodhead, *Bigness and Badness: A Review of the Requirement of “Deliberateness” in Monopolization*, 10 Sw. U.L. Rev. 117, 119 (1978). In the 1945 case *United States v. Aluminum Co. of America* (“Alcoa”), Judge Hand found that Alcoa illegally used its monopoly power simply by expanding its aluminum production capacity to meet increasing consumer demand. 148 F.2d 416, 431 (2d Cir. 1945); See Baker, *supra* note 19, at 905–06 (“Alcoa seemed to have done what we ask of a competitor in a competitive market—keep prices and profits down, stimulate demand, and be there ready to meet that demand on reasonable terms.”); John G. McGee, *Why Not “Deregulation” for Antitrust?*, 46 ANTITRUST L. J. 777, 786 (1977) (“[A]ny superior firm trying to drive price down to, or closer to, its own cost, runs head-on into *Alcoa* . . .”). Other cases followed *Alcoa's* lead in finding the requisite anticompetitive conduct from a monopolist’s general intent to maintain its position in a market. See, e.g., *United States v. Griffith*, 344 U.S. 100 (1947) (finding section 2 violation when motion picture distributors pooled their buying power to obtain lower rates in their royalty agreements with motion picture producers).

for exercising their market power would discourage firms from competing aggressively to meet consumers' needs.⁸⁷

The Supreme Court began to take a more lenient Chicago School approach to monopoly conduct in the late 1960s, in the case of *United States v. Grinnell Corp.*⁸⁸ Grinnell, a manufacturer of central station alarm services, had acquired many of its major competitors and had engaged in a series of geographic and product market allocation agreements.⁸⁹ The Supreme Court found little difficulty in inferring a section 2 violation from such conduct.⁹⁰ However, in dicta, the Court set forth a standard that would be used extensively by defendants to avoid liability in later cases. The Court stated that section 2 should only prohibit "the willful acquisition or maintenance of . . . [monopoly] power as distinguished from growth or development as a consequence of a superior product, business acumen, or historical accident."⁹¹ After *Grinnell*, the courts struggled to develop objective standards for determining whether monopoly power resulted from improper willful conduct or from aggressive competition that benefited consumers.

As in restraint of trade, merger, and joint venture cases, the courts' and agencies' decisions in post-Harvard School monopoly cases have failed to provide effective guidelines for business conduct. Indeed, since the *Grinnell* decision, the federal courts have been unable to articulate a consistent means for distinguishing between monopolists' proper and illegal conduct. For example, in certain cases, the Supreme Court has held that a monopolist, absent a legitimate business justification, cannot refuse to do business with a rival,⁹² while in other cases it has neglected to find such a duty to deal.⁹³ The Court has never adequately explained the distinction between these two lines of cases.

The federal courts have also adopted inconsistent standards for monopolists' tying and exclusive dealing arrangements. Under an exclusive dealing arrangement, a firm requires a customer or supplier to deal only with it and not to deal with its competitors.⁹⁴ Despite the anticompetitive effects of monopolists' exclusive dealing arrangements,⁹⁵ the courts have taken a permissive approach to such conduct. The

87. For example, Chicago School commentators have argued that it should not be illegal for monopolists to refuse to deal with their actual or potential rivals. *See, e.g.*, RICHARD A. POSNER, ANTITRUST LAW at 242–44 (2d ed. 2001) (arguing that unconditioned refusals to deal by dominant firms should never be violations of section 2 of the Sherman Act).

88. 384 U.S. 563 (1966).

89. *See id.* at 566–70.

90. *See id.* at 570–71, 576.

91. *Id.* at 570–71.

92. *See Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451 (1992) (illegality of Kodak's refusal to deal with independent service organizations that serviced its photocopiers); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985) (illegality of skiing resort's refusal to continue to cooperate with rival skiing resort in providing "multi-mountain" skiing ticket).

93. *See Verizon Commc'ns., Inc. v. Trinko*, 540 U.S. 398 (2004) (holding that monopoly telephone company had the right to refuse to give full access to its network to rivals).

94. *See* 1 ABA ANTITRUST SECTION, ANTITRUST LAW DEVELOPMENTS, at 169 (3d ed. 1992).

95. For a monopolist, such an arrangement constitutes a particularly effective means of excluding its competitors from the relevant market. By tying up a low-cost supplier or effective reseller, a monopolist can prevent actual or potential competitors from accessing the resources

courts have analyzed such arrangements under the rule of reason, which requires the fact finder to consider, among other things, the percent of the market foreclosed to competitors by the arrangements.⁹⁶ When less than thirty to forty percent of the suppliers or customers in a particular market have been subject to an exclusive dealing arrangement, the courts have been reluctant to find an antitrust violation.⁹⁷ Thus, monopolists can escape liability for an exclusive dealing arrangement simply by demonstrating that they did not foreclose a rival from a substantial percentage of available suppliers or customers.

In tying cases, however, monopolists have had no such defense. Under a tie, a monopolist agrees to sell one product in which it has market power (the tying product), but only on the condition that the buyer also purchases a different (or tied) product in a market in which the monopolist has less power.⁹⁸ Although tying and exclusive dealing arrangements have similar competitive effects,⁹⁹ the federal courts have applied a *per se* approach to tying arrangements. Monopolists repeatedly have been found to engage in illegal tying arrangements simply because of their power in the market for the tying product.¹⁰⁰

D. The Need for a Harvard/Chicago School Synthesis for Antitrust Regulation

The antitrust case law in the federal courts and agencies during the last forty years makes it clear that neither the Harvard nor the Chicago School approach should be used exclusively to analyze competitive conduct. The Harvard School's presumptions

necessary to compete in the monopolized market or in a related market to which it is attempting to extend its monopoly power.

96. See, e.g., *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984) (O'Connor, J., concurring) ("Exclusive dealing is an unreasonable restraint of trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal.").

97. See *id.* at 7, 32 (finding that exclusive contract which foreclosed thirty percent of the market was not illegal); *United States v. Microsoft Corp.*, No. Civ. A. 98-1232, 1998 WL 614485, at *19 (D.D.C. Sept. 14, 1998) (response to motion for summary judgment) (describing forty percent threshold of illegality for exclusive dealing arrangements); *Gonzales v. Insignares*, No. C84-1261A, 1985 WL 2206, at *2 (N.D. Ga. June 27, 1985) (granting summary judgment for defendant when only forty percent of consumers were affected by exclusive arrangement).

98. See *N. Pac. Ry. Co. v. United States*, 356 U.S. 1, 5-7 (1958) (finding that railroad illegally tied sales or leases of real estate to commitment to ship commodities on its system). The Supreme Court has pointed out that the vice of tying arrangements stems from a defendant's ability to exploit "its control over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms." *Jefferson Parish*, 466 U.S. at 12.

99. Like exclusive dealing, tying arrangements can be used by monopolists either to perpetuate their power in the monopolized market or to extend that power into a related market. See, e.g., *Jefferson Parish*, 466 U.S. at 35-36 (O'Connor, J., concurring) (stating that tying is illegal when "power in the market for the tying product is used to create *additional* market power in the market for the *tied* product" (emphasis in original)); *Smithkline Corp. v. Eli Lilly & Co.*, 575 F.2d 1056, 1061-62 (3d Cir. 1978) (holding that bundling of patented and nonpatented products violates section 2).

100. See, e.g., *Jefferson Parish*, 466 U.S. at 17 (stating that large market share is sufficient to prove requisite economic power); *Int'l Salt Co. v. United States*, 332 U.S. 392, 395-96 (1947) (requisite economic power inferred from defendant's use of patent monopoly); *IBM Corp. v. United States*, 298 U.S. 131, 137 (1936) (same).

of illegality deter beneficial competitive conduct. The courts overused the per se rule in restraint of trade cases brought under section 1 of the Sherman Act. It simply made no economic sense for the courts to presume the illegality of certain agreements among competitors that were designed to enhance their efficiency, thereby benefiting consumers.¹⁰¹ In merger and joint venture cases brought under section 7 of the Clayton Act, the Harvard School was too preoccupied with the parties' market power, and it caused courts to overlook the potential efficiencies resulting from the integration of rivals' resources.¹⁰² In monopoly cases under section 2 of the Sherman Act, the Harvard School approach precluded large firms from engaging in aggressive competitive conduct that could have benefited consumers.¹⁰³

The failings of the Harvard School caused the federal courts to reexamine their approach to antitrust regulation. The arguments of the Chicago School scholars for an antitrust regime based on respect for markets, economic efficiency, and consumer welfare resonated with a federal judiciary concerned about the interventionist approach of the Harvard School. However, as in the case of most revolutions, the Chicago School revisions went too far.

When the rule of reason supplanted the per se rule as the dominant approach in restraint of trade litigation, antitrust cases became more complicated and their outcome became more difficult to predict. As a result, antitrust enforcement under section 1 of the Sherman Act lost much of its deterrent effect. Antitrust practitioners were no longer able to advise their clients with certainty of the type of conduct that would be permitted or precluded.¹⁰⁴ The Chicago School's hegemony also increased confusion in merger and joint venture cases. No longer could American firms rely on "bright-line" market share concentration levels as markers of the legality of particular transactions. The federal courts and enforcement agencies introduced efficiencies analysis into merger and joint venture cases without articulating a clear standard for how to balance such effects against the anticompetitive aspects of a transaction. Finally, the Chicago School emphasized that monopolists should not be punished for obtaining their market power as a result of a superior product or business acumen. However, in cases involving monopolists' duty to deal, tying, and exclusive dealing, the more lenient Chicago School approach only confused the standards of conduct for dominant firms.¹⁰⁵

The federal courts and enforcement agencies need to move beyond the Harvard/Chicago School dichotomy to an integrated approach to antitrust regulation. It is possible to combine the clarity of the Harvard School with the economic sophistication of the Chicago School. The next Part describes the first tentative moves by antitrust commentators and the federal courts toward a "post-Chicago" approach to antitrust that combines the best insights of both schools of antitrust analysis.

101. See *supra* notes 48–49 and accompanying text.

102. See *supra* notes 67–72 and accompanying text.

103. See *supra* notes 84–86 and accompanying text.

104. See *supra* notes 64–65 and accompanying text.

105. See *supra* notes 92–100 and accompanying text.

III. MOVING BEYOND THE HARVARD/CHICAGO DICHOTOMY TO A NEW ANTITRUST APPROACH

In recent years, some academics, lower federal courts, and antitrust enforcement agencies have begun to move toward a new “post-Chicago” approach to antitrust. In its recent decision in *California Dental Ass’n v. FTC*,¹⁰⁶ the Supreme Court has indicated that it may also be willing to adopt an antitrust approach that combines the best insights of both the Chicago and Harvard Schools.

A. Post-Chicago Scholarship

There has been some recent movement among antitrust scholars toward a post-Chicago approach that lies between the extremes of the Harvard and Chicago Schools. Herbert Hovenkamp has stated that, in the last twenty years, “the Harvard School has moved rightward, closer to the Chicago position, while at least some Chicago School members have moderated their position to the left.”¹⁰⁷ Post-Chicago School economic literature argues that certain market structures and competitive conduct “are much more likely to have anticompetitive consequences than Chicago School antitrust writers imagined.”¹⁰⁸

The post-Chicago commentators have concluded that Chicago School theories on the perfection of markets are overly simplistic. In reality, markets do not always behave as perfectly as the Chicago School assumes. In many markets, there is no even playing field: competitive information is not equally available to all participants, entry is not possible for new firms, or dominant firms may have gained a position that is impossible to dislodge. Anticompetitive outcomes are more plausible in such markets than the Chicago School concedes, and antitrust intervention is required to correct competitive imbalances.¹⁰⁹

For example, high-technology networks, such as computer operating or telecommunications systems, “are subject to significant ‘network externalities,’ which means that they become more valuable to a particular user as a system gains larger numbers of other users.”¹¹⁰ Microsoft’s “Windows” operating system for personal computers is attractive to users because it has a large installed base and is compatible with many applications programs.¹¹¹ Post-Chicago School scholars have recognized that monopolists such as Microsoft have a unique ability to leverage the appeal of their networks to extend their market power into other markets or to prevent new firms from

106. 526 U.S. 756 (1999).

107. Hovenkamp, *supra* note 2, at 927.

108. Hovenkamp, *supra* note 27, at 270.

109. *See id.* at 279 (“[U]nder a more complex set of assumptions about how a market works, anticompetitive outcomes seem more plausible.”); Marina Lao, *Aspen Skiing and Trinko: Intent and “Sacrifice”*, 73 ANTITRUST L.J. 171, 179 n.50 (2005) (“The Chicago view of exclusionary conduct as rarely effective, and hence implausible, assumes that markets are robust. Market robustness, in turn, assumes few entry barriers and good information, but these assumptions are usually not valid in real markets. If markets are not as robust as Chicagoans assume, then strategic exclusionary behavior is more plausible.”).

110. Hovenkamp, *supra* note 27, at 300.

111. *See United States v. Microsoft Corp.*, 147 F.3d 935, 938 (D.C. Cir. 1998).

entering the market they have already monopolized. Thus, it is appropriate for the courts and agencies to preclude monopolists from engaging in certain types of conduct that may be perfectly legitimate for less dominant firms.¹¹²

B. The Lower Federal Courts' and Agencies' Movement Toward a New Approach

The lower federal courts and enforcement agencies have also begun to move toward an intermediate approach between the extremes of the Harvard and Chicago Schools. This movement has been most evident in restraint of trade cases brought under section 1 of the Sherman Act, where the courts and agencies have become dissatisfied with the per se/rule of reason dichotomy and have begun to adopt other approaches to section 1 conduct. Although well-intentioned, this development has introduced even greater uncertainty into section 1 analysis. The courts and agencies can now choose from among several different approaches to collaborations among competitors.

In addition to the traditional per se rule and rule of reason, the courts and agencies have endorsed various market-share-safe harbors and a so-called quick look at the competitive effects of a restraint. Under the market-share-safe harbor, the courts have required a plaintiff to prove that a defendant had a market share in excess of a particular threshold. The restraint at issue has been found legal when the plaintiff failed to meet its burden.¹¹³ The quick look absolves the plaintiff of the need to prove the anticompetitive effects of a particular restraint, including proof of the defendant's market power, at the initial stage of a case. Under the quick look, the plaintiff need merely prove initially that the restraint is of a type that is likely to have anticompetitive effects. After such a showing, the burden of proof shifts to the defendant to demonstrate a procompetitive justification for the restraint.¹¹⁴

112. See *United States v. E.I. DuPont de Nemours & Co.*, 96 F.T.C. 653, 751 n.42 (1980) ("If a monopoly results that proves impervious to competitive inroads and is unjustified by scale economies or other efficiencies, antitrust action in this or some other forum may be warranted, even in the absence of abusive conduct.").

113. See, e.g., *Gen. Leaseways, Inc. v. Nat'l Truck Leasing Ass'n*, 744 F.2d 588, 596 (7th Cir. 1984) (stating that in rule of reason analysis, "the plaintiff first [must] prove that the defendant has sufficient market power to restrain competition substantially . . . If not, the inquiry is at an end; the practice is lawful" (citations omitted)).

114. See, e.g., *Law v. NCAA*, 134 F.3d 1010, 1020 (10th Cir. 1998) ("Where a practice has obvious anticompetitive effects . . . there is no need to prove that the defendant possesses market power."); *United States v. Brown Univ.*, 5 F.3d 658, 673–78 (3d Cir. 1993) (employing a quick look analysis for agreements among universities on financial aid offerings to particular students); *U.S. Healthcare, Inc. v. Healthsource, Inc.*, 986 F.2d 589, 593–94 (1st Cir. 1993) (explaining the plaintiff's advantage in having a reduced burden of proof). The DOJ and FTC have also adopted versions of the quick look approach, shifting the burden to defendants to prove the efficiencies of inherently anticompetitive conduct. See *Mass. Bd. of Registration in Optometry*, 110 F.T.C. 549 (1988) (using quick look to analyze restrictions on advertising imposed by association of optometrists); *Antitrust Guidelines for Collaborations Among Competitors*, 4 Trade Reg. Rep. (CCH) ¶ 13,161, at 20,853 (Apr. 12, 2000) [hereinafter *Collaboration Guidelines*] (providing for a quick look form of the rule of reason for restraints that do not fall within a traditional per se category but nevertheless present a clear "likelihood of anticompetitive harm").

By the end of the 1990s, the federal courts and enforcement agencies had adopted inconsistent approaches to section 1 of the Sherman Act. It had become unclear to antitrust practitioners whether the courts and agencies would apply a per se, rule of reason, market-share-safe harbor, or quick look approach to particular restraints. To clarify the standards for analyzing section 1 restraints, the Supreme Court, in 1999, granted certiorari in *California Dental*.

C. The Supreme Court's New Approach in *California Dental*

This author has argued that the federal courts and enforcement agencies should abandon the false distinctions between the per se rule, the rule of reason, the quick look, and other fixed categories of antitrust analysis.¹¹⁵ Instead of relying on separate categories of analysis, the courts and agencies should judge antitrust conduct under a continuum, which would allow them to tailor their analysis to the likely competitive effects of the particular conduct at issue. In 1999, in *California Dental*, the Supreme Court explicitly recognized the proposal of this author for such a sliding scale approach to Sherman Act analysis.

California Dental involved advertising restrictions imposed by the California Dental Association.¹¹⁶ The restrictions precluded dentists from advertising their prices as "low" or of similar effect.¹¹⁷ The Ninth Circuit had held that the restrictions should be analyzed under the quick look because they made it "more difficult for consumers to find a lower price and for dentists to compete on the basis of price."¹¹⁸ The Supreme Court concluded that a quick look analysis was not appropriate, because it was not intuitively obvious that the advertising restrictions were likely to have anticompetitive effects.¹¹⁹ The restrictions might, for example, have promoted competition by eliminating misleading and unverifiable discount advertising.¹²⁰ The Court recognized, however, that the alternative to the quick look need not necessarily be a full rule of reason market power analysis.¹²¹ Instead of being divided into discrete categories, Sherman Act analysis should be viewed as a continuum under which courts can engage in a variety of inquiries "meet for the case."¹²² Citing Philip Areeda, this author, and other commentators, the Court stated that, in Sherman Act cases, "the quality of proof required should vary with the circumstances."¹²³ Turning to the advertising restrictions

115. See *supra* note 6 and accompanying text.

116. *Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 760 (1999).

117. See *id.* at 760–61 n.1.

118. *Cal. Dental Ass'n v. FTC*, 128 F.3d 720, 727 (9th Cir. 1997), *vacated*, 526 U.S. 756 (1999).

119. *California Dental*, 526 U.S. 756, 771–72, 779–81.

120. *Id.* at 771–72.

121. The Court stated that its rejection of the quick look did not mean a "call for the fullest market analysis. . . . [Not] every case attacking a less obviously anticompetitive restraint . . . is a candidate for plenary market examination." *Id.* at 779.

122. *Id.* at 781.

123. *Id.* at 780 (citing AREEDA, *supra* note 8, at ¶ 1507; Kolasky, *supra* note 8, at 41–42; Piraino, Jr., *Rule of Reason*, *supra* note 6, at 1771).

at issue, the Court held that “a less quick look” was required and remanded the case “for a fuller consideration of the issue.”¹²⁴

IV. A NEW APPROACH TO ANTITRUST REGULATION

Building on the Supreme Court’s decision in *California Dental*, the courts and agencies can adopt a new approach to antitrust analysis that categorizes all conduct on a continuum based upon its likely effect on consumers. The type of analysis applied by a court or agency would vary, depending upon the location of the relevant conduct on the continuum. Under such an approach, the courts and agencies could divide antitrust analysis into two broad categories: (1) presumptively legal or illegal conduct, and (2) conduct requiring a prioritized market analysis.

A. *Classifying Competitive Conduct on a California Dental Continuum*

The Supreme Court’s decision in *California Dental* has given the lower federal courts and enforcement agencies a means of reconciling the Harvard and Chicago Schools. The courts and agencies can now use both the presumptions of the Harvard School and the empirical economic analysis of the Chicago School to confirm the consumer welfare effects of competitive conduct. To adopt an inquiry “meet for the case,” as required by *California Dental*, the courts and agencies should categorize all competitive conduct on a continuum according to its likely effect on consumers.¹²⁵ In order to confirm that effect, the courts and agencies will have to undertake varying degrees of inquiry depending upon the type of conduct at issue. When the competitive effect of the relevant conduct is obvious, the courts and agencies can indulge presumptions similar to those favored by the Harvard School; when the competitive effect of the relevant conduct is not clear on its face, the courts and agencies can engage in a more detailed economic analysis similar to that favored by the Chicago School.

Under *California Dental*, fact finders need not confine their inquiry to the types of analysis previously identified by the courts and agencies. As the Supreme Court pointed out: “[O]ur categories of analysis of anticompetitive effect are less fixed than terms like ‘per se,’ ‘quick look,’ and ‘rule of reason’ tend to make them appear.”¹²⁶ Indeed, the time has come for the courts and agencies to abandon these outmoded phrases, which artificially limit fact finders’ discretion. There is no longer any need for the courts and agencies to confine themselves to a false choice between the per se rule’s conclusive presumption of illegality and the rule of reason’s formless pursuit of all conceivable economic circumstances.

124. *Id.* at 781.

125. *Id.* See also *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 35 (D.C. Cir. 2005) (stating that, in *California Dental*, the Supreme Court “backed away from any reliance upon fixed categories and toward a continuum”); *In re N. Tex. Specialty Physicians, 2005-2 Trade Cas. (CCH) ¶ 75,032*, at 103,463 (FTC, Nov. 29, 2005) (stating that *California Dental* and subsequent lower court and agency decisions “go beyond the simple dichotomy between categories like ‘per se’ or ‘rule of reason,’ and establish a continuum within which behavior can be analyzed”).

126. *California Dental*, 526 U.S. at 779.

In cases where judicial experience has demonstrated the likely competitive effect of the relevant conduct, the courts need not find the conduct conclusively legal or illegal. By using presumptions, the courts and agencies can retain the clarity of the Harvard School without sacrificing their search for the right economic answer. The courts and agencies should simply presume that the most likely competitive effect did, in fact, occur and shift the burden of proof to the party attempting to demonstrate that the actual outcome was contrary to normal expectations. Such an approach would be fairer to litigating parties than the Harvard School's *per se* standard, which conclusively presumes the illegality of conduct without giving defendants a rebuttal opportunity. The approach would ensure that, even when a court or agency was relatively certain about the competitive effect of the relevant conduct, it would not make a final decision on its legality without considering appropriate rebuttal arguments.

By the same token, when the likely competitive effect of the relevant conduct is not clear on its face, the courts and agencies need not inquire into all possible economic conditions before deciding on the conduct's legality. Even in such cases, the courts and agencies can avoid the endless empirical inquiry of the Chicago School. Although presumptions of legality or illegality would not be appropriate in such cases, the courts and agencies can prioritize their inquiry so that they first consider potentially dispositive factors, such as the parties' market power. This approach will permit the courts and agencies to dispose of many cases at an early stage if the plaintiff fails to meet its initial burden of proof.

The proposed approach will prevent judges, juries, and antitrust regulators from straying into the analysis of economic factors that are beyond their competence, and it will allow them to develop guidelines for competitive conduct that can be easily understood by the business community and by fact finders. Rather than viewing the various types of competitive conduct in isolation, this continuum-based approach would group together conduct, the legality of which could be determined in a similar manner. Under such an approach, all antitrust analysis can be divided into two broad categories: (1) presumptively legal or illegal conduct, and (2) conduct requiring a prioritized market analysis.

B. Presumptively Legal or Illegal Conduct

The federal courts and enforcement agencies have been analyzing competitive conduct under the federal antitrust laws for more than a century. They have enough experience to make an initial judgment at the outset of a case about the likely impact of particular conduct on consumers. In most cases, courts and agencies will be able to make a decision on the face of the relevant conduct. Indeed, given their years of experience in antitrust cases, the courts and agencies should be able to afford a presumption of legality or illegality to most competitive conduct.¹²⁷

The structure of most transactions should reveal whether it is appropriate to apply a presumption of legality or illegality. The federal courts and antitrust enforcement agencies have consistently concluded that vertical mergers and joint ventures between noncompetitors and vertical resale restraints imposed by suppliers on their distributors

127. See *Polygram Holding*, 416 F.3d at 37 (“[A]s economic learning and market experience evolve, so too will the class of restraints subject to summary adjudication.”).

almost always have a net beneficial effect on consumers.¹²⁸ Therefore it is appropriate for the courts and agencies to classify such vertical transactions at the presumptively legal end of the continuum of antitrust analysis.

The federal courts and enforcement agencies have also consistently concluded that horizontal agreements among competitors to fix prices, restrict competition, or allocate territories almost always restrict competition without any offsetting efficiency benefit for consumers.¹²⁹ Such horizontal agreements should be classified at the presumptively illegal extreme of the continuum of antitrust analysis.

Once a presumption applies, the relevant party should have an opportunity to rebut the presumption by proving that the actual purpose of the transaction was to effect a competitive outcome contrary to that which would normally be expected from its structure. It should be relatively easy for the courts and agencies to confirm whether the appropriate party has met its burden of proving that the purpose of the transaction was contrary to normal expectations. Fact finders can discern the purpose of parties' conduct by determining the credibility of their witnesses, their explanations for their conduct, and the relevance and significance of memoranda, minutes, hand-written notes, e-mails, and other documents that they have produced.¹³⁰ Nearly every day, judges and juries are called upon to use such means to determine the purpose of defendants' behavior in contract, tort, employment, and criminal disputes.¹³¹

Until the empirical approach of the Chicago School became ascendant,¹³² the federal courts were willing to use defendants' purpose as a proxy for the effects of their conduct on competition. In 1962, in *Poller v. CBS*,¹³³ the Court pointed out that "motive and intent play leading roles" in antitrust litigation. In 1979, the Court concluded in *Broadcast Music, Inc. v. CBS*,¹³⁴ that a defendant's purpose for particular competitive behavior "tends to show [its] effect." Most recently, in *Business Electronics Corp. v. Sharp Electronics Corp.*,¹³⁵ Justice Stevens, citing this author, pointed out in a dissenting opinion that "in antitrust, as in many other areas of the law, motivation matters and factfinders are able to distinguish bad from good intent."¹³⁶

128. See *infra* notes 135–37, 140–49, and accompanying text.

129. See *infra* notes 156–70 and accompanying text.

130. See *Crane*, *supra* note 62, at 15 (stating that fact finders excel in determining "who did what, when, and why").

131. For example, courts must often determine whether employers' decisions on hiring and promotion are made for a legitimate purpose or for an illegal discriminatory reason. See, e.g., *Price Waterhouse v. Hopkins*, 490 U.S. 228, 246 (1989) (calling these "mixed-motives" cases), *superseded by statute*, Civil Rights Act of 1991, Pub. L. No. 102-166, 105 Stat. 1074, *as recognized in* *Desert Palace, Inc. v. Costa*, 539 U.S. 90 (2003).

132. Chicago School adherents believe that economic data gives a more objective view of actual competitive effects than evidence of a defendant's intent. See *A.A. Poultry Farms v. Rose Acre Farms*, 881 F.2d 1396, 1402 (7th Cir. 1989) (Easterbrook, J.) (stating that intent evidence is "even more ambiguous than the economic data it seeks to illuminate").

133. 368 U.S. 464, 473 (1962).

134. 441 U.S. 1, 19 (1979).

135. 485 U.S. 717 (1988).

136. *Id.* at 754 (Stevens, J., dissenting) (citing *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 610–11 (1985); *McLain v. Real Estate Bd. of New Orleans, Inc.*, 444 U.S. 232, 243 (1980); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 224–26 n.59 (1940); *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918); *Thomas A. Piraino, Jr., The*

C. Conduct Requiring a Prioritized Market Analysis

Despite the courts' and agencies' decades of experience in antitrust cases, they will not be able to discern the likely competitive effects of all conduct on its face. When the conduct at issue is equally likely to benefit or to harm consumers, the courts and agencies will have to utilize an approach closer to the empirical economic analysis of the Chicago School than to the Harvard School's presumptions. The ultimate competitive effect of exclusive dealing, tying, monopoly conduct by individual firms, horizontal mergers, and joint ventures will depend upon the particular circumstances of the relevant market. In such cases, rather than applying presumptions in favor of a particular outcome, the courts and agencies should allocate the normal burdens of proof and rebuttal to the plaintiff and defendant. Even in such cases, however, the courts and agencies need not revert to the "catch-all" approach of the traditional rule of reason; they can simplify their analysis by prioritizing the factors they consider.

The most critical factor should be the defendants' market power. Firms cannot harm consumers unless they possess substantial market power in the relevant market. Thus, the courts and agencies should establish a market power threshold for the plaintiff's prima facie case. If a plaintiff fails to meet its initial burden of proving market power in excess of the applicable threshold, a court or agency can dismiss the case without considering other economic factors.

Figure 1 illustrates how presumptively legal and illegal conduct and conduct requiring a prioritized market analysis would be arrayed on the continuum of antitrust analysis:

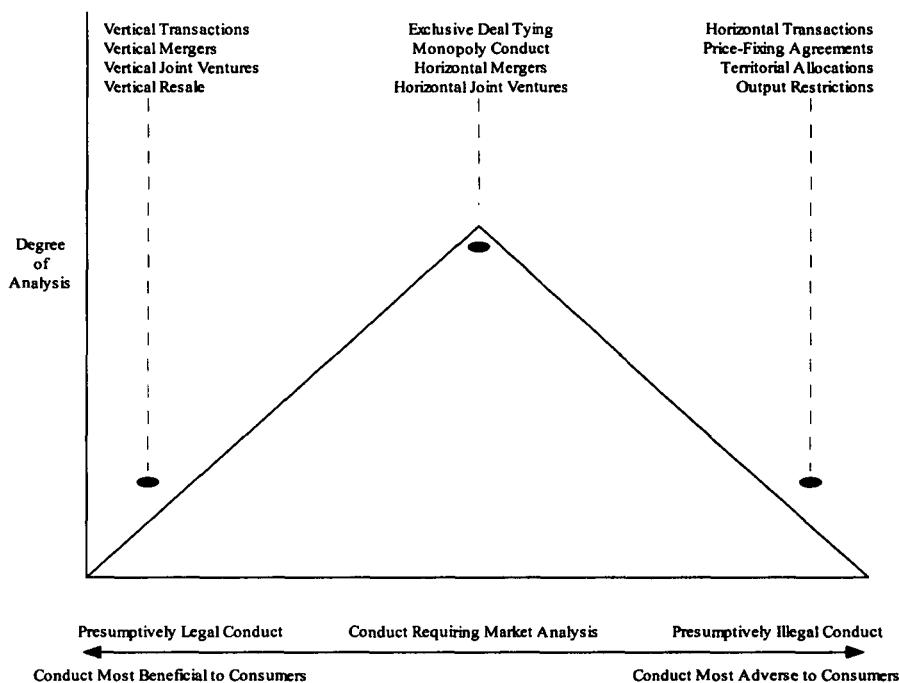


Figure 1. The continuum of antitrust analysis.

The “x”-axis begins with conduct most likely to benefit consumers and extends to conduct most likely to harm consumers. Presumptively legal and illegal conduct lie at the opposite extremes of the x-axis. The “y”-axis begins with conduct requiring the least amount of analysis and extends to conduct requiring the most detailed analysis. Both presumptively legal and illegal conduct lie at the low point of the y-axis, while conduct requiring a prioritized market analysis lies at an intermediate point that requires the courts and agencies to engage in a more in-depth factual analysis.

The following Parts explain how the courts and agencies can use this continuum-based approach to evaluate presumptively legal conduct, presumptively illegal conduct, and conduct requiring a prioritized market analysis.

V. PRESUMPTIVELY LEGAL CONDUCT

The courts and agencies should apply a rule of presumptive legality to vertical resale restraints, vertical mergers, and joint ventures. The presumption of legality should apply once a defendant has proven that a restraint of trade, merger, or joint venture is between noncompetitors. A plaintiff can rebut the presumption of legality for a vertical restraint of trade, vertical merger, or joint venture by proving that, despite the apparently benign structure of the transaction, the defendants were actually attempting to accomplish an anticompetitive objective.

A. Vertical Restraints of Trade

Vertical resale restraints constitute agreements between a supplier and its dealers, distributors, or other resellers. Vertical resale restraints are usually designed for a

procompetitive purpose and have a minimal anticompetitive effect. Vertical resale restraints only affect "intra-brand competition," that is, competition among dealers in the resale of the manufacturer's own product. Such restraints may increase resale prices for the manufacturer's product, but they do not adversely affect interbrand competition. Indeed, their only impact on interbrand competition is beneficial.¹³⁷

Consider a requirement by General Motors that its distributors sell automobiles only from certain authorized locations. The distributors might argue that the restriction limits their ability to compete against other General Motors dealers. General Motors, however, could legitimately argue that the benefits of the restriction outweigh its adverse effects. By limiting competition among General Motors' dealers, the restriction encourages dealers to invest in the types of point-of-sale services that are attractive to consumers. Such actions by the dealers help General Motors to compete more effectively against other automobile manufacturers, such as Toyota, which have recently been gaining market share at General Motors' expense.¹³⁸

1. The Presumption of Legality

The courts have recognized since *Sylvania* that vertical resale restraints should be upheld because they have the beneficial effect of encouraging dealers to provide quality-related services that make a manufacturer's products more competitive against other brands.¹³⁹ Internal growth or vertical mergers by manufacturers into the resale level are treated leniently under the antitrust laws because the integration of productive activities is obvious. Contract integration achieved through vertical resale restraints should be given at least as much deference.¹⁴⁰ Indeed, such restraints are preferable to vertical integration because they can achieve the productive purposes of integration without eliminating all intra-brand competition. Because vertical resale restraints are almost always procompetitive and beneficial to consumers, they should be afforded a rebuttable presumption of legality.¹⁴¹

137. See *Cont'l T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977) (applying rule of reason rather than per se approach to Sylvania's territorial restrictions on its television dealers on grounds that restrictions only adversely affected intra-brand competition among Sylvania dealers and benefitted interbrand competition between Sylvania and other television manufacturers).

138. See Jathon Sapsford, Norihiko Shirouzu & Joseph B. White, *Toyota Maps Plan to Displace GM as Top Car Maker*, WALL ST. J., Nov. 19, 2005, at A1 (describing Toyota's plans to overtake General Motors as "the world's biggest maker of cars").

139. See, e.g., *Sports Center, Inc. v. Riddell, Inc.*, 673 F.2d 786 (5th Cir. 1982); *Del Rio Distrib., Inc. v. Adolph Coors Co.*, 589 F.2d 176 (5th Cir. 1979); *Donald B. Rice Tire Co. v. Michelin Tire Corp.*, 483 F. Supp. 750 (D. Md. 1980); see also *Ricchetti v. Meister Brau, Inc.*, 431 F.2d 1211 (9th Cir. 1970) (decided before *Sylvania*, but foreshadowing the court's eventual move).

140. See Bork, *supra* note 3, at 264.

141. Several commentators have argued that vertical restrictions should be per se legal. See *id.* at 288; Ernest Gellhorn & Teresa Tatham, *Making Sense Out of the Rule of Reason*, 35 CASE W. RES. L. REV. 155, 178 (1984); Richard A. Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision*, 45 U. CHI. L. REV. 1, 13 (1977).

2. The Defendant's Rebuttal Case: Proving Induced Discrimination

A plaintiff can rebut the presumption of legality for vertical resale restraints by proving that the purpose of the restraint was not to enhance the supplier's efficiency but simply to placate dealers attempting to limit competition from their rivals. It is appropriate to place the burden on plaintiffs to rebut the presumption of legality for vertical resale restraints because dealers are rarely able to induce suppliers to take an adverse action against other dealers that the suppliers would not have taken on their own. In most cases, suppliers have legitimate, independent business reason for limiting competition among their dealers. In certain cases, however, dealers may be able to meet their burden of proving an anticompetitive purpose for a vertical resale restraint.

Consider a case in which a group of long-term General Motors dealers become concerned about the price-cutting activities of a group of recently appointed dealers. The older dealers demand that General Motors terminate the franchises of the newer dealers. If General Motors acceded to the older dealers' demands, such conduct would have no purpose or effect other than to limit price competition. Such conduct should be illegal because it eliminates consumer choice without any offsetting efficiency benefit.¹⁴²

A court's goal in cases of induced discrimination should be to determine whether the discrimination was initiated independently by a supplier or induced by one or more buyers in order to disadvantage a rival. Discriminatory actions against buyers are more likely to be initiated by suppliers for legitimate reasons than to be induced by rival retailers for anticompetitive purposes. Thus, in order to rebut the presumption of legality for vertical restraints, a plaintiff should be required to prove: (1) that a buyer and supplier had a mutual commitment to discriminate against a rival of the buyer, either by driving the rival from the market or raising its costs; (2) that the supplier's only reason to effect the discrimination was to meet the anticompetitive demands of the buyer; and (3) that the rival was competitively disadvantaged as a result of the actions of the supplier and the buyer. Once a plaintiff has met this burden of proof, however, it

142. The Supreme Court applied the per se rule to such conduct in *United States v. General Motors Corp.*, 384 U.S. 127 (1966) (applying per se rule when a group of automobile dealers induced General Motors not to sell to automobile discount houses). Unfortunately, however, the Court has opted for a rule of reason approach when only one buyer has convinced a supplier to take the relevant action. See *Nynex Corp. v. Discon, Inc.*, 525 U.S. 128 (1998) (declining to apply a per se analysis to a decision by a local telephone company to switch from one supplier to another); *Bus. Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717 (1988) (refusing to apply per se rule when a single dealer induced manufacturer of electronic calculators to terminate rival dealer). The Supreme Court failed to recognize in *Sharp* and *Nynex* that, in an induced discrimination case, the number of conspirators at each level of the supply chain has no economic relevance. Regardless of whether one or more buyers complain about a rival's prices or other competitive conduct, a supplier should not be permitted to knuckle under to its buyers' anticompetitive demands to exclude a rival from the market. As Justice Stevens pointed out, citing this author in his dissent in *Sharp*, the relevant inquiry in induced discrimination cases is "to insure that a manufacturer's motive for a vertical restriction is not simply to acquiesce in his distributors' desires to limit competition among themselves." *Sharp*, 485 U.S. at 750, n.14 (Stevens, J., dissenting) (citing Piraino, Jr., *Quality Motivated Restrictions*, *supra* note 136, at 17).

would not have to introduce evidence of the market power of the supplier or the inducing buyer, nor of any other conditions affecting the relevant market.

This approach will encourage suppliers to continue to impose and enforce legitimate performance-based standards on their buyers, but it will also deter suppliers from conspiring with their large buyers to discriminate against smaller buyers.

B. Vertical Mergers and Joint Ventures

Vertical mergers and joint ventures are between firms that are not actual or potential competitors. As in the case of vertical resale restraints, a defendant should be able to raise a presumption of legality for vertical mergers and joint ventures merely by proving their existence. Such transactions should be presumptively legal because they do not restrict any actual or potential competition between the parties.

1. The Presumption of Legality

Most courts and agencies have upheld mergers and joint ventures among parties that are not actual or potential competitors.¹⁴³ The courts and agencies should apply a presumption of legality to all vertical mergers and joint ventures, regardless of the parties' market shares in the markets affected by the transaction. For example, a merger between Microsoft and General Motors would create a gigantic enterprise with more than \$230 billion in annual revenue.¹⁴⁴ However, the new entity would not be able to exercise any more power in the automobile or computer operating system markets than the companies could have exercised prior to the transaction.

Joint ventures need not necessarily involve noncompetitors in order to be classified as vertical transactions entitled to a presumption of legality. Unlike mergers, which eliminate all competition between the parties, joint ventures are formed to accomplish specific objectives, and they allow their partners to compete in areas outside the narrow scope of the venture.¹⁴⁵ Thus, competitors may enter into joint ventures which

143. For a discussion of the courts' lenient approach to vertical mergers, see Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 ANTITRUST L.J. 513, 514 (1995). For decisions upholding joint ventures, see, for example, *United States v. FCC*, 652 F.2d 72, 96–101 (D.C. Cir. 1980) (en banc) (holding joint venture to construct a communications satellite network does not violate antitrust laws if parents were not actual or potential competitors in the relevant market). See also Robert Pitofsky, *A Framework for Antitrust Analysis of Joint Ventures*, 74 GEO. L.J. 1605, 1608–09 (1986) (asserting that joint ventures among noncompetitors in unconcentrated markets should be legal per se).

144. “[General Motors], still the world’s largest manufacturer, remains a colossus, with more than \$190 billion in annual revenue.” Jathon Sapsford, Joseph B. White & Dennis K. Berman, *GM Shares Sink to 23-Year Low as Woes Mount*, WALL ST. J., Dec. 21, 2005, at A1. Microsoft had approximately \$40 billion in revenue in its 2005 fiscal year. See MICROSOFT CORP., ANNUAL REPORT 2005 (2005), <http://www.microsoft.com/msft/reports/ar05/staticversion/index.html>.

145. See Thomas A. Piraino, Jr., *Beyond Per Se, Rule of Reason or Merger Analysis: A New Antitrust Standard for Joint Ventures*, 76 MINN. L. REV. 1, 7 (1991) [hereinafter Piraino, Jr., *Beyond Per Se*] (“While mergers eliminate all competition between the parties, joint ventures, by virtue of their limited scope, leave the parties free to compete in areas not covered by the joint venture.”); *Collaboration Guidelines*, *supra* note 114, at 20,853 (“The competitive effects from competitors’ collaborations may differ from those of mergers Most mergers

are limited to areas in which they are not currently competing. Competitors, for example, often form joint ventures to develop or produce new products that they could not have developed on their own. If the purpose of the venture is to allow the partners to enter new markets from which they would have been individually foreclosed, the venture will not restrict competition in any manner.¹⁴⁶

Consider a joint venture between General Motors and Ford to develop a hybrid engine that can boost fuel efficiency by combining a traditional gasoline motor with an electric motor.¹⁴⁷ Assume that General Motors and Ford do not have the financial capacity to independently make the multibillion dollar investment necessary for the development of such an engine.¹⁴⁸ Such a joint venture would not have any anticompetitive effects because it would not limit any preexisting competition between the parties. General Motors and Ford would be able to continue to compete in the production and sale of automobiles. The only effect of such a joint venture would be to expand the alternatives available to consumers by facilitating the commercialization of a new technology that neither company would have been able to develop on its own.¹⁴⁹

In some cases, even downstream-marketing joint ventures allow firms to enter new markets or produce new products. Indeed, certain unique products can be marketed only through a joint venture. A venture that allows the marketing of such a product cannot restrict competition because, in the absence of the venture, the relevant product would never have existed. In denying a per se approach in *BMI*, for example, the Supreme Court pointed out that the blanket license was a type of “different product” and that the composers’ arrangement was “necessary to market the product at all.”¹⁵⁰

completely end competition between the merging parties in the relevant market(s). By contrast, most competitor collaborations preserve some form of competition among the participants.”)

146. See Joseph Kattan, *Antitrust Analysis of Technology Joint Ventures: Allocative Efficiency and the Rewards of Innovation*, 61 ANTITRUST L.J. 937, 940 n.18 (1993) (describing joint venture among pharmaceutical companies that gave partners access to patents necessary to produce a multivalent childhood vaccine that could be effective against several diseases at once). This type of joint venture promotes competition by permitting “the introduction of a new competitor that otherwise might never have come into being.” Robert Pitofsky, *Joint Ventures Under the Antitrust Laws: Some Reflections on the Significance of Penn-Olin*, 82 HARV. L. REV. 1007, 1018 (1969).

147. General Motors has already entered into a joint venture with DaimlerChrysler AG and BMW AG to develop such a hybrid engine. See Norihko Shirouzu & Jathon Sapsford, *Power Struggle: As Hybrid Cars Gain Traction, Industry Battles Over Designs*, WALL ST. J., Oct. 19, 2005, at A1.

148. In May, 2005, the debt ratings of General Motors and Ford were downgraded to “junk status.” Jonathon Fuerbringer, *High-Yield Market Survives G.M. and Ford, But Now What?*, N.Y. TIMES, June 12, 2005, at B6. In the first nine months of 2005, General Motors’ losses alone totaled \$3.8 billion. Sapsford et al., *supra* note 144, at A1.

149. For example, a joint venture between United Technologies and Rolls Royce for the manufacture of a new jet engine allowed the parties to produce, at an estimated cost of \$600 million, a product that Rolls Royce did not have the financial capacity to make independently. See *U.S. DOJ Antitrust Guidelines Concerning Research Joint Ventures*, 4 Trade Reg. Rep. (CCH) ¶ 13,120, at 20,677–78 (1980). See also *United States v. FCC*, 652 F.2d 72, 94 (D.C. Cir. 1980) (upholding joint venture for the production of communications satellites based on fact that, because of high start-up costs, the joint venture partners “were unlikely both to enter the field separately”).

150. *Broad. Music, Inc. v. CBS*, 441 U.S. 1, 22–23 (1979).

Sports leagues also constitute a type of marketing joint venture necessary for the existence of a unique product. Neither collegiate nor professional athletics could operate without a league organization. Leagues regulate the various activities required to carry on a sport: the number of persons on a team, the rules of play, restrictions on player mobility, and revenue sharing. The Supreme Court recognized in *NCAA v. Board of Regents*¹⁵¹ that such league rules “are essential if the product is to be available at all.”¹⁵² Because they make possible the marketing of a unique product, amateur and professional sports leagues usually do not offend the antitrust laws.¹⁵³

2. Rebutting the Presumption of Legality

A plaintiff can rebut the presumption of legality for a vertical merger or joint venture by demonstrating that it was designed to foreclose competitors of the parties from one of the markets affected by the merger. Although the courts and enforcement agencies have allowed most vertical mergers and joint ventures to proceed, some decisions have attacked such transactions on the grounds that they cause “potential foreclosure” in one of the markets in which the parties compete. Foreclosure problems may arise both at the upstream supplier level, and at the downstream distribution level. For example, if a shoe manufacturer acquired a national chain of shoe retailers, it could foreclose competing manufacturers from access to the retail outlets.¹⁵⁴ If an automobile company acquired a spark plug supplier, it could foreclose competing automobile manufacturers from purchasing from that supplier.¹⁵⁵

151. 468 U.S. 85 (1984).

152. *Id.* at 101. Certain other Supreme Court decisions have implicitly recognized the legality of marketing joint ventures that facilitate entry into new markets. In *Associated Press v. United States*, 326 U.S. 1 (1944), the Court did not question the legality of the Associated Press joint venture itself because, according to one commentator, “[f]ew if any newspapers would have been sufficiently affluent to perform the news gathering services provided by the AP joint venture.” Robert Pitofsky, *Joint Ventures Under the Antitrust Laws: Some Reflections on the Significance of Penn-Olin*, 82 HARV. L. REV. 1007, 1057–58 (1969). In *United States v. Penn-Olin Chemical Co.*, 389 U.S. 308 (1967) (per curiam), the Court upheld a joint venture after the district court found that neither party was likely to have entered the relevant market in the absence of the joint venture. See *United States v. Penn-Olin Chem. Co.*, 246 F. Supp. 917, 933–34 (D. Del. 1965).

153. The Eighth Circuit, in *Mackey v. NFL*, 543 F.2d 606, 619 (8th Cir. 1976), concluded that “the NFL assumes some of the characteristics of a joint venture,” and that “the unique nature of the business of professional football renders it inappropriate to mechanically apply per se illegality rules.” (emphasis in original). Robert Bork has stated that “some activities can only be carried out jointly. Perhaps the leading example is league sports.” BORK, *supra* note 3, at 278. The only relevant antitrust issue for sports leagues is whether their related restraints on competition are no broader than required to effect the legitimate interests of individual teams in maintaining the viability of their joint venture. See *infra* notes 177–94 and accompanying text.

154. See *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962) (precluding merger between shoe manufacturer and shoe retailer on grounds that manufacturer would be able to foreclose competing manufacturers from access to retailer’s outlets).

155. See *Ford Motor Co. v. United States*, 405 U.S. 562, 568, 574 (1972) (precluding Ford’s acquisition of spark plug manufacturer); *N. Natural Gas Co. v. Fed. Power Comm’n*, 399 F.2d 953 (D.C. Cir. 1968) (precluding joint venture between natural gas distributor and pipeline

Courts and agencies have never developed a bright-line test as to the amount of foreclosure that should be permitted for a particular merger or joint venture.¹⁵⁶ Thus, business executives have little guidance as to the types of vertical mergers or joint ventures they will be permitted to pursue. The proposed approach would clarify the circumstances in which vertical mergers or joint ventures would be permitted or precluded.

Vertical mergers or joint ventures should only be precluded when the transaction gives the parties control over a resource essential for competition in one of the markets affected by the transaction. A plaintiff should only be able to rebut the presumption of legality for a vertical merger or joint venture by demonstrating that, in order to compete effectively in the market affected by the transaction, it must be able to access the products or services of one of the parties. In such a case, the parties to the merger or joint venture would have the power to exclude their rivals from the relevant market.

The Walt Disney Company, for example, owns ABC and ESPN. Cable systems must be able to carry both of those networks in order to be competitive.¹⁵⁷ If a large cable company such as Cablevision acquired Disney, it conceivably could prevent competing cable companies from carrying ABC or ESPN. In such a case, it would be appropriate for a court or agency either to preclude the merger entirely or to insure that competitors could carry ABC and ESPN on their cable systems upon reasonable terms.¹⁵⁸

company that gave distributor the ability to preclude its competitors from obtaining natural gas through pipeline).

156. Courts, for example, have precluded vertical mergers involving various degrees of market foreclosure. Courts have precluded vertical mergers involving market foreclosures of 7.4% (see *Int'l Tel. & Tel. Corp. v. Gen. Tel. & Elecs. Corp.*, 449 F. Supp. 1158, 1182–83 (D. Haw. 1978)), 20 % (see *Ash Grove Cement Co. v. FTC*, 577 F.2d 1368, 1371–72 (9th Cir. 1978)), 45 % (see *Harnischfeger Corp. v. Paccar, Inc.*, 474 F. Supp. 1151, 1158–59 (E.D. Wis. 1979)), and 75% (see *Heattransfer Corp. v. Volkswagenwerk A.G.*, 553 F.2d 964, 981–82 (5th Cir. 1977), *cert. denied*, 434 U.S. 1087 (1978)), and they have approved mergers with market foreclosures of eight percent (see *Crane Co. v. Harsco Corp.*, 509 F. Supp. 115, 125 (D. Del. 1981)) and 2.7% (see *United States v. Hammermill Paper Co.*, 429 F. Supp. 1271, 1280 (W.D. Pa. 1977)).

157. See Comments of American Cable Association at 3, *In re Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB Docket No. 03-172 (FCC Sept. 11, 2003). available at http://gullfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6515082093 (“A core set of video services is essential to the viability of a cable system. This programming includes the major broadcast networks and ‘must-have’ or ‘marquee’ satellite programming, including ESPN (Disney) . . .”).

158. The agencies have allowed vertical mergers in the entertainment and telecommunications industries to proceed under consent orders which insure that competitors are not foreclosed from accessing resources essential for competition in one of the markets affected by the transaction. See Proposed Final Judgment and Competitive Impact Statement, *United States v. AT&T Corp.*, 59 Fed. Reg. 44,158, 44,162–63 (Aug. 26, 1994) (allowing merger between long-distance telephone company and cellular telephone company, on condition that telephone company provide cellular phones to its rivals upon equal terms); Agreement Containing Consent Order, *In re Time Warner Inc.*, No. 961-0004, 1996 FTC LEXIS 389 (allowing merger between Time Warner and Turner Broadcasting, on condition that merged company give its rivals nondiscriminatory access to its cable operations).

VI. PRESUMPTIVELY ILLEGAL CONDUCT

Horizontal agreements among sellers or buyers to fix prices, restrict output, or allocate territories almost always harm consumers. Courts and agencies should presume the illegality of such conduct and shift the burden to defendants to prove that their purpose in collaborating was not to limit competition but to enhance the efficiency of a legitimate joint venture beneficial to consumers.

A. The Presumption of Illegality

The courts have applied the per se rule to horizontal cartels among sellers to fix prices, restrict output, or allocate territories. In most cases, such arrangements have a clear anticompetitive effect and lack any efficiency justifications.¹⁵⁹ Cartels are incapable of producing any economic benefit because they involve no integration of the parties' resources. Horizontal cartels raise prices, reduce output, and limit consumers' range of choices. Indeed, such direct restrictions on interfirm rivalry strike at the heart of the open competitive system that the antitrust laws were designed to protect.¹⁶⁰ Competitors restrict the free play of market forces when they agree to raise, lower, fix, or stabilize prices in concert.¹⁶¹ When rivals agree to fix a common price for their products without combining their resources in any manner, the arrangement will be incapable of enhancing efficiency; its only effect will be to limit price competition among the parties, thus reducing consumers' choice. Indirect price-fixing schemes, such as restrictions on output, have the same anticompetitive impact,¹⁶² and horizontal

159. Naked agreements among competing sellers to fix prices, restrict output, or allocate territories have been considered per se illegal since the earliest days of the Sherman Act. *See United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 293 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899) (refusing to consider possible justifications for horizontal price fixing); Diane P. Wood, *The Incredible Shrinking Per Se Rule: Is an End in Sight?*, Presentation Before the Antitrust Section of the American Bar Association 3 (Apr. 1, 2004) (on file with author) ("The area in which the per se rule continues to be invoked most often, and continues to have real bite, is that of the hard-core cartel. By the term 'hard-core cartel,' antitrust lawyers normally mean an agreement between horizontal competitors . . . to fix prices or to engage in equivalent behaviors . . ."). Although the federal courts have taken a less aggressive approach in many antitrust areas during the last three decades, they never have wavered in their condemnation of horizontal cartels. In 2004, Justice Scalia (rarely an advocate of aggressive antitrust enforcement) described cartels as "the supreme evil of antitrust." *Verizon Commc'ns, Inc. v. Trinko*, 540 U.S. 398, 408 (2004).

160. *See Joseph F. Brodley, The Economic Goals of Antitrust: Efficiency, Consumer Welfare, and Technological Progress*, 62 N.Y.U. L. REV. 1020, 1023 (1987) (stating that "the economic goal of antitrust policy is to increase the material welfare of society through the instrument of interfirm rivalry").

161. *See United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 221 (1940) (approving per se illegality of any conspiracy among competitors designed to raise, lower, fix, or stabilize prices on the grounds that such conspiracies directly interfere with "the free play of market forces").

162. *See FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 464-66 (1986) (holding illegal a refusal by dentists to provide patients' x-rays to insurers); *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 692-96 (1978) (holding illegal a ban on competitive bidding); *United*

territorial allocations are no less pernicious. In fact, horizontal territorial allocation often has a more adverse effect on competition than horizontal price fixing.¹⁶³ The parties to a price-fixing arrangement may continue to compete with each other in certain nonprice areas, such as customer service. Customer and territorial allocations, however, eliminate all competition among the parties, whether price or nonprice. Consider a bald agreement among General Motors, Ford, and DaimlerChrysler to market an automobile with a fuel-efficient hybrid engine within separate areas of the country. The automobile companies would be free, within their separate territories, not only to price the new automobile in any manner they saw fit, but also to limit its production or to refuse to make certain accessories or services available to consumers.

Cartels among buyers can harm consumers just as surely as cartels among sellers. Like seller cartels, buyer cartels should be presumptively illegal. "Oligopsony" pricing occurs when buyers agree to engage in joint purchasing negotiations and to offer a common purchase price to their suppliers.¹⁶⁴ Such arrangements prevent competition among buyers on input prices. The prices of raw materials and finished goods purchased for resale are an important component of buyers' overall costs. Consumers benefit when buyers seek their own innovative ways of limiting such costs and pass on the cost savings to their customers. Input prices are likely to reach their lowest levels when buyers are competing aggressively against each other to obtain the best possible terms from their suppliers. When buyers abandon such competition and offer identical prices to their suppliers, they lose all incentive to obtain a cost advantage over each other. Furthermore, such buyers are more likely to cooperate to retain the benefits of any cost savings for themselves. Once a group of buyers has successfully conspired to reduce their collective input prices, they will be more inclined to conspire with each other to keep their resale prices high.¹⁶⁵ Indeed, economic studies indicate that buyers engaged in oligopsony pricing are less likely than other buyers to pass on the benefit of lower input prices to consumers.¹⁶⁶

The anticompetitive effects of horizontal price fixing, output restrictions, and customer and territorial allocations among buyers and sellers are clear enough to excuse the plaintiff from a demonstration of the defendant's market power. A

States v. Container Corp. of America, 393 U.S. 333, 337–38 (1969) (holding illegal the exchange of price information); Chicago Prof'l Sports Ltd. P'ship v. NBA, 754 F. Supp. 1336, 1364 (N.D. Ill. 1991) (holding illegal the reduction by a sports league of the number of games broadcast).

163. The courts have consistently applied the per se rule to horizontal customer, territorial or, output allocations as well as to horizontal price fixing. *See* United States v. Topco Assocs., 405 U.S. 596, 608 (1972) (applying per se rule to horizontal territorial allocation); United States v. Cadillac Overall Supply Co., 568 F.2d 1078, 1089–90 (5th Cir. 1978) (applying per se rule to horizontal customer allocation). Even Chicago School commentators have concluded that horizontal market division is as great an evil as horizontal price fixing. *See, e.g.*, Posner, *supra* note 48, at 292.

164. *See In re Beef Indus. Antitrust Litig.*, 907 F.2d 510, 515 (5th Cir. 1990) (stating that an oligopsonist "could form an alliance with other oligopsonists in the relevant market and attempt to depress prices and increase profits").

165. *See* Jonathon B. Baker, *The Case for Antitrust Enforcement*, J. ECON. PERSP., Fall 2003, at 27, 30.

166. *See* Peter J. Hammer & William M. Sage, *Monopsony as an Agency and Regulatory Problem in Health Care*, 71 ANTITRUST L.J. 949, 967 (2004) ("[L]ower input prices do not lead to lower consumer output prices.").

presumption of illegality for these restraints would preserve the deterrent effect of the current per se approach to such conduct. When the detrimental effects of a restraint are apparent, there is no need to inquire into market power. The Supreme Court recognized in *NCAA v. Board of Regents* that “[a]s a matter of law, the absence of proof of market power does not justify a naked restriction on price or output.”¹⁶⁷ If a restraint is clearly anticompetitive on its face, the burden should shift to the defendant to come forward with proof of some procompetitive virtue that justifies the restraint.¹⁶⁸

Some Chicago School commentators have argued that plaintiffs should have the initial burden of proving market power even for such horizontal restraints as price fixing. They have emphasized that only firms with market power can injure competition over a meaningful period because the marketplace ultimately will undercut the effectiveness of any anticompetitive restraints as consumers switch to substitutes or new firms enter the market.¹⁶⁹ There are, however, several reasons to dispense with a market power analysis of horizontal price fixing, output restrictions, and territorial and customer allocations. For one thing, markets do not always react as quickly as some commentators have assumed: “[f]or reasons including market inertia and information failures . . . a small conspirator may be able to impede competition over some period of time.”¹⁷⁰ Furthermore, there is little to be gained and much to be lost by introducing the complexities of a market power test into the analysis of such inherently suspect conduct. The courts risk few mistakes by dispensing with a market power analysis of conduct which is likely to harm competition in most cases.¹⁷¹

On the other hand, requiring a market power analysis complicates antitrust trials, wastes judicial resources, and makes plaintiffs more reluctant to bring cases, thus reducing the deterrent effect of the antitrust laws. A clear rule prohibiting naked horizontal restrictions of competition precludes undesirable behavior at its inception and prevents it from ripening into a full-blown competitive threat. As Professor Areeda has asserted, “The defendants have little moral standing to demand proof of power or effect when the most they can say for themselves is that they tried to harm the public but were mistaken in their ability to do so.”¹⁷²

167. 468 U.S. 85, 109 (1984).

168. See *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 36 (D.C. Cir. 2005) (“If, based upon economic learning and the experience of the market, it is obvious that a restraint of trade likely impairs competition, then the restraint is presumed unlawful and, in order to avoid liability, the defendant must either identify some reason the restraint is unlikely to harm consumers or identify some competitive benefit that plausibly offsets the apparent or anticipated harm.”).

169. See, e.g., Thomas M. Jorde & David J. Teece, *Rule of Reason Analysis of Horizontal Arrangements: Agreements Designed to Advance Innovation and Commercialize Technology*, 61 ANTITRUST L.J. 579, 602–03 (1993) (stating that the marketplace will discipline firms that attempt to restrain trade if they lack substantial market power); M. Laurence Popofsky & David B. Goodwin, *The “Hard-Boiled” Rule of Reason Revisited*, 56 ANTITRUST L.J. 195, 203 (1987) (indicating that two firms that agree to a horizontal restraint are unlikely to injure competition if they lack market power).

170. *FTC v. Superior Court Trial Lawyers Ass’n*, 493 U.S. 411, 434–35 (1990).

171. As Professor Areeda has stated, “Once we decide that a class of practice is in the vast generality of cases detrimental and unjustified, why bother with the complicated and expensive inquiry into power?” Phillip Areeda, *The Changing Contours of the Per Se Rule*, 54 ANTITRUST L.J. 27, 28 (1985).

172. AREEDA, *supra* note 8, at ¶ 1510 (1986).

Defendants would not be unduly disadvantaged by bearing the burden of proving a justification for horizontal price fixing, output restrictions, and territorial and customer allocations. Indeed, a shifting of the burden of proof would be a vast improvement over the current per se approach, which gives defendants no opportunity to show that they had a legitimate purpose for a horizontal restraint. Placing that burden of proof on the defendant is fair since it will have access to the documents and witnesses most probative of the actual competitive effect of a horizontal restraint.¹⁷³ The defendant's internal documents and testimony from its own employees will usually reveal whether a particular restraint was intended to enhance the party's efficiency or merely to restrict competition. Firms usually can document in advance their efficiency objectives for particular restraints. A defendant's failure to produce such evidence may indicate that the real purpose for a restraint was anticompetitive.

B. The Plaintiff's Initial Burden of Proof

Restraints of trade are only illegal under section 1 of the Sherman Act if they are undertaken pursuant to a conspiracy among competing firms.¹⁷⁴ Thus, in order to raise a rebuttable presumption of illegality, a plaintiff must demonstrate that competing firms have entered into an agreement to fix prices, restrict output, or allocate territories or customers. The conspiracy may be either explicit or tacit. George Hay has explained that "[t]he prototype . . . [of an explicit cartel] is the smoke-filled room in which all the rivals engage in face-to-face communication."¹⁷⁵ Explicit agreements allow the participants to bargain openly on a consensus industry price level, to communicate to each other their intention to adhere to the consensus price, and to establish mechanisms for monitoring and enforcing such adherence. However, tacit conspiracies to fix prices or allocate customers or territories should be no less illegal than explicit agreements. There is now a consensus among economists that tacit price-fixing arrangements are just as harmful to consumers as explicit price-fixing agreements.¹⁷⁶ Firms engaged in tacit collusion can duplicate the conditions that occur under an explicit cartel. Like an express agreement, a tacit arrangement involves the reaching of a consensus on an above-market price and the adoption of a means of enforcing adherence to that

173. See Dennis A. Yao & Thomas N. Dahdouh, *Information Problems in Merger Decision Making and Their Impact on Development of an Efficiencies Defense*, 62 ANTITRUST L.J. 23, 27 (1993) ("Efficiency considerations and general principles of law suggest that the party with access to the relevant information should bear the burden of proving an issue dependent on that information.").

174. Section 1 precludes "[e]very contract, combination . . . or conspiracy, in restraint of trade." 15 U.S.C. § 1 (2000).

175. George A. Hay, *Oligopoly, Shared Monopoly, and Antitrust Law*, 67 CORNELL L. REV. 439, 452 (1982).

176. See, e.g., ROGER D. BLAIR & DAVID L. KASERMAN, ANTITRUST ECONOMICS 205–06 (1985) ("Section 1 attacks collusion because it is a joint effort to reap monopoly profits, and tacit collusion has a very similar impact."). Commentators have concluded that, since "there is no vital difference between formal cartels and tacit collusive arrangements . . . the tacit colluder should be punished like the express colluder." *Id.*

consensus. With greater assurance of their rivals' acquiescence, firms gain the confidence necessary to persist in pricing levels above the competitive norm.¹⁷⁷

It will be relatively easy for a plaintiff to meet its burden of proof when competitors have entered into an explicit horizontal conspiracy. However, the courts and agencies need to adopt a clearer standard by which plaintiffs can prove the existence of a tacit horizontal agreement. Tacit agreements often occur in "oligopoly" markets, where there are a small number of firms competing with each other. Recent models of "game theory" explain that oligopolists are able to maintain a price equilibrium at a level above that which would prevail in a perfectly competitive market (i.e., above marginal cost) simply by reacting to each other's pricing practices and without communicating directly with each other.¹⁷⁸ Such independent parallel conduct does not constitute an illegal "agreement" within the meaning of section 1 of the Sherman Act.

The courts and agencies have found it difficult to confirm when oligopolists have entered into illegal conspiracies rather than simply engaging in permissible parallel conduct. In oligopoly pricing cases, the courts have engaged in an extended search for various "plus factors" necessary to prove the existence of a formal agreement among the defendants. As a result, the courts have rendered a conflicting series of opinions that have only served to confuse business executives as to the dividing line between permissible and illegal oligopoly conduct.¹⁷⁹

Instead of engaging in a fruitless search for plus factors, the courts and agencies should concentrate on the purpose of defendants' conduct in oligopoly pricing cases. The courts and agencies should infer a conspiracy among oligopolists when they act in a manner that is contrary to their immediate self-interest and makes no economic sense other than as an invitation to join in a price-fixing or market-allocation arrangement. Indeed, actions by rivals against their own self-interest can communicate their consent to a higher price level just as clearly as a cartel's express commitment to a price-fixing

177. See Hay, *supra* note 175, at 446–47 (stating that firms engaged in tacit coordination can gain a mutual understanding of the consensus industry price and a mutual sense of confidence that all firms will adhere to that price).

178. In an oligopoly, where there are so few firms in the relevant market, it is easier for firms to make pricing decisions "in reference to the likely reaction of competitors." Robert A. Milne & Jack E. Pace III, *The Scope of Expert Testimony on the Subject of Conspiracies in a Sherman Act Case*, ANTITRUST, Spring 2003, at 36, 37 (emphasis omitted). Each firm recognizes its interdependence with other firms in the market and understands that "its optimal price is a function of the price charged by its rivals." BLAIR & KASERMAN, *supra* note 175, at 200. See also Bailey v. Allgas, Inc., 284 F.3d 1237, 1251 (11th Cir. 2002) ("[T]he distinctive characteristic of oligopoly is recognized interdependence among the leading firms: the profit-maximizing choice of price and output for one depends on the choices made by others.").

179. Recent Supreme Court decisions on the conspiracy issue have been particularly confusing. See *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984) (permitting inference of section 1 conspiracy among manufacturer and its distributors only when evidence "tends to exclude the possibility that the manufacturer and nonterminated distributors were acting independently"); *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986) (using *Monsanto* standard in declining to find predatory pricing conspiracy in case in which defendants had no rational business motive for entering into arrangement). There are no clear guidelines by which fact finders can determine how to exclude the possibility that a defendant had a legitimate independent purpose for its conduct under the Supreme Court's *Monsanto/Matsushita* standard.

arrangement. When a firm risks an immediate loss of volume, profits, or customer goodwill in announcing a higher price, it sends a strong signal to its rivals that it is safe for them to observe the same price. Such rivals will then be more likely to take the risk of acting against their own interests and falling in line with the higher price.

The cartel-enhancing effects of actions against oligopolists' self-interest are evident in the retail gasoline market. Automobile drivers do not need to know price changes in advance, because they have no way of storing excess gasoline (or changing their driving habits) in anticipation of a price increase. Thus, gasoline service stations have no legitimate independent reason for pre-announcing price changes. Indeed, pre-announcements of price increases are contrary to a station's independent interests, because they may cause consumers to immediately begin patronizing other stations. If one gasoline station does pre-announce a price increase, the announcement may signal to other stations the original station's intention to propose a higher consensus price. The other stations will have more confidence in the original station's intentions because of the risk it is taking of alienating its customers. Such a bold initiative by the original station eliminates uncertainty as to its willingness to participate in a tacit arrangement of price coordination. If other stations respond by pre-announcing a similar price increase, they send reinforcing signals back to the original station (and to all the other stations in the area) that the original station had, indeed, correctly judged its rivals' willingness to observe the consensus price. The responding stations' pre-announcements have added credibility because these stations also are risking their customers' goodwill in announcing a higher price. Such signals mutually reinforce a cartel's objectives and are no different, from an economic standpoint, than the explicit assurances that each member of a price-fixing cartel receives from its fellow conspirators.

Thus, a plaintiff should be able to meet its burden of proof in an oligopoly pricing case by demonstrating that one or more firms signaled their intention to initiate a price increase in a manner contrary to their individual self-interest and all firms in the market subsequently accepted the increase by acting in a manner no less contrary to their own interests. Under such circumstances, the initiating firm's action should be construed as an offer to participate in a price-fixing arrangement, and the other firms' conduct in response should be deemed an acceptance of that offer. This approach precisely identifies the "plus factors" necessary to prove the existence of a formal conspiracy under section 1 of the Sherman Act.

C. The Defendant's Rebuttal Case: Proving Restraints Ancillary to Joint Ventures

A court or enforcement agency should presume the illegality of a defendant's conduct once a plaintiff has proven the existence of an explicit or tacit price-fixing, output restraining, or territorial allocation conspiracy among competitors. The burden should then shift to the defendant to demonstrate that the conduct at issue was not likely to have the anticompetitive effects that normally result from a horizontal cartel. The defendant can meet its burden of proof by showing that its purpose in implementing the relevant restraint was to insure the effectiveness of an integrated joint venture designed to enhance its efficiency. In such a case, the courts and agencies should view the defendant's conduct not as a naked restraint of trade with purely anticompetitive effects but as an ancillary restraint that has the potential to benefit consumers.

1. The Ancillary Restraints Doctrine

This author has argued that, if a joint venture is legal, the courts should also permit the parties to the venture to enter into any agreements among themselves that are required to carry out the legitimate purposes of the venture.¹⁸⁰ This approach, which has been referred to as the “ancillary restraints doctrine,”¹⁸¹ was first established in an 1898 case, *United States v. Addyston Pipe & Steel Co.*¹⁸² In that case, Judge (later President and Chief Justice) William Howard Taft distinguished between “naked” restraints, which should be illegal on their face because they are unrelated to any efficiency-enhancing integration, and “ancillary” restraints, which are permissible because they are necessary to promote the legitimate objectives of a cooperative arrangement.¹⁸³

For nearly eighty years, the federal courts neglected Judge Taft’s approach. In the last twenty-five years, however, the ancillary restraints doctrine has reemerged in the lower federal courts, as they have begun to adopt a more sophisticated approach to antitrust analysis. In several cases, the federal circuit courts have separately examined competitive restraints among joint venture partners to determine whether they were necessary to promote a venture’s legitimate objectives.¹⁸⁴

Until 2006, the Supreme Court had never explicitly adopted the ancillary restraints doctrine. However, in *Texaco Inc. v. Dagher*¹⁸⁵ the Court stated in dicta that the doctrine could apply to certain restraints implemented in connection with joint ventures. The joint venture at issue had combined the gasoline refining and marketing operations of Shell and Texaco in the western United States. Prior to the formation of the joint venture, Shell and Texaco had competed in the sale of their separate brands of gasoline. After the marketing of the brands was combined in the joint venture, it established a uniform price for the sale of the two types of gasoline. The Ninth Circuit,

180. Piraino, Jr., *Beyond Per Se*, *supra* note 145, at 56 (“Any related competitive restrictions that are necessary for the legitimate purposes of a joint venture should be per se legal.”).

181. See Piraino, Jr., *High Technology Competition*, *supra* note 31, at 139 (describing the ancillary restraints doctrine).

182. 85 F. 271 (6th Cir. 1898), *aff’d*, 175 U.S. 211 (1899).

183. *Id.* at 282–83.

184. See, e.g., *SCFC ILC, Inc. v. VISA USA, Inc.*, 36 F.3d 958, 964 (10th Cir. 1994) (denial of membership in credit card system); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 211 (D.C. Cir. 1986) (noncompetition agreement among agents of van lines); *Polk Bros. v. Forest City Enters.*, 776 F.2d 185, 188–89 (7th Cir. 1985) (“A court must distinguish between ‘naked’ restraints, those in which the restriction on competition is unaccompanied by” noncompetition agreement between two stores in a shopping center); see also *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 31 (D.C. Cir. 2005) (upholding FTC decision that restrictions on marketing of particular concert recordings were not ancillary to joint venture formed to market other concert recordings). The Collaboration Guidelines provide for an ancillary restraints approach to section 1: “If . . . participants in an efficiency-enhancing integration of economic activity enter into an agreement that is reasonably related to the integration and reasonably necessary to achieve its procompetitive benefits, the Agencies analyze the agreement under the rule of reason, even if it is of a type that might otherwise be considered per se illegal.” *Collaboration Guidelines*, *supra* note 114, at 20,855.

185. 126 S. Ct. 1276 (2006).

citing this author, applied an ancillary restraints analysis to the pricing arrangement.¹⁸⁶ The Ninth Circuit concluded that the arrangement was per se illegal under the ancillary restraints doctrine, because it was not necessary to promote the legitimate objectives of the marketing joint venture between Shell and Texaco.¹⁸⁷

The Supreme Court reversed the decision of the Ninth Circuit, holding that it was not per se illegal for the Shell/Texaco joint venture to set the prices for its products.¹⁸⁸ The Court concluded that the pricing arrangement between Shell and Texaco did not constitute the type of price fixing that should be per se illegal, “because Texaco and Shell Oil did not compete with one another in the relevant market—namely, the sale of gasoline to service stations in the western United States—but instead participated in the market jointly through their investments in [the joint venture].”¹⁸⁹ The alleged price fixing by Shell and Texaco was in fact “little more than price setting by a single entity . . . and not a pricing agreement between competing entities with respect to their competing products.”¹⁹⁰ As a result, the Ninth Circuit should not have precluded the pricing arrangement under the per se rule. Since the plaintiffs had waived their rights to proceed under either the rule of reason or the quick look, the Court reversed the decision of the Ninth Circuit.¹⁹¹

Although the Supreme Court reversed the Ninth Circuit, it did acknowledge that the ancillary restraints doctrine should apply in certain circumstances. The Court stated that the “doctrine governs the validity of restrictions imposed by a legitimate business collaboration, such as a business association or joint venture, or nonventure activities. Under the doctrine, courts must determine whether the nonventure restriction is a naked restraint on trade, and thus invalid, or one that is ancillary to the legitimate and competitive purposes of the business associations, and thus valid.”¹⁹² Turning to the pricing arrangement at issue, the Court concluded that the ancillary restraints doctrine had “no application,” because the restraint at issue did not affect activities outside the scope of the joint venture: “the business practice being challenged involves the core activity of the joint venture itself—namely, the pricing of the very good produced and sold by [the joint venture].”¹⁹³

Although *Dagher* concluded that the rule of reason should apply to internal joint venture rules such as the pricing arrangement for the Shell and Texaco brands of gasoline, the logic of the decision implies that such rules should be exempt from scrutiny under section 1 of the Sherman Act altogether. Indeed, it was only because of the unique procedural posture of the case that the *Dagher* Court was unable to reach a conclusion. Once the Court decided that the per se rule was inapplicable, it could dispose of the case entirely, because the quick look was equally inapplicable and the

186. *Dagher v. Saudi Ref., Inc.*, 369 F.3d 1108, 1121 (9th Cir. 2004) (citing Piraino, Jr., *Antitrust Approach to Collaborations*, *supra* note 6, at 1188–89).

187. *Id.* at 1122.

188. *Dagher*, 126 S. Ct. at 1281.

189. *Id.* at 1279–80.

190. *Id.* at 1280.

191. *Id.* at 1281.

192. *Id.* at 1280–81 (citation omitted).

193. *Id.* at 1281. Furthermore, the Court stated that, even if the ancillary restraints approach did apply, the joint venture’s “pricing policy is clearly ancillary to the sale of its own products.” *Id.* at 1281.

plaintiffs had waived their right to proceed under the rule of reason.¹⁹⁴ The Court was clear, however, in its conclusion that the Shell/Texaco joint venture was a single entity and that, by virtue of their participation in the joint venture, Shell and Texaco had ceased to be competitors in the market for the sale of gasoline in the western United States.¹⁹⁵ Future cases, unencumbered by the unique procedural posture of *Dagher*, should recognize that firms are incapable of conspiring within the meaning of section 1 when they combine their operations in a joint venture. In such cases, any internal rules necessary for the effective operation of the joint venture do not restrict any competition that was not already eliminated as a result of the venture's formation. Accordingly, such rules should not be subject to challenge under section 1 as a potential restraint of trade.

Thus, relying on *Dagher*, the courts and agencies can easily determine the legality of horizontal price fixing and customer and territorial allocations that are implemented in connection with legitimate joint ventures. If such arrangements constitute an internal rule necessary for the effective operation of the joint venture, a defendant should be able to argue that the rule cannot be illegal under the antitrust laws. If such an arrangement affects competition outside the scope of a joint venture, a defendant will have to defend the legality of the arrangement under the ancillary restraints doctrine. Under the dicta of *Dagher*, the legality of any restraint on "nonventure activities" would depend upon whether it was "ancillary to the legitimate and competitive purposes" of the venture.¹⁹⁶ As this author argued in a series of articles beginning in 1991, the courts and agencies should make that determination by confirming whether the restraint at issue is "reasonably necessary" to promote the legitimate purposes of a joint venture.¹⁹⁷

2. Proving a Legitimate Joint Venture

The arrangement at issue cannot constitute a legitimate joint venture unless it involves more than a simple cooperative agreement between competitors. No economic benefit is possible when the parties' cooperation amounts only to the making of joint business decisions or a mere coordination of parallel activities.¹⁹⁸ By coordinating their

194. *Id.* at 1280 nn.2-3 (The "[r]espondents have not put forth a rule of reason claim" and "for the same reasons that *per se* liability is unwarranted here, we conclude that petitioners cannot be held liable under the quick look doctrine." (italics in original)).

195. See *supra* notes 186-87 and accompanying text.

196. See *supra* notes 189-90 and accompanying text.

197. See Piraino, Jr., *Antitrust Approach to Collaborations*, *supra* note 6, at 1189 ("The courts and enforcement agencies should require joint venture partners to prove that competitive restraints are 'reasonably necessary' for the accomplishment of a venture's efficiency-enhancing purposes."); Piraino, Jr., *Beyond Per Se*, *supra* note 145, at 56 ("An effective standard of legality would be whether an ancillary restraint is 'reasonably necessary' to accomplish the purposes of the joint venture."); Thomas A. Piraino, Jr., *Reconciling Competition and Cooperation: A New Antitrust Standard for Joint Ventures*, 35 WM. & MARY L. REV. 871, 924 (1994) [hereinafter Piraino, Jr., *Reconciling Competition*] ("The courts would uphold any restraint that is 'reasonably necessary' to accomplish the legitimate purposes of the cooperative arrangement . . .").

198. See *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 230 (D.C. Cir. 1986). In *United States v. Topco Assocs.*, 405 U.S. 596 (1972), the Court held a division of

efforts, the parties may only be attempting to insure the effectiveness of an anticompetitive scheme. Indeed, effective coordination of competitors' pricing or production activities is one of the hallmarks of a cartel. For example, the members of price-fixing cartels must agree on some minimum level of coordination and enforcement in order to be successful.¹⁹⁹ Such arrangements are naked restrictions of competition that should be deemed conclusively illegal.²⁰⁰

In order to meet their burden of proving a legitimate joint venture, defendants must demonstrate that the transaction joins together business functions or other resources previously held separate by the parties.²⁰¹ A cooperative arrangement among competitors can only generate efficiencies when the parties integrate their resources in some way. They may pool certain resources and assume certain common risks in order to create what is, in effect, a new entity. Items contributed by the parties may include such assets as employees, intellectual property, facilities, or distribution rights. In addition, the parties may share profits and losses and assume some of the joint venture's obligations to third parties. The parties' mutual contribution of assets and assumption of risks should create an entity that allows them to accomplish a competitive objective that they could not have achieved independently. If the parties could have accomplished their purpose separately from the joint venture, no justification exists for the harm caused to consumers or competitors by any incidental horizontal restrictions. However, as long as the joinder between the parties is substantial enough to create efficiencies that exceed the capabilities of each party individually, the parties can be viewed as partners rather than as competitors, and the restrictions need not be presumed to be illegal.

Consider the hypothetical research and development joint venture between Ford and General Motors, described in Part V.B.1, *supra*, and designed to develop a fuel-efficient-hybrid engine. Since Ford and General Motors would have integrated their relevant research operations in the venture, the venture would have access to more intellectual property and research capacity than would Ford and General Motors operating independently. The parties would have created an entity more capable of producing a hybrid engine than the companies acting on their own. Certain incidental restrictions on competition among the parties can be justified by such a joint venture's beneficial effect on consumers.

markets among independent grocery stores per se illegal. The Court emphasized that the members of the cooperative association operated independently and did not pool earnings, capital, management, or advertising resources. *Id.* at 598. As the Collaboration Guidelines recognize, "[t]he mere coordination of decisions on price, output, customers, territories, and the like" does not constitute sufficient integration to qualify for joint venture treatment. *Collaboration Guidelines, supra* note 114, at 20,855.

199. Indeed, the courts often use such coordination and enforcement to infer the existence of a per se illegal price fixing conspiracy. See *Albrecht v. Herald Co.*, 390 U.S. 145, 149–50 (1968) (inferring a price fixing conspiracy when a newspaper hired outside agents to enforce maximum resale prices), *overruled on other grounds*, *State Oil Co. v. Kahn*, 522 U.S. 3 (1997); *United States v. Parke, Davis & Co.*, 362 U.S. 29, 45 (1960) (inferring an illegal conspiracy from wholesalers' policing and enforcement of suggested resale prices).

200. See *Arthur, supra* note 39, at 377 ("The paradigm of a naked restraint is a classic cartel price-fixing agreement.").

201. See *id.* at 376 ("[E]conomic integration . . . is vital to productive efficiency.").

3. Proving Restraints Ancillary to Joint Ventures

Once a defendant proves the existence of a legitimate joint venture, a court or agency should consider the appropriateness of any related restrictions on competition agreed to by the partners of that venture. Building on the Supreme Court's recent decision in *Dagher*, the courts and agencies can establish a simple method for confirming the legality of such restraints. If the restraint at issue constitutes an internal rule necessary for the effective operation of an integrated joint venture, it should be regarded as single entity conduct exempt from section 1 entirely. The courts and agencies only need to consider the reasonableness of restraints that affect competition outside the scope of a joint venture's activities. For such restraints, an ancillary restraints analysis is appropriate. The courts and agencies should uphold any restraints that are reasonably necessary to promote a joint venture's legitimate purposes, and they should preclude any restraints that are broader than necessary to further such objectives.

Internal joint venture rules exempt from antitrust scrutiny should be readily apparent to fact finders. Consider the hypothetical Ford/General Motors research and development joint venture for a hybrid engine, described in Part V.B.1, *supra*. Ford and General Motors should be allowed to exchange the proprietary information required to conduct the venture's research programs; they should be able to limit the parties who can participate in the joint venture or who can access the technology developed by the joint venture;²⁰² and they should be permitted to agree not to separately undertake the venture's research activities or to otherwise compete with the venture. All of these activities should be exempt from antitrust scrutiny, because they do not eliminate any competition between the parties that continued after the joint venture's formation. The exchange of proprietary information is naturally contemplated by any research and development joint venture. Indeed, such joint ventures could not operate effectively without a free exchange of technological information with their partners. Restrictions on the parties who can join a research and development joint venture or access its technology are no less necessary for the effectiveness of such a venture. Finally, by agreeing not to compete with their own joint venture, Ford and General Motors would simply be acknowledging a natural effect of the joint venture's formation. Joint venture partners are unlikely to compete with their own affiliate in any

202. Courts should not allow access restrictions, however, when a joint venture controls an "essential facility" necessary to compete in the relevant market. The courts have required joint ventures that control such facilities to grant open access to all qualified parties. *See Silver v. New York Stock Exch.*, 373 U.S. 341 (1963) (precluding members of New York Stock Exchange from denying access to private wire system necessary for broker-dealers to trade in over-the-counter securities market); *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.*, 364 U.S. 656 (1961) (finding it *per se* illegal for industry-wide standards-setting organization to refuse to provide its "seal of approval" to plaintiff's gas burner); *Associated Press v. United States*, 326 U.S. 1 (1945) (requiring Associated Press to allow all qualified newspapers to receive its wire reports); *United States v. Terminal R.R.*, 224 U.S. 383 (1912) (requiring railroad association which controlled only means of access across Mississippi River to St. Louis to allow other railroads to use facilities upon equal terms).

event, because such competition merely reduces their profits as partners of the venture.²⁰³

In certain cases a defendant may be able to prove, as in *Dagher*, that a pricing arrangement should be exempt from antitrust scrutiny because it constitutes an internal rule necessary for the effective operation of a joint venture. A price-fixing arrangement might be necessary for the effectiveness of an industry-wide venture for the marketing of a unique product (such as the copyrighted musical compositions in *BMI*).²⁰⁴ It should be particularly easy for defendants to prove that price-fixing arrangements are necessary for purchasing joint ventures. Most purchasing joint ventures are formed by sellers in order to reduce their purchasing costs.²⁰⁵ Since purchasing joint ventures themselves have a net beneficial effect, sellers should be permitted to take the steps necessary to meet their legitimate objectives.²⁰⁶ In most cases, it will be necessary for a purchasing joint venture to submit a single bid on behalf of all its members in order to achieve its legitimate purpose. The partners to a purchasing joint venture cannot integrate their purchasing operations and reduce costs without allowing the joint venture to negotiate purchase prices on their behalf. The submission of joint bids is a natural consequence of the integration of purchasing functions in a joint venture. Indeed, after they have combined their purchasing functions in a joint venture, the partners should have no choice other than to submit joint bids to their suppliers.

Restrictions that affect competition outside the scope of a joint venture should continue to be subject to antitrust regulation under the ancillary restraints approach

203. See *United States v. Penn-Olin Chem. Co.*, 378 U.S. 158, 169 (1964) (“If the parent companies are in competition, . . . it may be assumed that neither will compete with the progeny in its line of commerce.”).

204. *Broad. Music, Inc. v. CBS*, 441 U.S. 1, 21–23 (1979). There is other precedent in the Supreme Court for allowing a defendant to prove the potential beneficial effects of price fixing. See *Appalachian Coals, Inc. v. United States*, 288 U.S. 344, 359 (1933) (upholding an arrangement under which coal producers fixed the price of coal in order to eliminate “destructive trade practices”); *Chicago Bd. of Trade v. United States*, 246 U.S. 231 (1918) (sustaining a Chicago Board of Trade rule which froze grain prices during the period the market was closed).

205. Purchasing joint ventures have a minimal anticompetitive effect because they operate at the upstream level of the production process. As long as they are confined to the purchasing level, such joint ventures cannot affect their partners’ decisions on output or on pricing. Some commentators have argued that joint purchasing arrangements should be treated even more leniently than joint ventures among sellers. Jonathon M. Jacobson & Gary J. Dorman, *Joint Purchasing, Monopsony, and Antitrust*, 36 ANTITRUST BULL. 1, 4 (1991) (“[T]he antitrust treatment of joint buyer activity should not be symmetric to the treatment of joint seller activity.”); see also Piraino, Jr., *Reconciling Competition*, *supra* note 197, at 922 (“Purchasing cooperatives . . . are not likely to increase the price or limit the availability of consumer end products.”).

206. Many commentators have argued that the antitrust laws should not interfere with buyers’ joint purchasing activities. *E.g.*, Jacobson & Dorman, *supra* note 205, at 23 (“[A]ntitrust rules should be designed to avoid interfering with most joint purchasing activities.”); Michael K. Lindsey, *Joint Purchasing Arrangements*, 61 ANTITRUST L.J. 401, 402 (1993) (suggesting that competitors that agree to jointly purchase resale inventory can buy at lower prices and increase efficiency).

described in *Dagher*.²⁰⁷ Consider the hypothetical Ford/General Motors research and development joint venture for a new hybrid engine. Assume that Ford and General Motors agree to fix the price at which they will sell hybrid engines using the technology developed by the joint venture. Such a restriction should be illegal under an ancillary restraints analysis. The pricing arrangement would not be reasonably necessary to accomplish the joint venture's legitimate purposes. In order to effectively develop a new hybrid engine, the parties would have no need to limit competition in their ultimate use of the engine. Thus, the pricing arrangement should be illegal as a naked restraint of trade.

VII. CONDUCT REQUIRING A PRIORITIZED MARKET ANALYSIS

The likely effects of certain competitive conduct will not be obvious from its structure or the parties' purpose. In such cases, the courts and agencies will have to engage in a more complex market analysis. A market-based analysis is appropriate in cases involving monopoly conduct by individual firms, tying and exclusive dealing, and horizontal mergers and joint ventures. Such conduct should be arrayed at the middle portions of the antitrust continuum, where there would be no presumption of legality or illegality. Instead, the plaintiff and the defendant would have the normal burdens of proof and rebuttal.

The courts and agencies can simplify their analysis in monopolization, tying, exclusive dealing, and horizontal merger and joint-venture cases by establishing a market-power threshold for the plaintiff's prima facie case. If a plaintiff fails to meet its initial burden of proving market power in excess of the applicable threshold, a court or an agency can dismiss the case without considering other more complex economic factors (such as entry conditions in the market or the efficiencies likely to be generated by the relevant transaction).

Consumers cannot be harmed in monopolization, tying, exclusive dealing, or horizontal merger or joint-venture cases when defendants lack substantial market power. A firm cannot unilaterally extend or perpetuate its market power if it holds less than a monopoly share of the relevant market. If such a firm attempts to compete other than on the merits, other firms should be able to step in and steal market share from it. When the parties to a merger or a joint venture have a relatively small market share, they will not be able to raise prices above the normal competitive level after the transaction is consummated.²⁰⁸ Similarly, without a significant share of the applicable product market, a manufacturer cannot force a substantial number of its customers to buy the product exclusively from it or to forego purchasing the product from its competitors.²⁰⁹

Once a plaintiff meets its burden of proving market power in a case involving monopolization, tying, exclusive dealing, or a horizontal merger or joint venture, the burden should shift to the defendant to demonstrate that, despite its market power, the net effect of its conduct will be beneficial to consumers. A monopolist may have obtained a large share of the relevant market, not because of any exclusionary business

207. See *supra* Part VI.C.1.

208. See *supra* notes 66–69 and accompanying text.

209. See *supra* notes 96–97 and accompanying text.

practices, but simply because it provided consumers with the best products at the lowest possible prices. The net effect of an exclusive dealing arrangement may not be to exclude competitors from the relevant market but to provide enhanced point-of-sale services to consumers. A tying arrangement may be designed to insure the effective functioning of two related products. A merger or joint venture between relatively large competitors may allow the new entity to achieve efficiencies in the production or delivery of products to consumers that outweigh the adverse competitive effects of the combination.

A. Tying and Exclusive Dealing Arrangements

Tying and exclusive dealing arrangements are just as likely to enhance as to limit competition. Such arrangements can further a manufacturer's effectiveness in competing against other brands;²¹⁰ they can also deprive consumers of choice and competitors of access to important markets.²¹¹ Thus, it is not appropriate for courts or enforcement agencies to indulge in any presumptions of legality or illegality for such

210. The courts have upheld tying arrangements in cases where two products had to be used in conjunction with one another to insure the proper functioning of either product. *See* *Mozart Co. v. Mercedes-Benz of N. Am., Inc.*, 833 F.2d 1342, 1351 (9th Cir. 1987) (upholding requirement that automobile dealers purchase replacement parts from automobile manufacturer); *Dehydrating Process Co. v. A.O. Smith Corp.*, 292 F.2d 653, 656–57 (1st Cir. 1961) (approving tie-in of unloading device and silo on grounds that separate sales had led to widespread customer dissatisfaction); *United States v. Jerrold Elecs. Corp.*, 187 F. Supp. 545, 556–57 (E.D. Pa. 1960) (approving sale of components of television antenna as single system in order to assure effective functioning of system), *aff'd per curiam*, 365 U.S. 567 (1961). The courts have also permitted exclusive dealing arrangements that enhance interbrand competition. *See* *Roland Mach. Co. v. Dresser Indus., Inc.*, 749 F.2d 380, 395 (7th Cir. 1984) (stating that an exclusive dealing arrangement may encourage a dealer to promote the manufacturer's product more vigorously); *Am. Motor Inns, Inc. v. Holiday Inns, Inc.*, 521 F.2d 1230, 1252 (3d Cir. 1975) (stating that a hotel chain's exclusionary agreements with franchisees were justified, in part, by the chain's desire to strengthen its position against its competitors); Howard P. Marvel, *Exclusive Dealing*, 25 J.L. & ECON. 1, 3 (1982) (stating that exclusive dealing can increase a distributor's promotional efforts).

211. By requiring customers to deal exclusively with it, a supplier can prevent its competitors from accessing potential sales outlets. *See* *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984) (O'Connor, J., concurring) (stating that exclusive dealing can deprive other suppliers of a market for their goods and other buyers of supply sources). A buyer also can deprive competitors of a potential source of supply by requiring suppliers to sell solely to it. *See id.* Tying arrangements can force consumers to buy products they would not otherwise have purchased or to pay higher prices than they would in a competitive market. When a firm is successful in tying the purchase of one product to another, it can raise barriers to entry in the tied product market (thereby excluding potential competitors) and can insulate potentially inferior products from competition by current manufacturers. *See id.* at 14–15 (explaining anticompetitive effects of tying arrangements); *United States v. Loew's, Inc.*, 371 U.S. 38, 51–52 (1962) (holding that the block booking of films for television raised barriers to entry for potential competitors and was illegal), *overruled in part by* *Ill. Tool Works Inc. v. Indep. Ink, Inc.*, 126 S.Ct. 1281 (2006); Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price*, 96 YALE L.J. 209, 215–19, 234–48 (1986) (explaining how ties can raise costs).

conduct. Instead, courts and agencies should allocate the ordinary burden of proof to the plaintiff and the ordinary burden of rebuttal to the defendant.

1. The Plaintiff's Initial Burden of Proof

The plaintiff in a tying or exclusive dealing case should have the initial burden of proving that the parties to such arrangements hold a market share in excess of thirty percent.²¹² Consumers or competitors cannot be harmed by tying or exclusive dealing arrangements implemented by firms that control less than thirty percent of the relevant market. Without a significant share of the tying product market, a manufacturer cannot force a buyer to purchase a tied product or to pay a supracompetitive price. Consumers are not unfairly disadvantaged when they can freely choose whether or not to purchase the product. An exclusive dealing arrangement also cannot adversely affect competitors unless a defendant has enough power to foreclose a significant number of supplier or customer outlets. A firm without market power will be unable to "lock up" a significant number of suppliers or customers through exclusive dealing arrangements. As a result, competitors will have access to sufficient remaining outlets to compete effectively in the relevant market.²¹³

2. The Defendant's Rebuttal Case

Once a plaintiff has demonstrated that a defendant controls more than thirty percent of the relevant market, the defendant should have the opportunity to rebut by proving that it had a procompetitive purpose for a tying or exclusive dealing arrangement. In the case of tying arrangements, the courts can avoid the complicated task of weighing the defendant's efficiency justifications against the plaintiff's proof of market power. The procompetitive justifications for tying arrangements are limited, but, once proven, they should be decisive. A tying arrangement should be permitted if a defendant can demonstrate that the tie was necessary for the quality, safety, or effectiveness of its products. A defendant may be able to prove that two products had to be bundled in order to function effectively. A defendant should also be able to justify its conduct

212. In *Jefferson Parish*, the Supreme Court found that a market share of thirty percent was not sufficient to prove the illegality of a tying arrangement. 466 U.S. at 31–32. Since *Jefferson Parish*, many lower federal courts have used thirty percent as a market-share threshold for tying arrangements. See, e.g., *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792, 797 (1st Cir. 1988); *M. Leff Radio Parts, Inc. v. Mattel, Inc.*, 706 F. Supp. 387, 399 (W.D. Pa. 1988). The concurring opinion in *Jefferson Parish* also applied a thirty percent market-share threshold to exclusive dealing arrangements. 466 U.S. at 46 (O'Connor, J., concurring).

213. The courts have traditionally judged the legality of exclusive dealing arrangements on the basis of whether they foreclose a significant number of buyer or seller outlets from competitors. See, e.g., *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 334 (1961) (holding a requirements contract legal in the context of the competitive bituminous coal market); *Standard Fashion Co. v. Magrane-Houston Co.*, 258 U.S. 346, 357 (1922) (holding that an exclusive dealing contract between a pattern manufacturer and a merchant substantially lessened competition in violation of the Clayton Act); *Joyce Beverages, Inc. v. Royal Crown Cola Co.*, 555 F. Supp. 271, 278 (S.D.N.Y. 1983) (holding that an exclusive cola franchise was not illegal because it encouraged rather than foreclosed competition).

whenever it can show that a new product integration had a plausible efficiency benefit. If the newly packaged product enhances performance or lowers cost, it should be permitted even if it was adopted in part to preclude competition.²¹⁴ As one commentator has stated, “[I]f engineering data suggest that a new product is superior to the product it replaces, antitrust inquiry should end.”²¹⁵ Assume, for example, that a tobacco company developed a special filter that could be attached to a cigarette and would prevent any harmful by-products from entering smokers’ lungs. Such a technological breakthrough would give the tobacco company a significant advantage over its competitors. However, the antitrust laws should not preclude the company from requiring consumers to purchase cigarettes with the filter attached.

The courts will have to undertake a more detailed balancing analysis for exclusive dealing arrangements with customers. Such arrangements can enhance competition by encouraging distributors to promote a manufacturer’s products more aggressively, but they can also restrict competition by denying other manufacturers access to the customers covered by the exclusive deal. It is therefore insufficient for a defendant merely to show that it had a procompetitive purpose for an exclusive dealing arrangement with its customers. The courts must balance such purpose against the potential foreclosure of outlets resulting from the arrangement. The greater the manufacturer’s market share, the more difficult it should be for it to prevail. A manufacturer with a large market share has the ability to foreclose a greater number of distribution outlets from its competitors. Moreover, such a manufacturer would have less need to use an exclusive dealing arrangement to enhance its ability to compete against other brands. Such a manufacturer would have a heavier burden in rebutting a plaintiff’s prima facie proof of illegality.

It might be possible, however, for manufacturers with large, but declining, market shares to prove the legality of an exclusive dealing arrangement. Consider a requirement by General Motors that its dealers buy automobiles only from it and not from its rivals. In rebutting a plaintiff’s case attacking the exclusive dealing arrangement, General Motors could demonstrate that the landscape of the U.S. automotive market has changed dramatically in the last two decades, “from a cozy, three-way oligopoly . . . [among Ford, General Motors, and Chrysler] to a knife fight among six to eight global players.”²¹⁶ General Motors’s share of the domestic automobile market has declined from 46 % in the 1950s to 25.6% in 2004, as foreign manufacturers such as Toyota and Honda have increased their own market share.²¹⁷

214. See *In re IBM Peripheral EDP Devices Antitrust Litig.*, 481 F. Supp. 965, 1005 (N.D. Cal. 1979) (holding that IBM did not violate section 2 by tying its computer central processing unit to its peripheral devices, because the combination resulted in an improved design), *aff’d sub nom.* *Transamerica Computer Co. v. IBM Corp.*, 698 F.2d 1377 (9th Cir. 1983).

215. Janusz A. Ordover & Robert D. Willig, *An Economic Definition of Predation: Pricing and Product Innovation*, 91 YALE L.J. 8, 29 (1981).

216. Joseph B. White & Jeffrey McCracken, *Troubled Legacy: How U.S. Auto Industry Finds Itself Stalled by Its Own History*, WALL ST. J., Jan. 7, 2006, at A1.

217. See Gregg Easterbrook, *What’s Bad for G.M. Is . . .*, N.Y. TIMES, June 12, 2005, at WK1 (describing GM’s forty-six percent share of the domestic automobile market in the 1950s and stating that “Toyota is on pace to pass [GM] as the world’s No. 1 automaker”); Lee Hawkins, Jr., Neal E. Boudette & Kris Maher, *Wielding the Ax: GM, Amid Industry Overhaul, Cuts Health Benefits for Retirees*, WALL ST. J., Oct. 18, 2005, at A1 (describing GM’s current

General Motors could argue that it should be allowed to require its dealers to purchase automobiles exclusively from it so that it could compete more effectively against such foreign rivals.

It should be difficult for a defendant to rebut a plaintiff's prima facie case against an exclusive dealing arrangement involving suppliers. A firm with market power can substantially harm its rivals by tying up critical sources of supply in the relevant market. Ford, for example, has accused Toyota of attempting to control the key suppliers of components for hybrid engines, in order to prevent Ford and other automobile companies from obtaining the components they need to manufacture their own hybrids.²¹⁸ Such actions could limit innovation in the hybrid engine market and deprive consumers of alternative sources of more fuel-efficient automobiles. Toyota could only prevail in an antitrust action by Ford if it could demonstrate that its exclusive dealing arrangements with suppliers of hybrid components had a legitimate efficiency justification, such as assuring Toyota of an adequate supply of scarce components for its hybrid engines.

B. Monopoly Cases

In monopoly cases, the plaintiff should have the burden of proving both that the defendant possesses monopoly power and that it has misused its monopoly power in some manner. If the plaintiff meets its burden of proof, the defendant should have an opportunity to rebut by proving that it had a legitimate business justification for the conduct at issue.

1. The Plaintiff's Burden of Proof

Most courts and agencies have equated monopoly power with a market share in excess of seventy percent. Such firms usually have the power to raise prices unilaterally and to establish the standards for service, quality, and innovation in the relevant market.²¹⁹ In cases brought under section 2 of the Sherman Act, the plaintiff should have the initial burden of proving that the defendant possesses the requisite

market share of 25.6%).

218. See Norihiko Shirouzu & Jathon Sapsford, *Power Struggle: As Hybrid Cars Gain Traction, Industry Battles Over Designs*, WALL ST. J., Oct. 19, 2005, at A1 (referring to statement by Ford spokesperson that "Toyota is trying to squeeze the supply of components" used in hybrid engines).

219. See *United States v. E.I. DuPont de Nemours & Co.*, 351 U.S. 377, 379, 391 (1956) (inferring monopoly power from seventy-five percent market share); *Colo. Interstate Gas Co. v. Natural Gas Pipeline Co. of Am.*, 885 F.2d 683, 694 n.18 (10th Cir. 1989) ("[To establish] monopoly power, lower courts generally require a minimum market share of between 70% and 80%."); *Exxon Corp. v. Berwick Bay Real Estate Partners*, 748 F.2d 937, 940 (5th Cir. 1984) ("[M]onopolization is rarely found when the defendant's share of the relevant market is below 70%."); *Heattransfer Corp. v. Volkswagenwerk, A.G.*, 553 F.2d 964, 981 (5th Cir. 1977) (noting that seventy-one to seventy-six percent market share supports inference); *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 424 (2d Cir. 1945) (stating that ninety percent market share supports inference); *Illinois ex rel. Hartigan v. Panhandle E. Pipe Line Co.*, 730 F. Supp. 826, 902 (C.D. Ill. 1990) ("Where the record reveals a market share of 70 to 80%, courts have simply inferred the existence of monopoly power without specifically examining . . . control over prices [or] competition . . ."), *aff'd*, 935 F.2d 1469 (7th Cir. 1991).

monopoly power. A court or an agency should dismiss any section 2 case in which the plaintiff fails to prove that the defendant controls at least seventy percent of the relevant market. However, proving a defendant's mere possession of monopoly power should not suffice to prove a section 2 violation. A plaintiff should also have to make out a prima facie case that a defendant has misused its monopoly power to exclude actual or potential rivals from the market.

Placing this additional burden of proof on the plaintiff is necessary because firms should not be punished simply for obtaining monopoly power.²²⁰ Consumers benefit when firms fight aggressively to enhance their market power. Monopolies often represent the triumph of the most efficient firm in the relevant market. Firms usually obtain the greatest share of a particular market because they have provided consumers with the best products at the lowest possible prices. As a recent *Wall Street Journal* editorial said of Wal-Mart, "You don't sell \$300 billion a year worth of anything without doing something right."²²¹

Consider the reasons for Microsoft's 90 percent share of the market for personal computer operating systems.²²² Many observers argue that Microsoft gained its monopoly power because its "Windows" operating system was the most efficient, cost-effective product in the market.²²³ One commentator recently opined, "[N]o company anywhere has done more to put high-quality software into more people's hands."²²⁴

220. As one commentator recently explained, "The innovative firm that invents the better mousetrap may harm its rivals, but at the same time, also does society a great service. The injured rival that burns down the innovator's factory or slanders its product does not. A defensible definition of 'monopolize' would presumably distinguish between the two." Alan J. Meese, *Monopolization, Exclusion, and the Theory of the Firm*, 89 MINN. L. REV. 743, 744 (2005). The Supreme Court has consistently recognized, since 1904, that monopoly power itself should not violate section 2 of the Sherman Act. See *United States v. U.S. Steel Co.*, 251 U.S. 417, 449–50 (1920); *Standard Oil Co. v. United States*, 221 U.S. 1, 62, 75–77 (1911); *N. Sec. Co. v. United States*, 193 U.S. 197 (1904). In *Verizon Communications, Inc. v. Trinko*, 540 U.S. 398 (2004), the Court refused to find a monopoly telephone company liable under section 2 for denying a rival access to its telephone network. The Court emphasized that the pursuit of "monopoly prices . . . is an important element of the free-market system. . . . [It] is what attracts 'business acumen' in the first place . . ." *Id.* at 407.

221. Editorial, *Is Wal-Mart Good for America?*, WALL ST. J., Dec. 3, 2005, at A10.

222. Steve Lohr, *Can This Man Reprogram Microsoft?*, N.Y. TIMES, Dec. 11, 2005, at BU4.

223. See, e.g., Ben Heskett & Michael Kanellos, *Ballmer: MS is the American Way*, CNET NEWS.COM, Dec. 5, 1997, http://news.com.com/Ballmer+MS+is+the+American+way/2100-1023_3-206065.html ("I think what we're doing is right, lawful, moral, proper, and competitive. I might even say it's the American way. We're innovating, adding value, driving down prices, competing, serving our customers, and we're doing it well. A lot of other companies in the United States are benefiting because they're building on top of our platform and thriving. I might start playing the "Star-Spangled Banner" if I went on too long.") (quoting Steve Ballmer, Executive Vice President of Microsoft Corp.).

224. Lee Gomes, *Microsoft Complains About Complacency, But Who Is at Fault?*, WALL ST. J., Sept. 22, 2003, at B1. Some commentators, in fact, argue that Windows constitutes a "natural monopoly," due to the fact that consumers prefer the ease of using a single standard for all personal computer applications programs. See David Balto & Robert Pitofsky, *Antitrust and High-Tech Industries: The New Challenge*, 43 ANTITRUST BULL. 583, 604 (1998) ("In industries characterized by networks, even monopoly is seen by some observers as inevitable and merely an accommodation to consumer demand for a compatible technical standard.").

Although firms should be permitted to obtain monopoly power through superior efficiency, their conduct should be more closely regulated after they have achieved such power. Because of their market power, monopolists have an enhanced ability to affect consumers, either for good or for ill. As the Supreme Court emphasized in the 1932 case *United States v. Swift & Co.*, “[S]ize carries with it an opportunity for abuse that is not to be ignored.”²²⁵ Because of their ability to control the relevant market, monopolists often can perpetuate or extend their monopoly power for reasons unrelated to the quality of their products or services.

The courts have held that certain conduct that would be perfectly permissible for a firm with a small market share can be illegal when undertaken by a monopolist.²²⁶ The courts have been unable, however, to establish a consistent dividing line between monopolists’ permissible and illegal conduct. For example, although tying and exclusive dealing arrangements have similar competitive effects, the courts have treated monopolists’ tying arrangements more severely.²²⁷ Because it lacks a valid economic basis, the courts’ current approach to monopoly conduct has confused practitioners and business executives as to the applicable standards of behavior for firms with large market shares.²²⁸ The courts and agencies should more clearly define how a plaintiff can meet its burden of proving wrongful acts by monopolists in section 2 cases. Conduct should be illegal under section 2 if it is contrary to a monopolist’s legitimate self-interest in enhancing its efficiency and “makes no economic sense other than as a means of perpetuating or extending monopoly power.”²²⁹ Such a standard would preclude conduct harmful to consumers without deterring monopolists from improving their products and services. When monopolists intentionally incur losses that are contrary to their immediate self-interest, it is reasonable to assume that they anticipate a long-term benefit that will outweigh such losses. Such benefit usually results from the maintenance or extension of a monopolist’s market power. Consumers are harmed in such cases, because, instead of competing aggressively on the merits, monopolists refrain from competition in order to obtain the long-term benefits of enhanced market power.

Consider the most common types of monopolistic conduct: access restrictions, tying, exclusive dealing, predatory pricing, and fraudulent trade practices such as false product pre-announcements and sham litigation. Each of these acts appears irrational

225. 286 U.S. 106, 116 (1932).

226. See *supra* notes 85–86, 92, 98–100 and accompanying text.

227. See Piraino, Jr., *Identifying Monopolists*, *supra* note 85, at 836; *supra* notes 94–100 and accompanying text.

228. See *Telex Corp. v. IBM Corp.*, 367 F. Supp. 258, 833–44 (N.D. Okla. 1973). Recognizing the lack of clear standards in monopolization cases, the FTC and DOJ planned hearings for early 2006 to recommend better means of determining “when specific types of single-firm conduct are pro-competitive or benign, and when they may harm consumers.” *Hearings To Focus on Antitrust Implications of Single-Firm Conduct*, Trade Reg. Rep. (CCH) No. 919, at 1 (Dec. 1, 2005).

229. Piraino, Jr., *Identifying Monopolists*, *supra* note 85, at 845; see also John E. Lopatka & William H. Page, *Bargaining and Monopolization: In Search of the “Boundary of Section 2 Liability” Between Aspen and Trinko*, 73 ANTITRUST L.J. 115, 122 (2005) (“If it makes no sense for a rational firm to adopt the practice other than as a means of enhancing monopoly power, it is more likely to be characterized as unlawfully exclusionary.”).

on its face because it is likely to inflict immediate losses upon a monopolist. Access restrictions limit the potential market for a monopolist's products or services. Tying arrangements generate ill will with customers who are forced to purchase unwanted products.²³⁰ Exclusive dealing arrangements waste bargaining leverage that a monopolist could have used to obtain concessions on price, delivery, and other terms of sale from its customers and suppliers. Predatory pricing requires a monopolist to forego profits on each product that it sells. A monopolist alienates its customers and wastes its own resources when it makes false announcements about future products or pursues baseless litigation.

No firm, however, intentionally engages in conduct that will harm it in the marketplace. There must be an explanation for monopolists' willingness to incur losses in implementing access restrictions, tying and exclusive dealing arrangements, predatory pricing, or fraudulent trade practices. A firm would not want to forego profits, irritate its customers, reduce its sales, or waste scarce resources unless it perceived a payback that compensated for such losses. In the case of a monopolist, the payback often comes from its ability to exclude competitors that might threaten its monopoly position in its current market or in a new market to which it is attempting to extend its monopoly power.²³¹ For example, when Microsoft designs its Windows operating system in a way that makes it difficult for competitors' word-processing, Internet-access, or other applications programs to run on the system, Microsoft is acting against its own legitimate self-interest in making Windows a universal platform for all related applications. In such a case, a court or enforcement agency can assume that Microsoft's only purpose is to extend its monopoly power from the operating-systems market to various applications markets.²³²

2. The Defendant's Rebuttal Case

Once the plaintiff demonstrates that the defendant possesses monopoly power and has used that power in a manner that appears to be contrary to its legitimate economic interest, the burden should shift to the defendant to demonstrate that it actually had a legitimate business justification for the conduct at issue. Shifting the burden to the

230. In *Alaska Airlines v. United Airlines*, 948 F.2d 536, 549 (9th Cir. 1991), the Ninth Circuit pointed out the usual lack of any economic rationale for such conduct: "Every time the monopolist asserts its market dominance on a firm in the leveraged market, the leveraged firm has more incentive to find an alternative supplier . . ."

231. Some courts have inferred a section 2 violation when monopolists have incurred short-term costs in order to drive a rival from the market. See *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 608-11 (1985) (pointing out that "jury may well have concluded that [defendant] elected to forego . . . short-run benefits" in refusing to deal with plaintiff and that evidence supported inference that defendant was "willing to sacrifice short-run benefits and consumer goodwill in exchange for a perceived long-run impact on its smaller rival"); *Advanced Health-Care Servs. v. Radford Cmty. Hosp.*, 910 F.2d 139, 148 (4th Cir. 1990) ("[I]f a plaintiff shows that a defendant has harmed consumers and competition by making a short-term sacrifice in order to further its exclusive, anti-competitive objectives, it has shown predation by that defendant.").

232. See Piraino, Jr., *Identifying Monopolists*, *supra* note 85, at 852-55 (describing ways in which Microsoft can misuse its monopoly power).

monopolist to prove a benign intent for its conduct is fair because the monopolist is the party with access to the evidence that will prove its legitimate competitive purpose. Documentary evidence should be particularly helpful in establishing a monopolist's intent. Most large corporations engage in considerable strategic planning concerning their competitors. Formal strategic plans, memoranda, e-mail and other internal correspondence, and minutes of meetings often will reveal a monopolist's purpose for a particular course of conduct.²³³

Monopolists' tying arrangements, access restrictions, below-market pricing, product pre-announcements, and litigation practices all may have a legitimate purpose. Such conduct may be designed not to drive rivals from the market but to preserve efficiencies beneficial to consumers. An ostensible tying arrangement may actually be intended to insure the effective functioning of integrated products.²³⁴ Although some commentators have claimed that Microsoft has tied features such as its Web browser and word-processing system into its Windows operating system for anticompetitive purposes,²³⁵ Microsoft has actually improved the functionality of its operating system by providing a seamless means by which users can move back and forth among various applications.²³⁶

An access restriction may be designed to insure that a third party is qualified to use a monopolist's resources. For example, Microsoft may be able to prove that the interfaces to its operating system were designed, not to exclude competing applications programs, but to insure the efficient operation of its Windows program. Similarly, a monopolist's low prices may simply reflect a lower cost structure resulting from its economies of scale and may not require a monopolist to incur any short-term losses at all.²³⁷ Pre-announcements by monopolists of legitimate product improvements may be intended to assist consumers in planning their future purchases.²³⁸ Finally, litigation by

233. See Lawrence A. Sullivan, *Monopolization: Corporate Strategy, the IBM Cases, and the Transformation of the Law*, 60 TEX. L. REV. 587, 634 (1982) ("The end products of corporate strategic planning can provide solid evidence of corporate intent . . .").

234. The courts have upheld tying arrangements designed to integrate separate components necessary for the effective functioning of a product. See *supra* note 207.

235. See, e.g., Lohr, *supra* note 222 ("Microsoft has bundled outstanding programs with mediocre ones, and all of them typically become the industry standards.")

236. See *United States v. Microsoft Corp.*, 84 F. Supp. 2d 9, 55 (D.D.C. 1999) (findings of fact) ("[C]onsumers can be said to benefit from Microsoft's provision of Web browsing functionality with its Windows operating system at no additional charge."); Ronald A. Cass, *The Terms of Trade: Antitrust a la Carte*, WALL ST. J., Dec. 16, 2005, at A18 ("Years ago, Microsoft combined its more cumbersome, less user-friendly DOS program with an optical interface program to create Windows. It has been adding features . . . and expanding what its operating system does ever since. Consumers have approved that approach to product evolution.")

237. Since discount pricing is so beneficial to consumers, a monopolist should not be liable for any sales made at prices above its marginal costs. See Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697, 711-12 (1975) (concluding that sales by monopolist should be legal if made at prices equal to or above marginal cost and illegal if made at prices below marginal cost).

238. See Piraino, Jr., *Identifying Monopolists*, *supra* note 85, at 877 ("Consumers generally benefit from pre-announcements because they provide valuable information about forthcoming products.")

a monopolist against its competitors may have the legitimate purpose of protecting its intellectual property rights.²³⁹

A monopolist should not, however, be able to meet its burden of proving a legitimate justification for an exclusive dealing arrangement. In a competitive market, a firm may have legitimate reasons for requiring its customers and suppliers to deal exclusively with it and not with its competitors. For example, exclusive dealing contracts with customers may force a reseller to concentrate on promoting the seller's products and prevent it from giving rivals a free ride on the seller's promotional efforts.²⁴⁰ Such rationale, however, do not apply to monopolists. Since a monopolist's products are, by definition, already dominant in the relevant market, it need not require its resellers to focus their efforts exclusively on its products. Furthermore, a monopolist incurs short-term costs when it imposes exclusive dealing arrangements on its customers or suppliers. Such agreements reduce a monopolist's reservoir of goodwill with its customers and suppliers and use up leverage with which a monopolist could have pursued concessions on price, delivery, and other terms of sale. A monopolist would risk incurring such short-term costs only if it believed that in the long run, it could benefit by making it more difficult for potential rivals to access the customer or supplier outlets necessary to survive in the relevant market. Since exclusive dealing arrangements raise the already-high barriers to entry in monopoly markets, the courts and agencies should preclude monopolists from entering into such arrangements with any customer or supplier.

C. Horizontal Mergers

In horizontal merger cases, the plaintiff should have the initial burden of proving that the parties to the merger have a collective market share in excess of a particular threshold. If the plaintiff meets its burden of proof, the parties to the merger should have an opportunity to rebut by proving that factors such as ease of entry, lack of unilateral or coordinated effects, and efficiencies will eliminate or mitigate the potential adverse competitive effects of the merger.

1. The Plaintiff's Burden of Proof

The plaintiff should have the initial burden of proving the market power of the parties in merger cases brought under section 7 of the Clayton Act. By considering the parties' market power at the first stage of their analysis, the courts and agencies can confirm the legality of many mergers without any further inquiry.

The courts and agencies should create safe harbors of legality for mergers that create entities that have up to a thirty percent market share. Such transactions do not have the potential to generate any real anticompetitive effects. In such cases, there is no

239. See *id.* at 878–79 (“In most cases monopolists have legitimate reasons to assert their regulatory and intellectual property rights.”).

240. See *Cont'l T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 55 (1977) (preventing free riding may justify certain restraints placed by a seller on its customers); *Joyce Beverages, Inc. v. Royal Crown Cola Co.*, 555 F. Supp. 271, 278 (S.D.N.Y. 1983) (“[Exclusive dealing] insures that the [retailer] devotes undivided loyalty to its particular brand and that it competes vigorously against all competing brands.”).

need for the courts to consider any mitigating factors, such as ease of entry or the potential for efficiencies. The Merger Guidelines of the DOJ and FTC recognize that “[m]ergers that . . . do not significantly increase concentration . . . ordinarily require no further analysis.”²⁴¹ Neither unilateral nor coordinated effects should be a concern when the parties to a merger collectively control less than thirty percent of the relevant market.²⁴² Thus, plaintiffs should not be able to meet their initial burden of proof unless they can demonstrate that the parties to the merger had a collective market share in excess of thirty percent.²⁴³

If the plaintiff meets its burden of proving a merger above the thirty percent threshold, the burden should shift to the defendant to demonstrate that the merger will not have substantial anticompetitive effects. The relative burden imposed on a defendant should vary according to the market shares proven by a plaintiff. The presumption of illegality should be relatively weak when the collective market shares of the parties to a merger are less than fifty percent. In such a case, it should be easier for a defendant to rebut the presumption by demonstrating that the merger is unlikely to cause anticompetitive effects. A plaintiff can strengthen its case against mergers below the fifty percent market share level by proving that the merger raises the risk of coordinated anticompetitive effects.

A transaction may not give the merged entity enough market power to raise prices, to reduce output, or to engage in other anticompetitive conduct on its own, but it may reduce the number of firms in the market to a point at which the remaining players can exercise oligopoly power. “Firms are more likely to be able to coordinate their conduct to exercise such power when the products in the relevant market are homogeneous, transactions are frequent, pricing is standardized, information on the pricing and output strategies of rivals is easily accessible, or customers are insensitive to price changes.”²⁴⁴ When two or more of such factors are present, the elimination of a single player may make coordinated action more likely, even when the merged entity holds considerably less than 50 percent of the relevant market.

In the U.S. airline industry, for example, carriers can easily coordinate their pricing because fares change frequently and are publicly posted on computer reservation systems and Internet sites. Indeed, the airlines have been accused of using their

241. Merger Guidelines, *supra* note 69, ¶ 13,104, at 20,571.

242. For example, the DOJ and FTC 1996 *Statements of Antitrust Enforcement Policy in Health Care*, establish an “antitrust safety zone” for joint purchasing arrangements among health care providers where “the purchases account for less than 35 percent of the total sales of the purchased product or service in the relevant market.” 4 Trade Reg. Rep. (CCH) ¶ 13,153, at 20,812 (Sept. 5, 1996).

243. In *United States v. Philadelphia National Bank*, the Supreme Court concluded that a presumption of illegality should apply whenever a merged entity’s market share reaches thirty percent or more. 374 U.S. 321, 364 (1963) (“Without attempting to specify the smallest market share which would still be considered to threaten undue concentration, we are clear that 30% represents that threat.”). Subsequent Supreme Court cases reduced that threshold to twenty-five percent. See *United States v. Cont’l Can Co.*, 378 U.S. 441, 461–66 (1964) (finding that a merged company with twenty-five percent market share violated section 7); *United States v. Aluminum Co. of Am.*, 377 U.S. 271, 277–80 (1964) (holding that a merged company with twenty-nine percent of the market violated section 7).

244. Thomas A. Piraino, Jr., *A New Approach to the Antitrust Analysis of Mergers*, 83 B.U. L. REV. 785, 820 (2003) [hereinafter Piraino, Jr., *Mergers*].

computer reservations systems and Internet sites to signal pricing decisions to each other.²⁴⁵ Thus, the courts and agencies might preclude airline mergers in which the merged entity holds less than fifty percent of the market.

It should be difficult for parties to a merger to rebut the presumption of illegality when they collectively control more than fifty percent of the relevant market. Indeed, if the plaintiff proves a market share of seventy percent or more, the transaction should be considered a merger to monopoly, and the presumption of illegality should become irrebuttable. No mitigating factors should save such transactions from illegality. Although firms should be permitted—and indeed encouraged—to obtain monopoly power through internal growth generated by superior products and services,²⁴⁶ they should not be allowed to obtain monopolies by acquisition. Mergers to monopoly are not the result of consumer demand for a better product but simply the result of a potential monopolist's ability to pay the highest price to purchase its rivals. As one commentator has explained, “[A] merger to monopoly . . . should not be subject to an efficiencies justification because of the serious exploitative risk from such a high degree of market power.”²⁴⁷ The illegality of such mergers is consistent with the language of section 7 of the Clayton Act, which prohibits without exception any mergers that “tend to create a monopoly.”²⁴⁸ Thus, the courts should preclude, without any further inquiry, any mergers that would give the resulting entity a market share in excess of seventy percent of the relevant market.²⁴⁹

2. The Defendant's Rebuttal Case

a. Ease of Entry

Proving ease of entry should be a defendant's most effective means of rebutting a plaintiff's proof of market power because entry conditions have the potential to

245. See *United States v. Airline Tariff Publ'g Co.*, 1994-2 Trade Cas. (CCH) ¶ 70,687 (D.D.C. 1994) (authorizing consent agreement involving alleged price signaling among airlines in computerized fare publication venture); Marilyn Geewax, *Orbitz Ready for Launch*, CLEVELAND PLAIN DEALER, Apr. 28, 2001, at 1C (noting the concern of Thomas Underwood, an online travel industry analyst, that the Orbitz online ticketing joint venture among airlines “permits price signaling and allows instant competitive response”).

246. See *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 430 (2d Cir. 1945) (Hand, J.) (“The successful competitor, having been urged to compete, must not be turned upon when he wins.”).

247. Joseph F. Brodley, *Proof of Efficiencies in Mergers and Joint Ventures*, 64 ANTITRUST L.J. 575, 587 (1996). The courts generally have denied an efficiencies defense in cases of mergers to monopoly. See *FTC v. Tenet Healthcare Corp.*, 17 F. Supp. 2d 937 (E.D. Mo. 1998) (granting an injunction against a merger between the only two hospitals in the relevant market), *rev'd*, 186 F.3d 1045 (8th Cir. 1999); *FTC v. Staples, Inc.*, 970 F. Supp. 1066 (D.D.C. 1997) (granting an injunction against a merger among office supply companies that operated the only two “superstores” in several local markets).

248. 15 U.S.C. § 18 (2000 & Supp. II 2002).

249. Cf. Robert Pitofsky, *Efficiencies in Defense of Mergers: Two Years After*, 7 GEO. MASON L. REV. 485, 492 (1999) (“When two firms, as a result of merger, will account for as much as 80% of a properly defined relevant market[,] . . . efficiency claims . . . should not usually reverse a finding of illegality.”).

eliminate entirely the adverse competitive effects of a merger. In markets in which entry is relatively easy, neither coordinated nor unilateral anticompetitive effects are likely to occur, even if the parties hold a large collective market share. Neither the merged entity acting alone nor the remaining competitors acting collectively will be able to raise prices, to limit output, or to otherwise restrict competition for any meaningful period if other firms are likely to enter the market in response to such anticompetitive conduct.²⁵⁰

If a defendant meets its burden of proving that entry into the relevant market is easy, courts and agencies should approve the merger without further inquiry. As the Merger Guidelines point out, where ease of entry exists, “[T]he merger raises no antitrust concern and ordinarily requires no further analysis.”²⁵¹ For example, the capital costs of entering the dry cleaning business are not excessive. If two of the three dry cleaners in a community merged and thereafter attempted to raise prices, it is likely that one or more other firms would be induced to enter the market quickly, thus making the price increase unsuccessful. Such mergers do not have any ongoing adverse effect on consumers, and courts and agencies need not engage in an analysis of other mitigating factors in order to uphold them.

b. Proof of Lack of Unilateral or Coordinated Effects

A defendant may rebut a plaintiff’s prima facie case against a merger by demonstrating that the transaction does not increase the likelihood that competition will be reduced either by coordinated activity among the remaining firms in the market or by the merged entity acting on its own. Even when a merger occurs among firms in a concentrated oligopoly market, a defendant may be able to prove that, due to certain characteristics of the relevant market, the remaining firms will not be able to coordinate their conduct to restrict competition. Coordination among oligopolists is less likely when competing products have distinct characteristics and prices vary accordingly. Consider the market for turbine engines used in electric power plants. It would be difficult for the manufacturers of such engines to coordinate their pricing after a merger because each engine has unique specifications designed for a particular application, and prices vary widely.²⁵² Therefore, a merger of two turbine engine manufacturers should not unduly harm consumers, even in relatively concentrated markets.

250. As two antitrust commentators have explained, “The ultimate issue is whether entry is so easy that it ‘would likely avert [the] anti-competitive effects’ resulting from the proposed acquisition.” Richard G. Parker & David A. Balto, *The Merger Wave: Trends in Merger Enforcement and Litigation*, 55 BUS. LAW. 351, 361 (1999) (quoting *Staples*, 970 F. Supp. at 1086). The Merger Guidelines state that “A merger is not likely to create or enhance market power or to facilitate its exercise, if entry into the market is so easy that market participants, after the merger, either collectively or unilaterally could not profitably maintain a price increase above premerger levels.” Merger Guidelines, *supra* note 69, ¶ 13,104, at 20,573-9.

251. Merger Guidelines, *supra* note 69, ¶ 13,104, at 20,573-10.

252. See Richard A. Oppel, Jr. & Lowell Bergman, *Judge Says Supplier Inflated Gas Prices in California Crisis*, N.Y. TIMES, Sept. 24, 2002, at A1 (describing “gas-fired turbines” used in electric power plants).

A defendant could also make various arguments against the adverse unilateral effects of a horizontal merger. A defendant should have a particularly strong rebuttal argument on unilateral effects when the collective market share of the parties to a merger is less than fifty percent. Firms that control less than fifty percent of the output in the relevant market should not be able to act alone to raise prices, to reduce output, or to engage in other conduct harmful to consumers. If a firm with less than fifty percent of a market attempted to raise prices above the competitive level, other firms would likely hold prices at the competitive level—diverting business and making the price increase ultimately unsuccessful. As a firm's market share exceeds fifty percent, however, it becomes increasingly able to engage in unilateral anticompetitive conduct.²⁵³

In order to approve a merger that would confer market power above the fifty percent threshold, a court or agency would have to be convinced that certain unique market factors made the exercise of unilateral market power unlikely. For example, in certain markets, buyers may be powerful enough to prevent a merged entity from raising prices even if it has substantial market power. As one commentator has explained, “[T]he power of customers to push down price . . . can be just as important . . . as the number . . . of competitors in the market.”²⁵⁴ In certain cases, a reduction of firms from four to three, or even from three to two, may not harm consumers at all.²⁵⁵ In 1997, the FTC approved Boeing's merger with McDonnell Douglas, which gave Boeing more than fifty percent of the worldwide airplane manufacturing market and left only Airbus to compete with Boeing in the manufacture of commercial aircraft.²⁵⁶ Despite this duopoly, airlines have had sufficient bargaining power to win significant price concessions from the two companies.²⁵⁷ The Boeing/McDonnell Douglas merger

253. See Robert H. Lande & James Langenfeld, *From Surrogates to Stories: The Evolution of Federal Merger Policy*, ANTITRUST, Spring 1997, at 5, 8 (describing the approach of antitrust regulators to mergers resulting in thirty-five to fifty percent market share).

254. Michael E. Porter, *Competition and Antitrust: Toward a Productivity-Based Approach to Evaluating Mergers and Joint Ventures*, 46 ANTITRUST BULL. 919, 937 (2001). Some courts have found that buyers have sufficient leverage to counteract the anticompetitive effects of proposed mergers. See *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 60 (D.D.C. 1998) (finding that customers of drug wholesalers “possess a significant amount of leverage in contract negotiations”); *United States v. Archer-Daniels-Midland Co.*, 781 F. Supp. 1400, 1416 (S.D. Iowa 1991) (“The existence of large, powerful buyers . . . mitigates against the ability of sellers to raise prices.”); *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 986 (D.D.C. 1990) (“[T]he sophistication [of the defendant's customers] was likely to promote competition even in a highly concentrated market.”).

255. *But see* Thomas B. Leary, *An Inside Look at the Heinz Case*, ANTITRUST, Spring 2002, at 32, 32 (“[T]here is a broad consensus in the economic community that . . . 3–2 combinations are likely to be particularly troublesome.”).

256. See *In re Boeing Co.*, [1997–2001 FTC Complaints & Orders Transfer Binder] Trade Reg. Rep. (CCH), ¶ 24,295, at 24,123 (July 1, 1997); Amy J. Boatner, *Consolidation of the Aerospace and Defense Industries: The Effect of the Big Three Mergers in the United States Defense Industry*, 64 J. AIR L. & COM. 913, 920–22 (1999) (describing the effects of the merger between Boeing and McDonnell-Douglas).

257. J. Lynn Lunsford & Daniel Michaels, *KLM to Order Planes from Both Boeing, Airbus*, WALL ST. J., Mar. 29, 2002, at A2 (describing “an all-out [pricing] war” between the two companies to obtain new airplane orders).

has actually been advantageous for consumers. Airlines have benefited from their suppliers' economies of scale, which allow them to invest in improved airplane models, such as the new fuel-efficient aircraft under development at Boeing and the new wide-body plane being manufactured by Airbus.²⁵⁸

c. Proof of Efficiencies

The parties to a merger may also rebut a plaintiff's prima facie case by demonstrating that the potential efficiencies of the transaction outweigh its anticompetitive effects. There is currently no consensus among antitrust commentators and regulators as to whether efficiencies can ever justify mergers that substantially increase concentration levels in a particular market, and no federal court has yet been willing to concede that efficiencies can outweigh the anticompetitive effects of a merger.²⁵⁹

Efficiencies do, however, have their place in merger analysis. Efficiencies should not be as decisive in the analysis of mergers as ease of entry or factors bearing on the likelihood of coordinated or unilateral effects. If a defendant can prevail on such arguments, a court or an agency can be confident that a merger will not have adverse competitive effects. By contrast, efficiencies do not eliminate or mitigate a merger's anticompetitive effects; they simply provide a countervailing benefit that courts and agencies should balance against the transaction's adverse effects on consumers.

Antitrust regulators have struggled for years to determine how to balance the potential efficiencies of a merger against its potential anticompetitive effects.²⁶⁰ Courts and agencies can clarify the balancing test by ranking efficiencies in the order of their importance. The critical issue is whether a merger has the potential to leave consumers better off than they would have been if the parties had never combined. Efficiencies should be weighed in the balancing analysis according to their likelihood of being legitimate, realizable, beneficial to consumers, and unattainable other than through the proposed merger. Under these criteria, efficiencies should be recognized in the following order: (1) cost savings, (2) synergies resulting from the combination of

258. *Id.*; see also Edward Wong, *Boeing Drops Plans for High-Speed Airplane*, N.Y. TIMES, Dec. 21, 2002, at C2. Several courts and commentators, however, believe that an efficiencies defense is not appropriate for mergers that leave only two dominant firms in the relevant market. See, e.g., *FTC v. H.J. Heinz Co.*, 246 F.3d 708 (D.C. Cir. 2001) (holding that a merger that would reduce the number of baby food producers from three to two would be found illegal); *Cardinal Health*, 12 F. Supp. 2d 34 (holding that a merger that would reduce the number of national pharmaceutical wholesalers from four to two would likely be illegal); Yochi J. Dreazen, Greg Ip & Nicholas Kulish, *Why the Sudden Rise in the Urge to Merge and Form Oligopolies?*, WALL ST. J., Feb. 25, 2002, at A1 ("Twenty [competitors] to four is good . . . It's four to two that is much more dubious." (quoting Carl Shapiro, Professor, University of California-Berkeley)).

259. See *supra* note 80 and accompanying text. Robert Pitofsky has suggested that the efficiencies defense should not be permitted for mergers leading to a single firm market share of thirty-five percent or more. Robert Pitofsky, *Proposals for Revised United States Merger Enforcement in a Global Economy*, 81 GEO. L.J. 195, 218 (1992). "In the European Community the cutoff for an efficiencies-justified merger is a market share of 40-45 percent . . ." Brodley, *supra* note 247, at 588.

260. See *supra* notes 80-81 and accompanying text.

complementary assets, (3) economies of scale, and (4) the resolution of imbalances between supply and demand. The higher-ranked efficiencies (cost savings and synergies) should justify mergers effecting concentration levels of up to fifty percent, while the lower-ranked efficiencies (economies of scale and resolution of capacity imbalances) should only permit mergers in which the parties have a combined market share of up to forty percent.²⁶¹

D. Horizontal Joint Ventures

Courts and agencies should balance the potential efficiencies and anticompetitive effects of joint ventures in markets in which the joint venture partners are currently competing. The plaintiff should have the initial burden of proving that the collective market power of the parties to the joint venture exceeds a particular threshold. If the plaintiff meets its burden of proof, the parties to the venture should have the opportunity to rebut by proving the circumstances that mitigate a joint venture's adverse effect on competition.

1. Balancing Efficiencies and Anticompetitive Effects

Under the proposed approach, the courts and enforcement agencies would be able to determine the legality of a substantial number of joint ventures on their face. Indeed, all vertical joint ventures would be entitled to a presumption of legality because, in most cases, their only effect is beneficial.²⁶² Thus, the courts and enforcement agencies would only have to engage in the complex task of balancing economic efficiencies and adverse effects when joint ventures involve products in which the partners are currently engaged in competition.

A balancing test is appropriate for joint ventures designed to enhance their partners' efficiencies in markets in which they are already competing. Joint ventures in existing markets restrict competition as well as enhance efficiency. Such ventures reduce the number of competitors in the market because the partners will refrain, in the natural course, from competing with their own affiliate.²⁶³ The joint venture, in effect, will take the place of its partners within the scope of its operations. Whether or not the parties expressly agree not to compete with the joint venture, they usually will avoid competition that could harm their own affiliate.²⁶⁴ For such ventures, the courts must balance the "tradeoff between efficiency gains . . . and the potential anticompetitive losses."²⁶⁵

261. For a more detailed discussion of the relative role of such efficiencies in merger analysis, see generally Piraino, Jr., *Mergers*, *supra* note 244, at 822–31.

262. See *supra* notes 140–49 and accompanying text.

263. A joint venture "reduces the parents' incentive for competition because whatever a parent might earn by making individual sales in the joint market is now offset by its lowered profit as a partner in the joint venture." Joseph F. Brodley, *Analyzing Joint Ventures with Foreign Partners*, 53 ANTITRUST L.J. 73, 76 (1984).

264. See *id.*

265. Thomas L. Greaney & Jody L. Sindelar, *Physician-Sponsored Joint Ventures: An Antitrust Analysis of Preferred Provider Organizations*, 18 RUTGERS L.J. 513, 571 (1987). David Clanton has characterized the FTC's analysis of the General Motors-Toyota joint venture

A balancing approach is appropriate not only when a joint venture restricts existing competition among its partners but also when it limits potential competition. Firms may form joint ventures for the purpose of enhancing their efficiency in a new market, which one or more of the partners could have entered on their own. Such a venture forecloses the partners' individual entry into the relevant market. By virtue of the partners' participation in the joint venture, other competitors will no longer perceive them as potential entrants into the market. In making their decisions on pricing and output, the incumbent competitors will not feel constrained by the threat of individual entry by the joint venture partners.²⁶⁶ Thus, the courts should balance the efficiencies and anticompetitive effects of joint ventures that cover areas in which their partners currently compete or, but for the joint venture, would have competed.

2. The Plaintiff's Burden of Proof

The plaintiff should have the initial burden of proving the market power of the parties to joint ventures that restrict actual or potential competition. Substantial reductions in research and development, production output, or price competition will only occur when the joint venture partners collectively can exercise market power. Thus, as part of its prima facie case, the plaintiff should be required to prove that the partners to joint ventures in existing markets have a market share above a particular threshold. If a plaintiff fails to meet its burden, a court or an agency should allow the joint venture to proceed.

Because "[t]he potential for price-fixing and market domination grows as a company moves closer to the marketplace,"²⁶⁷ the market share threshold should be higher for "upstream" than for "downstream" joint ventures. Upstream joint ventures limited to research and development, industry-standards setting, joint buying, or other "inputs" into the production process usually do not affect the partners' decisions on pricing and output.²⁶⁸ Thus, a relatively high market share threshold of 40 percent would be appropriate for such ventures.²⁶⁹ Downstream production and marketing joint

as a balancing approach. See David A. Clanton, *Horizontal Agreements, the Rule of Reason, and the General Motors-Toyota Joint Venture*, 30 WAYNE L. REV. 1239 (1984). Such an approach was appropriate for this partially integrated joint venture that covered an area—the production of compact cars—in which the two companies already competed.

266. The Supreme Court recognized in *United States v. Penn-Olin Chem. Co.*, that such adverse consequences could result from a joint venture's elimination of potential competition. 378 U.S. 158, 173–74 (1964); see also *Yamaha Motor Co. v. FTC*, 657 F.2d 971 (8th Cir. 1981) (finding illegal a joint venture between a domestic outboard motor manufacturer and a foreign manufacturer that probably would have entered the U.S. market in the absence of the joint venture).

267. Joel B. Eisen, *Antitrust Reform for Production Joint Ventures*, 30 JURIMETRICS J. 253, 263 (1990).

268. See Walter T. Winslow, *Joint Ventures—Antitrust Problems and Opportunities*, 54 ANTITRUST L.J. 979, 983–84 (1985); Robert Pitofsky, *supra* note 146, at 1041–42 (1969).

269. This Article proposes a market share threshold of only 30 percent for a plaintiff's prima facie case against mergers. The higher market share threshold for joint ventures is justified by the fact that such transactions have less of an anticompetitive effect than mergers. See *supra* notes 142–50 and accompanying text.

ventures, however, have a greater potential for anticompetitive effects. A lower market share threshold of thirty percent should apply to such ventures.²⁷⁰

3. The Defendant's Rebuttal Case

Once a plaintiff makes a prima facie case of market power, a defendant should be allowed to rebut by showing circumstances that mitigate a joint venture's adverse effect on competition. Because joint ventures are less anticompetitive than mergers,²⁷¹ it should be easier for a defendant to meet its rebuttal burden in joint venture cases than in merger cases. Even if the parties have a large collective market share, the joint venture will not have a significant adverse effect if it is of limited scope and duration. In joint ventures limited to a short term, the parties will be acutely aware that their self-interest lies in maintaining their individual competitive capacities. If the venture covers only an upstream phase of the production cycle, the parties will retain their incentive to compete in the production and marketing phases. The "Big Three" automobile companies, for example, have entered into several research and development consortia for such products as an electric car, pollution control equipment, safety devices, and lightweight materials to replace steel in automobiles.²⁷² These consortia have not prevented Ford, General Motors, and Chrysler from competing just as fiercely against each other in the production and sale of automobiles.

A defendant can also rebut a plaintiff's prima facie case by proving that the efficiencies of a joint venture are likely to outweigh its anticompetitive effects. Traditionally, courts have given little weight to efficiency defenses in merger and joint venture analysis, believing that such arguments are easy to assert but difficult to confirm.²⁷³

Courts should have no trouble, however, distinguishing genuine from sham efficiency arguments in favor of a joint venture. First of all, the defendant, who will have access to the relevant documents and witnesses, will have the burden of proving a legitimate efficiency justification. Furthermore, efficiencies are easier to confirm in joint venture cases than in merger cases. The efficiencies likely to result from a particular joint venture often will be evident from the degree to which the venture

270. In the vertical restraints area, "[T]he courts appear to be converging on a definition of safe harbor for firms possessing less than a 20–25% market share in a relevant market." Thomas M. Jorde & David J. Teece, *Innovation, Cooperation and Antitrust*, 4 HIGH TECH. L.J. 1, 45 (1989).

271. See *supra* notes 142–43 and accompanying text.

272. See Oscar Suris, *Big Three Win Joint Patent, Marking a First*, WALL ST. J., Apr. 13, 1993, at B1; Christopher Jensen, *Big 3 Work Together on Research*, CLEVELAND PLAIN DEALER, Feb. 28, 1993, at 1E.

273. See Pitofsky, *supra* note 81, at 221–22; Joseph Kattan, *Efficiencies and Merger Analysis*, 62 ANTITRUST L.J. 513, 514 (1994) ("The problem of proof is the principal reason why, in an antitrust era that has been quite hospitable to efficiencies claims in a wide variety of other contexts, efficiencies have yet to play an outcome-determinative role in any litigated merger case."). The Merger Guidelines, which do not give efficiencies a high status in merger analysis, provide: "[E]fficiencies do not constitute a defense to an otherwise anticompetitive merger but are one of many factors that will be considered by the Department in determining whether to challenge a merger." Merger Guidelines, *supra* note 69, ¶ 13, 103, at 20,554.

integrates the parties' resources. Robert Pitofsky has pointed out that "the assumption that higher levels of integration are likely to be associated with more substantial efficiencies. . . . is a premise underlying all of antitrust."²⁷⁴

The amount of integration present in a joint venture is an objective standard from which the courts easily should be able to infer the most probable efficiencies of a joint venture. If the partners contribute substantial technology, assets, or capital and share the risks of a joint venture's success or failure, they are likely to create a new competitive entity with capacities beyond those of the individual partners. Research and development joint ventures, for example, are more likely to achieve technical advances when the partners are willing to share freely all of their relevant proprietary know-how with the venture. Production joint ventures are most efficient when the partners invest significant amounts of their own capital to improve the production process. Marketing joint ventures benefit consumers if the partners combine their sales networks to enhance point-of-sale services.

Conversely, when partners contribute little to joint ventures, they are more likely acting for their own competitive benefit rather than to enhance general economic efficiency. An agreement by purchasers to pool their bargaining power or a joint marketing agreement among competing sellers, unaccompanied by any other efforts at integration, may very well enhance the profitability of individual partners. These arrangements, however, are not likely to create substantial overall efficiencies in the relevant market.

Substantially integrated joint ventures of limited scope and duration should easily pass muster under the balancing test. Such arrangements generate significant efficiencies and have minimal anticompetitive effects, even when the parties have large market shares. The FTC's analysis of a 1984 joint venture between Toyota and General Motors is instructive. The joint venture involved the production of a compact car at a plant in Fremont, California.²⁷⁵ The FTC recognized that such a downstream venture between what were then the first- and third-largest automobile manufacturers in the world could have an adverse effect on competition.²⁷⁶ However, the FTC also pointed out that such effects would be limited because the venture only covered the production of a single automobile and the parties were free to continue to compete in the marketing phase.²⁷⁷ Furthermore, any adverse competitive effects would be outweighed by the efficiencies that could result from the parties' integration of their production capacity.²⁷⁸ The FTC emphasized in particular that General Motors would have the opportunity to learn more efficient Japanese manufacturing techniques.²⁷⁹

274. Pitofsky, *supra* note 140, at 1623.

275. *In re General Motors Corp.*, 103 F.T.C. 374 (1984).

276. *Id.* at 386-88.

277. *See id.* at 386.

278. *Id.* at 387-88.

279. *Id.* This assumption has been borne out by later events, for General Motors has assigned alumni of the joint venture to oversee changes in manufacturing techniques at many of its plants. See Paul Ingrassia & Joseph B. White, *Major Overhaul: Determined to Change, General Motors is Said to Pick New Chairman*, WALL ST. J., Oct. 23, 1992, at A1.

CONCLUSION

Both the Harvard School and the Chicago School have made valuable contributions to antitrust analysis. Unfortunately, the ideological battle between the two theories has polarized antitrust thinking not only within the academic community but also among the federal courts and enforcement agencies. The Chicago School approach was adopted by the courts and agencies to redress the harsh approach of the Harvard School, which often invalidated conduct that had the potential to enhance firms' efficiency and thereby benefit consumers. However, the Chicago School had its own excesses. By mandating a complicated empirical analysis of the economic efforts of most competitive conduct, the Chicago School approach made the outcome of antitrust cases more difficult to predict. As a result, antitrust enforcement lost much of its deterrent effect. Antitrust practitioners were no longer able to advise their clients with certainty of conduct that would be permitted or precluded.

The Supreme Court's 1999 decision in *California Dental* holds the promise for healing the divide between the Harvard School and the Chicago School. By adopting the continuum-based approach proposed in that case, the courts and agencies can retain both the clarity of the Harvard School and the economic sophistication of the Chicago School.

This Article has proposed a means of arraying all competitive conduct on a continuum according to its likely effect on consumers. Under the proposed approach, the courts and agencies will be able to confirm the consumer welfare effect of most types of conduct in an abbreviated fashion without considering complex economic issues. The courts and agencies will only have to engage in a more detailed market analysis in those rare cases in which the effect of conduct on consumers is not readily apparent. Even in such cases, the approach proposed in this Article will allow the courts and agencies to limit their inquiry to a few decisive factors.

Under the proposed approach, judges and juries will have objective guidelines for making decisions and will not have to engage in economic inquiries that are beyond their competence. As a result, the outcome of antitrust cases will again become easier to predict. Business executives will be able to plan their conduct accordingly, and the antitrust laws will regain their deterrent effect. This approach will clarify the standards of competition for American business, insuring that firms avoid conduct harmful to consumers and pursue conduct with the potential to promote consumer welfare.

