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ANTITRUST LAW—PRICE FIXING—RULE OF REASON IN HEALTH CARE—Arizona v. Maricopa County Medical Society, [1980-1] Trade Cases (CCH) ¶ 63,239 (9th Cir. March 20, 1980)

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NOTES

ANTITRUST LAW—PRICE FIXING—RULE OF REASON IN HEALTH CARE—*Arizona v. Maricopa County Medical Society*, [1980-1] Trade Cases (CCH) ¶ 63,239 (9th Cir. March 20, 1980).

I. INTRODUCTION

> Consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to only so far as it may be necessary for promoting that of the consumer.[1]

Health care is often unavailable in the United States.[2] When available, it is increasingly expensive.[3] Many people are underinsured or simply uninsured.[4] Furthermore, the existence of insurance tends to increase fees[5] and induce unnecessary surgery.[6]

In response to this health care crisis the State of Arizona brought an action under the Sherman Act[7] alleging illegal price fixing against two foundations for medical care (FMC's) and the county medical society associated with each.[8] The FMC's are non-

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1. Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* in 39 GREAT BOOKS OF THE WESTERN WORLD 287 (R. H. Hutchins ed. 1962).

2. In 1972 more than 800 towns in the four states of Minnesota, Montana, and North and South Dakota were without any doctor. Fifty years earlier four out of five of these towns had had at least one general practitioner. S. KLAW, THE GREAT AMERICAN MEDICINE SHOW: THE UNHEALTHY STATE OF U.S. MEDICAL CARE, AND WHAT CAN BE DONE ABOUT IT 46 (1975).

3. J. BRAVERMAN, CRISIS IN HEALTH CARE 8-15 (1978). In the six months following former President Nixon's lifting of wage and price controls in the spring of 1974, doctors' fees rose by 8%, the equivalent of a 16% annual rate and 25% greater than the rise in the overall cost of living in that period. S. KLAW, *supra* note 2, at 16.

4. As of December 31, 1975, 37.3% of all Americans over the age of 65 were uninsured for the costs of hospital care; 78.2% were uninsured for the costs of out-of-hospital medication; and 80.4% were uninsured for nursing home care. J. BRAVERMAN, *supra* note 3, at 212.

5. Kallstrom, *Health Care Costs Control by Third-Party Payors: Fee schedules and the Sherman Act*, 1978 DUKE L.J. 645, 647.

6. S. KLAW, *supra* note 2, at 6-8. We pay a price for these unnecessary operations which can not be stated in monetary terms. One surgeon has estimated that at least 500 women die each year as a result of complications arising out of unnecessary hysterectomies. More generally, unnecessary surgery of all types may take 10,000 lives in the United States each year. *Id.* at 9.

7. 15 U.S.C. §§ 1-2 (1976).

8. Arizona v. Maricopa County Medical Soc'y, [1980-1] TRADE CASES (CCH), ¶ 63,239 at 78,153 (9th Cir. 1980).

profit organizations that poll their members from time to time to set upper limits on fees the membership may charge patients covered on approved insurance plans. They also evaluate the medical necessity and appropriateness of treatments and the use of hospital services.[9] When an increase in the fee ceiling is approved, insurance companies are notified in advance so that they can increase premiums to cover their higher costs.[10] The participating physicians draw funds directly from insurers' bank accounts to pay their bills.[11] The state, in *Arizona v. Maricopa County Medical Society*,[12] argued that this system was responsible for raising the fees of foundation members above fees otherwise charged by Arizona doctors.[13] The state brought an injunctive suit to halt the price-fixing activity.[14]

Arizona moved for summary judgment on the issue of the FMC's liability. The United States District Court for the District of Arizona denied this motion but certified for appeal[15] the question of whether the FMC membership agreement, which contained a promise to abide by the majority-set prices, was per se illegal under section 1 of the Sherman Act. The United States Court of Appeals for the Ninth Circuit, in a split decision, affirmed the denial of summary judgment and remanded with instructions to apply a rule of reason analysis, which involves an evaluation of the agreement's impact upon competition within the particular relevant circumstances in which it arose.[16]

The court employed three major arguments in denying the state's assertion of per se illegality. First, it cited *Broadcast Music, Inc. v. Columbia Broadcasting Co.*[17] for the proposition that not

9. *Id.*
10. *Id.* at 78,164 (Larson, J., dissenting).
11. *Id.* at 78,153.
12. *Id.*
13. *Id.*
14. *Id.*
15. 28 U.S.C. § 1292(b) (1976) provides for certification for appeal from an order when the district judge is "of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion. . . ."
16. [1980-1] TRADE CASES (CCH) at 78,157.
17. 441 U.S. 1 (1979). This case involved a challenge by the Columbia Broadcasting System [hereinafter referred to as CBS] to the legality of blanket licenses. A blanket license allows the licensee to perform any of the several musical compositions in a repertory. Broadcast Music, Inc. [hereinafter referred to as BMI] is an organization of copyright owners who sold their product, the right to use their music, in this fashion. The price of a basket of compositions was sometimes a flat dollar amount and, at other times, a percentage of the revenue gained from their use. The

every joint action among horizontal competitors[18] that has an effect upon prices is to be treated as per se illegal price fixing.[19] The *Maricopa County* court held that per se illegality could not be extended to an industry with which the judiciary has had very little experience.[20]

The court also reasoned that the application of the per se rule would be inappropriate in light of its own doubts as to the cogency of limit price theory. Limit price theory asserts that established firms may maximize long-range profits at price levels less than the short-run monopoly price by seeking a level that will best inhibit entry by competitors and thus in the long run will preserve prices greater than those that a competitive environment would allow. The state had contended that FMC's are in a position to limit prices to protect themselves from potential competition.[21] The court, however, noted that some commentators have suggested that limit pricing is economically irrational behavior.[22] The court concluded that a body of thought as controversial as limit price theory cannot serve as a justification for the imposition of liability on a motion for summary judgment.[23] Finally, the court suggested that the medical profession is not subject to the same antitrust rules as other sectors of the economy due to its noncommercial character.[24]

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lower courts held this an illegal exercise of price fixing. The Supreme Court reversed and remanded for a rule of reason analysis. *Id.*

18. A "horizontal" relationship is one between firms performing "similar functions" in the manufacture or distribution of a good or service. Brown Shoe Co. v. United States, 370 U.S. 294, 334 (1962).

19. [1980-1] TRADE CASES (CCH) at 78,156.

20. "[W]e are uncertain about the competitive order that should exist within the health care industry pursuant to the Sherman Act as interpreted by the courts. Only recently have the professions been brought by the Supreme Court within the reach of the Act." *Id.* at 78,154. "I agree with my brother Sneed that we know too little about the effects on competition produced by the practices here in question to brand them per se violations of the Sherman Act at this point." *Id.* at 78,157 (Kennedy, J., concurring). *Contra*, "It is not our task to determine what the competitive order should be. The Sherman Act requires that absent very unusual circumstances market forces should be given free rein." *Id.* at 78,162 (Larson, J., dissenting).

21. *Id.* at 78,156 (citing Havighurst, *Health Maintenance Organizations and the Market for Services*, 35 LAW & CONTEMP. PROB. 716, 767-76 (1971)).

22. *Id.* at 78,156 (citing R. POSNER, ANTITRUST LAW: AN ECONOMIC PERSPECTIVE 115 n.50 (1976)); *see* Markovits, *Potential Competition, Limit Price Theory, and the Legality of Horizontal and Conglomerate Mergers Under the American Antitrust Laws*, 1975 WIS. L. REV. 658.

23. [1980-1] TRADE CASES (CCH) at 78,156.

24. *Id.* at 78,157.

Judge Larson, dissenting in *Maricopa County*, would have reversed the denial of summary judgment and granted preliminary relief for plaintiff.[25] His interpretation of *Broadcast Music* would not allow the exemption of entire industries or professions from the per se rule against price fixing.[26] He asserted that the whole purpose and effect of the FMC-set maximum prices was to remove desired cost-cutting incentives from doctors and insurers alike.[27] Furthermore, even if the net effect of the arrangement were a reduction of health care costs, the law looks with the same disfavor upon both downward and upward price fixing.[28] Finally, he reasoned

25. *Id.* at 78,158-65 (Larson, J., dissenting). Judge Larson's dissent opens with some discussion of a procedural issue. The state was appealing from both the denial of summary judgment and the vacation of a temporary restraining order which had earlier been issued prohibiting further adherence to the fee schedules. The defendants denied that the circuit court had the jurisdiction to hear an appeal on the vacation of the restraining order at that point. *Id.* at 78,153. The dissent asserted that the temporary restraining order had been in effect long enough to have become in fact, although not in label, a preliminary injunction. Preliminary injunctions can be the subject of an interlocutory appeal, pursuant to 28 U.S.C. § 1292(a)(1) (1976). *Id.* at 78,158-59.

The dissent's discussion of the substantive questions is divided into three parts: The first addressing the question of whether the practice involved here had traditionally been categorized as per se illegal; the second rejecting any claim that this case fell within an exemption from traditional antitrust rules; and the third arguing that the practice was so plainly anticompetitive that, even if a rule of reason analysis were necessary, it would operate to bar the practice on the instant record. That third point was important, given the defendant's challenge to the jurisdiction of the circuit court, because it contributed to the conclusion that the district court plainly had been in error in refusing relief, strengthening the argument in favor of the propriety of interlocutory appeal.

26. In a footnote, Judge Larson stated that the *Broadcast Music* Court's major concern was the danger of a hasty categorization of conduct as price-fixing. The Foundation for Medical Care [hereinafter referred to as FMC], however, was very clearly fixing prices between horizontal competitors in the instant case. What was different here was not the challenged practice itself, but the industry in which it occurred. *Broadcast Music* did not sanction an abandonment of the per se rules on the basis of the nature of the particular industry in which they were to be applied. *Id.* at 78,163 n.11.

27. "The entire system is designed to avoid providing any one with an incentive to control costs." *Id.* at 78,164. The dissent also objected that the "cozy" character of the system for insurers and doctors was locking them into the existing pattern, so that they would be unwilling to experiment with other forms of health care. Because of the resultant dearth of experimentation, physicians' incomes were being insulated from competitive pressures. *Id.* This is not the same argument as the limit pricing theory to be examined later, *see* text accompanying notes 100-19 *infra*, but it is a speculation as to a nonprice mechanism by which established firms may limit the possibility of new entry.

28. [1980-1] TRADE CASES (CCH) at 78,164 (citing National Soc'y of Professional Eng'rs v. United States, 435 U.S. 679, 689 (1978) and United States v. Trenton Potteries, Inc., 273 U.S. 392, 397 (1927)).

that, although the medical profession may have some degree of antitrust exemption for collective, noncommercial activities, price setting is entirely commercial.[29]

This note will analyze the effect that a general acceptance of *Maricopa County's* rule of reason would have upon the policing of price competition in the health care field. It will be contended that substantial barriers deter potential competition in that field. This structural fact makes it possible for the established firms, if allowed to set prices in tandem, to price at an entry-limiting level above the competitive level. That possibility poses a threat to consumer welfare that can be reduced through an adherence to the per se illegality rule against price fixing.

II. ECONOMIC BACKGROUND

Under conditions of perfect competition[30] each producer will operate at its own marginal cost.[31] Allowing the free exit and entry of suppliers in a particular market will insure that the producers as a whole will supply any desired quantity at its lowest cost.[32] This condition is optimal since consumers are paying the minimum necessary for that amount of a good or service they are willing to buy.

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29. *Id.* at 78,161.

30. Perfect competition, as defined by economists, exists only if no producer is a large enough part of the market to unilaterally affect the market price of a produced good. Furthermore, every producer must know the methods of every other producer. P. SAMUELSON, ECONOMICS 43-48 (10th ed. 1976). Perfect competition is an idealized working hypothesis, comparable to a physicist's assumption of a frictionless surface. *Id.* at 69.

31. Marginal cost at any output is the extra cost of producing one more unit. The law of diminishing returns asserts that, beyond an initial phase utilizing economies of scale, the marginal cost will rise because more units of input will be necessary to obtain a constant increment to output. Since a perfect competitor is by definition a firm which cannot unilaterally influence price, it will continue increasing production without having to worry about causing a market glut. These production increases will cause the marginal cost to increase, until at some point the cost of the last unit of output is equal to the extra revenue obtained from selling it; that is, the price of that unit. This equality is expressed as the output level where price equals marginal cost (P=MC). The supply curve and the marginal cost curve for a perfect competitor are identical; each represents the quantity producers are willing to supply at the various possible prices. *Id.* at 452-57.

32. Under conditions of free exit and entry, firms will sell at their minimum long-run competitive costs. If the market price drops below this cost level, firms will leave the industry, reducing total supply and pushing the price up. If the market price is above the minimum long-range cost, new firms will be attracted into the market and the price will be pushed down. The economist's use of the word "cost" includes a reasonable rate of return on investment—that minimum rate necessary to insure further investment. *Id.* at 472.

Economists have given up on the possibility of realizing this model of perfect competition.[33] They have substituted the notion of workable competition, which exists whenever an industry provides a combination of prices and outputs reasonably compatible with consumer welfare and technological progress.[34] The rule of reason test for medical association price fixing, enunciated in *Maricopa County*, will be justified only if it can aid in bringing about or preserving workable competition.

The price of any commodity or service is determined by the equilibrium of supply and demand:[35] any increase in price can be explained by either a supply shortage or an increase in demand. If the explanation of the contemporary health care crisis is to be found in a sudden increase in the demand for care, a focus on supply would be misplaced. In the field of medical services, however, a demand explanation would not be plausible. The reduction in the demand for physician hours in the treatment of polio as a result of the Salk vaccine is an example of the way in which advances in medical technology tend to reduce demand.[36] There is room for dispute as to whether the spread of health insurance coverage has brought about an increase in the demand for care.[37] Whatever the merits of that dispute, it seems clear that the dominant factor determining the demand for health care is epidemiology, that is, the natural incidence of disease, a force beyond our control.[38] Consequently, a solution to the problems of health care must be sought on the side of supply.

In a noncompetitive industry prices rise above marginal cost.[39]

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33. *Id.* at 531.

34. The concept of workable competition was first discussed by Clark, *Toward a Concept of Workable Competition*, 30 AM. ECON. REV. 241 (1940).

35. P. SAMUELSON, *supra* note 30, at 63-65.

36. *See, e.g.*, V. FUCHS, WHO SHALL LIVE? HEALTH, ECONOMICS AND SOCIAL CHOICE 92-95 (1975).

37. H. KLARMAN, ECONOMICS OF HEALTH 33-35 (1965).

38. There are serious limits to the ability of the young science of health economics to quantify relationships between demand for care and price. There is no dispute that an increase in the price of health care will cause demand to fall. For example, as prices increase people will decide to forego their annual check-ups, or to stop going to dermatologists about dandruff. This inverse relation between demand and price is called "elasticity." Unfortunately, very little is known about the degree of elasticity. V. FUCHS, *supra* note 36, at 147-48. A further discussion of that problem is probably not essential to an understanding of *Maricopa County*.

39. A noncompetitive industry is one in which the product of a particular supplier composes a substantial part of the market. Therefore, the quantity which a producer in such a situation provides helps to sate the total demand or, put more technically, drives price down along the demand curve. Only through a philanthropic act

Therefore, public policy is directed toward the preservation of competition. There are two separate concepts of competition. In the narrower sense there is what can be termed actual competition:[40] The struggle between rivals for the same trade at the same time.[41] But prices also are held in check by potential competition: The ease of entry for future rivals into the market.[42] Antitrust prosecutions for price fixing police the actual competition among existing rivals. This enforcement activity increases in importance as the threat of potential competition recedes, that is, as the barriers to entry increase.[43] The effects of price fixing therefore are most pernicious in markets where the probability of new entry is low, for example, where rivalry is discouraged.

Certain barriers to entry into health care arise as a result of the uncertainties involved in predicting the incidence of disease and the efficacy of treatment.[44] State laws impose licensing re-

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would a supplier in such a situation set price at marginal cost. Consumers would be willing to pay more than marginal cost at the profit maximizing level of output. P. SAMUELSON, *supra* note 30, at 512-17.

40. The term "actual competition" is used here to describe what the cases refer to as "competition" when they are using that term in a sense excluding "potential competition." *See, e.g.*, Anthony Augliera, Inc. v. Loughlin, 149 Conn. 478, 485, 181 A.2d 596, 600 (1962); Merchants' Nat'l Bank of Glendive v. Dawson County, 93 Mont. 310, 321, 19 P.2d 892, 896 (1933). The term is coined for precision, to connote that actual competition is only one element of competition in the wider sense.

41. *E.g.*, Anthony Augliera, Inc. v. Loughlin, 149 Conn. 478, 485, 181 A.2d 596, 600 (1962); Merchants' Nat'l Bank of Glendive v. Dawson County, 93 Mont. 310, 321, 19 P.2d 892, 896 (1933).

42. FTC v. Raladam Co., 283 U.S. 643, 649 (1930); Allen B. Wrisley Co. v. FTC, 113 F.2d 437, 441 (7th Cir. 1940).

43. "It may be, as suggested . . . that local monopolies cannot endure long, because their very existence tempts outside capital into competition; but the public policy embodied in the common law requires the discouragement of monopolies, however temporary their existence may be." Addyston Pipe & Steel Co. v. United States, 85 F. 271, 284 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899) (citations omitted). By reasoning in this manner, Sixth Circuit Judge Taft permits or encourages the inference that the public policy against local monopolies becomes stronger as the likelihood of their duration increases. That duration depends upon the various factors which bar outside capital from entering into the local market.

This note's discussion of entry barriers is qualitative, rather than quantitative. The need for a long-run quantitative measure of the power to exclude is, however, addressed in Grossack, *The Concept and Measurement of Permanent Industrial Concentration*, 80 J. POL. ECON. 745 (1972).

44. Arrow, *Uncertainty and the Welfare Economics of Medical Care*, 53 AM. ECON. REV. 940, 941 (1963).

Senator Edward M. Kennedy has asserted that market competition in the health care field is both irrelevant and inappropriate. He describes the "economic injunction" of a free marketplace as "more is better." That injunction does not apply, he quirements upon persons wishing to enter one of the health-related professions. The licensing tests generally require an extended period of medical education, which requirement creates a delay between a change in market demand and the readjustment of the supply of healers. The threat of malpractice litigation and the high insurance premiums created by that threat may be deterring the expansion of existing health care facilities. Finally, the drug industry has an interest in preserving these barriers to entry so that it can deal with a limited number of drug-dispensing middlemen. Some of these structural features of the health care market are justified in part by the public desire, arising out of the uncertainties involved in the incidence and treatment of disease, to be assured of its healers' competence.[45] Unfortunately, they go further in their anticompetitive effect than is necessary for the public peace of mind.[46] A review of the nature and importance of the chief barriers to new competitors will illustrate their effect.

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reasons, to health care. Too many surgeons in one area produce unnecessary surgery and unduly high fees. J. BRAVERMAN, *supra* note 3, at 28.

The logic of this viewpoint is less than compelling. It is tautologically true that too many doctors are too many, and therefore more than enough. But in the absence of a competitive market system, there is no nonarbitrary standard to determine how many are enough. A market system does not imply that more is better. It only implies that what the consumer wants is better than what the consumer does not want. There is no reason why the wants of the consumer are less normative in health care than elsewhere.

45. Arrow, *supra* note 44, at 966.

46. For example, after the reform of such laws one might see immunization centers staffed entirely by registered nurses or other nonphysican health professionals. *Id.* at 956.

More generally, a periodic recertification system has been proposed. Several grades of skill could be established. A person wishing to obtain a certificate to practice medicine would submit to examination every five years, or at some other agreed-upon interval. The certificant would be rated along a publicized set of grades of skill. The certificate, with the rating on it, would have to be shown to all prospective patients. Patients could choose to buy health care from a practitioner at any of the skill levels or even, if they wished, from a "doctor" whom they knew not to have any certificate at all. In this freed-up market, the lower-skilled levels of health care professional would remain competitive by offering lower fees than the others. A consumer would make an informed trade-off between cost and quality. The advocates claim that the effects of such wide-open competition would most probably be a lowering of the cost of even the highest-certified doctors below most doctors' fees today.

Another plan, which some might consider less drastic, is called institutional licensure. Institutions, such as hospitals, health maintenance organizations, and professional associations, would require a license in order to operate. But there would be no further restrictions on the personnel a certified institution could hire, or which functions it could assign to which employees. This increased flexibility might have the same economic effect as the periodic certification plan. V. FUCHS, *supra* note 36, at 60-61.

A. *Licenses and Education*

Some states license as many as two dozen separate health occupations.[47] The effectiveness of licensing as a form of quality control is highly questionable given the extreme rarity of revocation or suspension of a practitioner's license.[48] Less restrictive alternatives to the present licensing system have been proposed that would allow greater leeway to competitive forces while providing an assurance of quality.[49]

A decade or more, depending on the degree of specialization, will elapse from the time of a student's decision to take a premedical curriculum to the time of emergence as a full practitioner.[50] Only a student who has completed two years at an American Medical Association (AMA) approved school can take the first part of the licensing exam, which deals with basic science.[51] This requirement is an unnecessary restriction upon the supply of physicians.[52] If one has acquired the knowledge to be able to pass such an examination at all, the source from which it has been acquired cannot reflect upon one's competence.[53] Therefore, the first half of the exam ought to be open to all who care to take it. Such an open examination system would not diminish the quality of the typical doctor. It would have a positive effect upon quality since it would

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47. V. FUCHS *supra* note 36, at 76.

48. *Id.*

49. *See* note 46 *supra* and accompanying text.

50. For a discussion of the economic effects of specialization, particularly of the postponement of earnings that prolonged training involves, *see* H. KLARMAN, *supra* note 37, at 82-83. It is also to be noted here that the term "health care supplier" is treated as synonymous with "physician." This usage is obviously a simplification, although helpful for our purposes. In 1901, two out of every three persons in the health care field were physicians. By 1975 the ratio was one out of twelve. V. FUCHS, *supra* note 36, at 56. But the physician clearly remains the central figure in the production of medical care. *Id.* at 56-57.

51. Kessel, *Higher Education and the Nation's Health: A Review of the Carnegie Commission Report on Medical Education*, 15 J. LAW & ECON. 115, 121 (1972).

52. Another factor distorting the operation of market forces in medical education is public subsidization. The high subsidies *encourage* entry by allowing for artificially low tuitions. Any positive effect upon competition this might have is, however, more than eliminated by the highly selective admissions process and the elimination of students during the course of studies. Arrow, *supra* note 44, at 952.

It has also been suggested that there are equitable reasons to be concerned about this public subsidization. Admission to medical school is generally a ticket to the upper 10% in the income distribution of the United States. If this ticket is being bought out of general tax-obtained revenues, it has some of the features of a regressive tax. Kessel, *supra* note 51, at 118-19.

53. *Id.* at 122.

force medical schools to compete with liberal arts colleges, university science departments, and scientific institutes in developing curriculum to provide the biological knowledge for which one will be tested.[54] Passing this exam, under an open system, would be an admission to the second two years, the more clinically oriented half, of medical school.[55]

These interlocking restrictions on licensing and education date from the 1910 publication of the Flexner report.[56] That report critiqued medical education and advised that medical schools be certified by the AMA in order to assure their quality.[57] This quality assurance, naturally, has amounted to a control over quantity as well and thus indirectly to a control over the annual number of graduates from medical school.[58] Medical science since 1910 has undergone a series of triumphs; but medical economics since that year, when educational barriers to entry into the health care field were significantly raised, has been a disaster.[59]

B. *Relationship Between Medical Profession and Drug Industry*

Other than education, the major supply market for the medical field is the drug industry. There are close ties between the drug industry and the medical profession.[60] These ties may strengthen the incentives of the medical profession to limit new entrants.[61] The AMA owns $28 million in drug company stock, and more than a quarter of the AMA's income comes from drug company advertisements placed in AMA publications.[62] This financial

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54. *Id.* at 121, 126.

55. *Id.* at 122.

56. A. FLEXNER, MEDICAL EDUC. IN THE U.S. & CANADA, A REPORT TO THE CARNEGIE FOUNDATION FOR THE ADVANCEMENT OF LEARNING (4 Carnegie Foundation Bulletin 1910).

57. Kessel, *supra* note 51, at 121.

58. S. KLAW, *supra* note 2, at 20.

59. *Id.* at 21. In 1937 an alumnus of Harvard Medical School warned students at that institution that "I should recommend [medicine] only for the man who has plenty of money back of him. Many men never make much in medicine." L. THOMAS, THE MEDUSA AND THE SNAIL: MORE NOTES OF A BIOLOGY WATCHER 144 (1979).

60. These ties between the dominant firms in a supplier industry and those they supply are manifestations of "imperfections in supply markets" as discussed in J. BAIN, BARRIERS TO NEW COMPETITION 15-20 (1956).

61. The Supreme Court took account of the possibility of anticompetitive effects arising out of ties between supplier firms and their supplied industries in United States v. duPont & Co., 353 U.S. 586 (1956).

62. S. KLAW, *supra* note 2, at 124. Some of these drug advertisements raise serious issues in themselves. For example, medical journals have run ads which ad-

interface perhaps helps to explain why the AMA Journal continued carrying advertisements for certain drugs long after the clear consensus of scientific authority was that these drugs were ineffective and unsafe.[63] Likewise, if an increase in the number of practicing physicians is not in the interest of the drug companies, the increase will be looked upon with some heightened degree of suspicion by the AMA. For reasons which shortly will become clear, the established firms in the drug industry would not look kindly upon a large increase in the number of practicing physicians.

The advertising tactics of the drug companies are geared to appeal to a limited number of doctors and are conducted in intensive campaigns. The salespersons, known as detail men, discuss the advantages of one firm's products face-to-face with as many doctors as they can meet.[64] What is not done in person is done through large, direct mailing campaigns.[65] Large advertising costs are a recognized part of product differentiation strategies: the seller in such a campaign incurs large costs in order to create significant buyer preferences for the established products. These preferences help the established firms to set prices above their marginal costs without attracting entry.[66] Buyer preferences created by the large advertising expenses of the established firms are a barrier to the entry of new firms.[67] The drug companies are acting rationally in courting the loyalty of the doctors because if those doctors, the essential retailers of pharmaceuticals, are loyal to name brands, they will not provide a toehold for the entry of new competitors.

Clearly, any enlargement in the set of medical doctors will make such tactics correspondingly less feasible. It intuitively might seem irrational for drug companies to want to limit the number of doctors for it would seem that more doctors would lead to the sale

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vised doctors to prescribe tranquilizers and antidepressants for patients, who are suffering from nothing more than the normal strains of a full life: For a woman "depressed" over the marriage of her youngest child; for the loneliness of a newcomer in town; or for the excessive use of the telephone. *Id.* at 120-21.

63. V. FUCHS *supra* note 36, at 111-12.

64. S. KLAW, *supra* note 2, at 122-25.

65. For example, a Tennessee physician, who kept records of his mail, received 44 drug samples, 125 direct mail advertisements, and 41 drug company published periodicals in one month. *Id.* at 117.

66. In the absence of product differentiation or other entry barriers, an increase in price above the competitive level will improve the profit expectations of a potential entrant. Resources will be moved into this profitable field from elsewhere. *See* notes 30-34 *supra* and accompanying text.

67. J. BAIN, *supra* note 60, at 115-17.

of more drugs. But there is no reason to expect that the presently established firms would make the extra sales. In understanding the barriers to entry to the medical profession, particularly the support of licensing and educational requirements by the AMA, it is important to remember that the AMA has a financial interest in the success of drug companies and that those companies conduct business in ways that rely upon a continuing limit upon the supply of physicians.[68]

C. *Malpractice Litigation and Premiums*

The threat of malpractice litigation and the high insurance premiums created by that threat may serve as another barrier to entry into health care. In the middle of the 1970's, malpractice claims were being filed at a rate of over 18,000 per year.[69] The frequency of malpractice claims made against those physicians insured by one major midwestern underwriter increased by 139% between 1969 and 1974.[70] The increase in claims, combined with the great unpredictability in this area of the law, led to a dramatic increase in the size of the premiums required by some insurers and to the abandonment of the field by others.[71]

The entry barrier effect of malpractice insurance perhaps operates more noticeably upon institutions than upon individuals. It would be difficult to tell how many persons, if any, have abandoned or decided against a medical career because of the malpractice problem: but a Cornwall, New York, hospital paid ten percent of its operations budget for insurance coverage in 1975.[72] The like-

68. In 1973, there were 15 drug companies in the FORTUNE 500. These 15 companies earned, after taxes, more profit as a percentage of stockholder equity than any other industry group on that select list. This was one-half higher than the average rate of return for the FORTUNE firms listed that year. This would seem on its face to be evidence that the drug industry is itself less than perfectly competitive. S. KLAW, *supra* note 2, at 29.

69. *Id.* at 95.

70. Abraham, *Medical Malpractice Reform: A Preliminary Analysis*, 36 MD. L. REV. 489, 490 n.3 (1977). The problem of malpractice insurance premiums became so severe that between 1975 and 1977 almost every state legislature enacted one or more measures intended to ease those costs. *Id.* at 489. The Abraham article was an attempt to evaluate the effectiveness of those measures.

71. In 1975, the principal malpractice insurer in Ohio asked the state insurance board for permission to raise its rates by 747%. S. KLAW, *supra* note 2, at 106.

72. J. BRAVERMAN, *supra* note 3, at 156. It seems logical to infer that the effect of malpractice insurance rates upon the expansion of institutions also slows the entry of individuals into a geographic market. If high premiums prevent a hospital from expanding to meet public demand, that hospital will not hire the extra personnel who otherwise would have been essential to that expansion.

lihood is that a hospital with such insurance costs will be deterred from expanding its facilities even when local health needs otherwise would call for such an expansion. Aside from this effect, the malpractice problem has inspired what has come to be called "defensive medicine." This involves the use of unduly expensive and unnecessary procedures with an eye to impressing a possible future jury.[73]

This background material has identified the factors that are likely to raise health care prices, separately or in combination, by lowering competitive pressures.[74] The possible entry of new health care providers is not operating as a realistic threat to pricing at higher than the competitive level.[75] Competition between the actual providers of care in a given geographic market must consequently be policed scrupulously to guard against inflated prices.

III. Legal Analysis

The Sherman Act prohibits contracts or combinations "in restraint of trade."[76] A restraint of trade is any form of resource allocation intended to supersede free, competitive forces.[77] Since 1910 the United States Supreme Court has defined "restraint of trade" by applying what has come to be called the rule of reason.[78] Under this approach the effects of an arrangement are judged within a particular factual context; the arrangement is prohibited if those ef-

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73. *Id.* at 149.

74. One barrier not discussed in the text is the national requirement of a state-issued certificate of need prior to the creation or expansion of a medical facility. National Health Planning and Resources Development Act of 1974, 42 U.S.C. §§ 300k-300t (1976), *as amended by* Health Planning and Development Amendments of 1979, Pub. L. No. 96-79, 93 Stat. 592 (1979).

For a discussion of the anticompetitive effect of the certificates of need, *see* Comment, *Certificate of Need and the Antitrust Laws: Can They Co-Exist?*, 1980 DET. C. OF L. REV. 599.

75. This statement is not meant to imply that there is a national shortage of doctors. Since the markets for care are local, the notion of a shortage or surplus on a national level makes little sense. Until the supply of physicians begins adjusting itself to the demand through the discipline of a price system, there will be localized shortages. There is a concentration of physicians in the northeast and in the urbanized west. The rural west and south have difficulty attracting physicians. J. BRAVERMAN, *supra* note 3, at 35. Since the principal case with which this note is concerned arose in Arizona, there is most likely an undersupply of physicians relative to demand in that state.

76. 15 U.S.C. § 1 (1976).

77. *Forward: Antitrust and the Judiciary*, 12:2 ANTITRUST L. & ECON. REV. 1, 8-9 (1980).

78. Standard Oil Co. v. United States, 221 U.S. 1 (1910).

fects are, on the whole, anticompetitive.[79] Some restraints of trade, though, are believed to have procompetitive effects and ought not be prohibited.[80]

A business relationship becomes categorized as per se illegal and thus no longer entitled to an ad hoc assessment of its reasonableness, however, if the probability of any particular instance of that activity being found to be procompetitive in effect is too small to justify the protractions and uncertainties of case-by-case adjudication.[81] Per se rules are attempts to save judicial resources by taking shortcuts to reasonable results.[82]

A. *Price Fixing and Ancillary Restraints*

Price fixing has long been regarded as per se illegal.[83] Its illegality does not depend upon whether the price level thus arrived at allows only a normal rate of profit for the participating firms because a price which is reasonable today may well be exorbitant tomorrow.[84] Furthermore, price fixing is illegal even if it results in lower prices than some of the participants otherwise would have charged.[85]

The illegality of price lowering arrangements is important to an analysis of the instant case. Three major considerations support holding price lowering schemes illegal. First, contracts to lower prices, as well as those to raise prices, limit the ability of traders to sell in accordance with their own best judgment. Second, an artificial lowering of prices will deprive consumers of services and conveniences for which they otherwise would be willing to pay.[86]

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79. *See, e.g.*, Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977); American Column & Lumber Co. v. United States, 257 U.S. 377 (1921); Standard Oil Co. v. United States, 221 U.S. 1 (1910).

80. United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 218-21 (1940).

81. *See* United States v. Topco Assocs., Inc., 405 U.S. 596 (1972). "The fact is that courts are of limited utility in examining difficult economic problems. Our inability to weigh, in any meaningful sense, destruction of competition in one sector of the economy against promotion of competition in another sector is one important reason we have formulated *per se* rules." *Id.* at 609-10 (emphasis in original) (footnotes omitted).

82. United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 221 (1940).

83. *Id.*

84. Albrecht v. Herald Co., 390 U.S. 145 (1968); Kiefer-Stewart Co. v. Seagram & Sons, 340 U.S. 211 (1951); *In re* Yarn Processing Patent Validity Litigation, 541 F.2d 1127 (5th Cir. 1976). *See generally* Brace & Nissen, *Antitrust: Recent Developments in the Per Se Doctrine*, 61 CHI. B. REC. 49 (1979).

85. Kiefer-Stewart Co. v. Seagram & Sons, 340 U.S. 211, 213 (1951).

86. Albrecht v. Herald Co., 390 U.S. 145, 152-54 (1968). *See also* National Soc'y

Third, courts will not always be able to distinguish a maximum price from a minimum price.[87] *Maricopa County* itself helps demonstrate the difficulty of making that distinction: although the challenged arrangement was referred to by the participants, and by the court, as a maximum price, the state produced evidence tending to show that it had operated in fact as a minimum price.[88] The cogency of the state's evidence on that point was not determined but was left to be determined by the district court upon remand.[89]

Per se prohibitions are applied to disfavored business practices, generally without regard to the specific industry following the practice.[90] An industry-by-industry analysis of the impact of per se rules would demonstrate that such rules are most useful where limit pricing is the greatest threat to consumer welfare, for example, where entry barriers are highest. In one area of antitrust decisionmaking the existence of entry barriers has long played an important role. Courts frequently base decisions as to whether to allow a merger under section 7 of the Clayton Act[91] upon a determination of whether the acquiring firm reasonably might have been expected to enter the same market as the acquired firm through internal expansion. The law favors internal expansion over merger.[92] In banking cases especially, this approach has engendered a concern for state-imposed barriers to the entry of banks into new geo-

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of Professional Eng'rs v. United States, 435 U.S. 679 (1978). "The assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain—quality, service, safety, and durability—and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers." *Id.* at 695.

87. Albrecht v. Herald Co., 390 U.S. 145, 153 (1968), points out that if the actual price charged under a maximum price scheme is nearly always that maximum price, the scheme acquires all the attributes of a minimum fixed price. The distinction ceases to correspond to a difference.

88. [1980-1] TRADE CASES (CCH) at 78,153.

89. "Nor are we prepared to reject out of hand the claim that a ceiling on fees does in fact reduce them." *Id.* at 78,155.

90. *See generally* Note, *Price Fixing and the Per Se Rule: A Redefinition,* Broadcast Music, Inc. v. Columbia Broadcasting System, Inc., 5 DEL. J. CORP. L. 73 (1979).

91. 15 U.S.C. § 18 (1976).

92. *See, e.g.,* United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973); United States v. El Paso Natural Gas Co., 376 U.S. 651 (1964). El Paso was the only supplier of natural gas in California. Pacific Northwest was the only other important interstate pipeline network west of the Rocky Mountains. The proposed merger was disallowed because the Court found that Pacific Northwest was a potential competitor of El Paso. This potential competition was a check upon El Paso's monopoly power, and that check would be removed by a merger. *Id.* at 658-59.

graphic markets. The presence of such barriers makes the courts more hospitable to merger as internal expansion has been made more difficult.[93] That concern is analogous to this note's approach to *Maricopa County*.

The *Maricopa County* decision relies heavily upon *Broadcast Music*[94] for the proposition that certain horizontal arrangements which affect prices are not per se illegal. Dicta in the court's opinion implies that *Maricopa County* would have been decided the other way had the Supreme Court never issued its *Broadcast Music* opinion.[95] Yet the *Maricopa County* court seems confused as to what *Broadcast Music* means. In one sentence it says that *Broadcast Music* mandated a rule of reason analysis of "a traditional form of minimum price fixing."[96] In the very next sentence the court says that *Broadcast Music* denied that the facts with which it was dealing warranted the label "price fixing" at all.[97] In addition to these mutually contradictory sentences there is no analysis of why the *Broadcast Music* court reached its holding.[98]

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93. United States v. Citizens & Southern Nat'l Bank, 422 U.S. 86 (1975); United States v. Marine Bancorp., Inc., 418 U.S. 602 (1974). In *Citizens & Southern*, the State of Georgia had long prohibited Atlanta banks from operating suburban offices. The Citizens and Southern National Bank [hereinafter referred to as C&S] bought 5% of the stock of several suburban banks, and much of the remainder of the stock of those banks was purchased by parties friendly to C&S. These suburban banks thereafter functioned as de facto branch offices, using the C&S logo and receiving advice from C&S officers. *Id.* at 89.

In 1970, Georgia changed its banking laws. C&S applied to the Federal Deposit Ins. Corp. [hereinafter referred to as FDIC] for permission to acquire the de facto branch offices outright. The FDIC authorized the acquisitions. The Justice Department, however, brought suit, alleging both the threat of a reduction in competition in relevant markets and the Sherman Act illegality of the earlier de facto arrangements themselves. *Id.* at 90.

The Supreme Court decided that the de facto arrangements had been a reasonable and procompetitive response to the anticompetitive state-imposed restraints. Those restraints were anticompetitive precisely in that they removed the threat of the entry of banks like C&S into the suburban markets. *Id.* at 91.

Furthermore, the Justice Department's concern that the merger would diminish competition depended upon the Sherman Act argument against the de facto arrangements, and they fell together. If the association with suburban banks prior to merger was a reasonable, competitive response to an anticompetitive law, formalizing those associations through a merger also was not anticompetitive. *Id.* at 121.

94. *See* notes 17-18 *supra* and accompanying text.

95. [1980-1] TRADE CASES (CCH) at 78,156.

96. *Id.*

97. *Id.*

98. In *Broadcast Music*, the majority pointed out that in the absence of an aggregating of licenses thousands of individual negotiations would have to be conducted separately. This, the majority believed, would be a virtual impossibility. Were it possible to conduct individual negotiations, the prohibitive costs would have

Maricopa County and *Broadcast Music* are distinguishable on their facts. The latter case involved an association of composers who sold their copyrighted works to television networks for a flat fee.[99] One effect of this procedure was to reduce the opportunity for the competitive pricing of such works. But the court thought that this anticompetitive effect was incidental to the main lawful purpose, the creation of a mechanism by which the unauthorized use of these materials could be policed.[100] *Broadcast Music* was the most recent in a line of cases that distinguishes agreements having the central purpose and effect of tampering with competitive price from those agreements that have only an incidental or ancillary effect upon prices.[101] This distinction has very little relation to the facts of *Maricopa County*.

Maricopa County presented a direct restraint upon price competition, not an ancillary restraint with some other, lawful, chief purpose and effect. The FMC's arguments justifying the plan effectively concede this point.[102] Furthermore, the legal distinction between the facts of *Maricopa County* and *Broadcast Music* is supported by a genuine economic difference. Ancillary restraints upon competition sometimes can be justified by their economic effect, the reduction of transaction costs. Courts use a rule of reason anal-

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anticonsumer effects which the law should seek to avoid. 441 U.S. at 20.

Justice Stevens, in a separate opinion, concurred with the holding that the blanket license was not price fixing, but dissented from the decision to remand. He would have affirmed the lower court's decision that blanket licensing was an illegal practice on the ground that there was a sufficient record for the Supreme Court to do its own rule of reason analysis and to conclude from that analysis that the anticonsumer effects of the blanket license scheme were greater than whatever the benefits may have warranted. *Id.* at 25 (Stevens, J., concurring).

99. *See* note 17 *supra* for the facts of *Broadcast Music*.

100. Although the copyright laws confer no right on copyright owners to fix prices among themselves or otherwise to violate the antitrust laws, we would not expect that any market arrangements reasonably necessary to effectuate the rights that are granted would be deemed a per se violation of the Sherman Act.

441 U.S. at 19.

101. *E.g.*, Virginia Excelsior Mills, Inc. v. FTC, 256 F.2d 538 (4th Cir. 1958); Leader v. Apex Hosiery Co., 108 F.2d 71, *aff'd*, 310 U.S. 469 (1940); Konecky v. Jewish Press, 288 F. 179 (8th Cir. 1923).

102. The defendants claimed, for example, that setting the level of fees was necessary to preserve minimum standards of quality. [1980-1] TRADE CASES (CCH) at 78,153. There would have been no price fixing, according to the ancillary restraints theory, if FMC simply had set such minimum standards of quality which in turn had an unavoidable effect upon prices as an accidental byproduct. To set a price level on the theory that it will help preserve quality is to enact a direct restraint, however, not an ancillary one.

ysis to preserve agreements that reduce the costs of transacting when such transaction costs otherwise would create a threat to the efficient allocation of resources. For example, a pooling of copyrights can achieve what otherwise would require thousands of individual negotiations and an intricate schedule of fees and uses negotiated between individual composers and users.[103]

The economic benefits of reducing transaction costs may exceed the consumer loss attending an unavoidable and unplanned reduction in price competition with which it is accompanied.[104] But the ancillary restraints exception to the per se rule against price fixing, employed in *Broadcast Music*, was erroneously relied upon in *Maricopa County* in a way that threatens to destroy the rule. The restrictions agreed upon by defendant doctors were initiated explicitly to stabilize prices. There is no reason to believe that the restrictions had any effect upon transaction costs.

The per se rules were described earlier as an aid in the policing of actual competition. The State of Arizona, however, also argued that such rules help maintain potential competition. That is the import of its contention that the FMC's might be pricing so low as to limit the threat of new entry. The court rejected this argument, in part on the authority of Richard Markovits, a scholarly critic of limit price theory who has argued that there can be no satisfactory limit price theory without an account of the mechanism by which low prices will discourage, or high prices encourage, new entrants. There are two likely mechanisms: either the lower prices cause possible entrants to underestimate the available rate of return in that industry or the lowering of prices carries an implicit threat of power to retaliate in a price war against the entrants.[105] Markovits then suggests that most well-placed entrants, in most industries, are conglomerates looking for new areas of expansion. They are unlikely to be intimidated by an implicit threat of expansion.[106] They also are unlikely to be kept in ignorance of the available rate of return in the target market by an artificial lowering of

103. The problem of transactions costs and their tendency to produce inefficient results, that is, to prevent economic actors from bargaining toward their highest joint profits position was first clearly stated in Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1 (1960). Coase's analysis was applied to the problem of the optimal use of copyrights in Besen, Manning & Mitchell, *Copyright Liability for Cable Television: Compulsory Licensing and the Coase Theorem*, 21 J. L. & ECON. 67 (1978).

104. Oliver Williamson reviewed the whole field of antitrust from a transactions cost standpoint in O. WILLIAMSON, MARKETS AND HIERARCHIES (1975).

105. Markovits, *supra* note 22, at 668-69.

106. *Id.* at 671.

prices.[107] Furthermore, limit pricing is not profit maximizing because an established firm can more cheaply preserve its market power by expanding to fill the market demand. Markovits describes this preferable course as "limit investment."[108]

These general objections to the validity of limit price theories have very little applicability to the facts of *Maricopa County*. Conglomerates are not the kind of potential entrant with which the State of Arizona was concerned. Furthermore, the chief expansionary investment a physician can make is an increase in the number of hours per day he spends administering patients' needs.[109] Yet that is not likely to limit entry significantly. A more general objection to the Markovits contention that limit pricing occurs rarely if ever is simply the empirical fact that it does occur. That being the case, further dispute as to its possibility is moot.[110]

Richard Posner, another critic of limit price theory, also was cited by the court in its discussion of Arizona's limit pricing contention.[111] Posner describes limit pricing as a "foolish policy" of "zero monopoly profits,"[112] but he expressly bases that conclusion upon the assumption that the entrant will have the same costs as an established firm, meaning that entry barriers are insignificant.[113] Identical costs, though, are not likely to exist because in many situations the established firms will have developed idiosyn-

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107. *Id.* at 670.

108. *Id.* at 680-84. The main burden of the case that Markovits is attempting to make against limit price theory is the irrationality of that policy in comparison with the much more efficient limits to the entry of competitors that aggressive investment can create. Unfortunately for the Markovits thesis, there is no reason why a combination might not pursue both courses. *See* note 27 *supra* for facts which might indicate that the FMC's were pursuing a course compatible with the Markovits concept of limit investment.

109. S. KLAW, *supra* note 2, at 19.

110. For example, there is reason to believe that duPont has deliberately adopted a pricing strategy to increase its control over the market for a particular paint pigment. Evidence shows that duPont has used limit pricing to make permanent an accidental temporary advantage in its ability to produce a particular paint pigment. duPont's temporary advantage arose when Congress revised particulate emission standards for manufacturers, and the changes affected the production methods of the competitors more severely than they affected those of duPont. A price strategy has enabled duPont to prevent its competitors from achieving the full scale changeover to the now more efficient production method, and to drastically increase its own market share. Shepard, *Anatomy of a Monopoly (II): The Power to Control Prices*, 12:1 ANTITRUST L. & ECON. REV. 73, 88-90 (1980).

111. R. POSNER, *supra* note 22, at 115 n.50.

112. *Id.*

113. *Id.*

cratic skills or information which will give them a cost advantage over entrants.[114]

The state argued that FMC's are in a position to unfairly prevent health maintenance organizations (HMO's) from recruiting subscribers.[115] HMO's are widely believed to present several advantages as a form of health care to consumers and to society.[116] Those economists who have defended the theory of limit pricing believe that such a price strategy is probable only when the actual suppliers, here the established physicians, are able to act in concert.[117] Since the existence of an FMC creates exactly that sort of concerted action, the limit pricing argument has considerable merit in support of retaining the per se illegality rule for price fixing within the health care industry.[118]

The intention to limit entry through pricing may be illegal whatever the probability of success may have been. The dissent contends that "vigorous enforcement of the law could encourage new forms of health care delivery that would significantly benefit

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114. O. WILLIAMSON, *supra* note 104, at 31-33.

115. [1980-1] TRADE CASES (CCH) at 78,156.

116. Ten benefits have been attributed to HMO's as distinct from fee-for-service medicine: The HMO's remove incentives which otherwise exist for the provision of unnecessary services; introduce incentives for cost-effectiveness in the provision of care; create a decisionmaking body with both the knowledge and the incentive to discriminate in the purchase of supply products; strengthen incentives for the efficient internal organization of the supplier operation; eliminate duplicative records; create an incentive for the practice of preventive medicine; encourage referral to specialists when necessary; eliminate duplicative effort on the part of the consumer; provide a better vehicle for post-discharge care; and strengthen the atmosphere for effective peer review. Havighurst, *supra* note 21, at 720-22. All these benefits are gained by combining the provision of care with the function of insurer. The HMO receives a prepaid premium from client families. The premium is determined actuarially, like an insurance company premium, in return for a promise to provide care to the extent of the subscriber's needs over the course of the contracted-for period. *Id.* at 718.

117. Joseph Bain's original formulation of limit price theory rested upon four articulated assumptions: That there is a generally effective concurrence of market action among established sellers; that differences of opinion between these sellers will be settled in favor of the larger firms in the industry; that those larger firms will have the most favorable cost positions; and that those leaders generally will be correct in their estimate of what will forestall entry. J. BAIN, *supra* note 60, at 33.

118. Havighurst, *supra* note 21, at 769-72. In *Maricopa County* the dissent noted that "defendants have quite openly stated that their purpose is to protect fee-for-service medicine against competing forms of health care delivery. While the defendants may take steps to preserve traditional forms of doing business, they may not use restraints of trade to do so." [1980-1] TRADE CASES (CCH) at 78,164 (Larson, J., dissenting).

the public."[119] It also contends that, whether new forms of health care delivery are being barred from entry by limit pricing or not, "It may not be necessary to assess the actual competitive effects of the controverted behavior where the unlawful purpose is clear."[120] Intention to reduce competition may be shown directly or by inference from the actions taken by the defendant.[121]

Maricopa County acknowledged the law's disapproval of predatory pricing, the practice of deliberately sacrificing present revenues for the purpose of driving out rivals and recouping the losses through higher prices to be charged in the absence of competition.[122] The court, however, distinguished predatory pricing from limit pricing.[123] Predatory pricing is a short-term sacrifice, whereas limit pricing would be, the court suggests, a long-term sacrifice analogous to suicide.[124] This is not a convincing distinction. A price designed to limit entry allows the established firms more than the competitive profits, although smaller profits than a short-term, entry-inviting, monopolistic price. This does not resemble suicide.

B. *Exemptions*

The *Maricopa County* court also asserts that the special characteristics of the medical profession deserve unique antitrust treatment. Proposals for professional immunity have received a poor reception in recent Supreme Court decisions.[125] Some of those opinions, however, contain language that recognizes that professional organizations have noncommercial purposes, such as peer review, which might warrant somewhat different treatment than would be appropriate had they come into existence for purely commercial purposes.[126] The dissent noted an important flaw in the use of this argument under the instant facts: price fixing is clearly a commercial activity whether engaged in by doctors or plumbers.[127]

119. [1980-1] TRADE CASES (CCH) at 78,163 (Larson, J., dissenting).

120. *Id.* at n.12.

121. McLain v. Real Estate Bd. Inc., 100 S. Ct. 502 (1980); United States v. United States Gypsum Co., 438 U.S. 422, 436 n.13 (1978); United States v. Aluminum Co. of Am., 148 F.2d 416 (2d Cir. 1945).

122. [1980-1] TRADE CASES (CCH) at 78,156.

123. *Id.* at 78,157.

124. *Id.*

125. *Id.* at 78,154 (citing Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975)).

126. *Id.* at 78,157 (citing National Soc'y of Professional Eng'rs v. United States, 435 U.S. 679, 696 n.22 (1978); Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975); Boddicker v. Arizona State Dental Ass'n, 549 F.2d 626 (9th Cir. 1977)).

127. [1980-1] TRADE CASES (CCH) at 78,161 (Larson, J., dissenting).

There is another flaw in the argument for special antitrust treatment of professional organizations. When Congress intends to carve out an exemption, it can, and does, do so explicitly.[128] The trend at present is in favor of removing some of those exemptions.[129] For example, two provisos in section 1 of the Sherman Act, permitting certain kinds of resale price maintenance, were repealed in 1975.[130] Regardless of the duration of that trend, it is inappropriate for courts to create exemptions or more lenient rules for the professions when Congress, if only by negative implication, has made the professions subject to the same strictures as other occupations.[131] An argument based upon the special characteristics of a trade ought to succeed only if that trade can be brought within a specific statutory exemption.[132]

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128. *E.g.*, Capper-Volstead Act, 7 U.S.C. §§ 291-292 (1976); McCarran-Ferguson Act, 15 U.S.C. §§ 1, 1011-1015 (1976).

129. McCormick, *Modification of the Agricultural Cooperative Exemption: Good or Bad?*, 48 ANTITRUST L.J. 565, 565-66 (1980); Schmalz, *The Insurance Exemption: Can It Be Modified Successfully?*, 48 ANTITRUST L.J. 579, 581-84 (1980).

130.
> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal: *Provided*, That nothing contained in sections 1 to 7 of this title shall render illegal, contracts or agreements prescribing minimum prices for the resale of a commodity which bears, or the label or container of which bears, the trademark, brand, or name of the producer or distributor of such commodity and which is in free and open competition with commodities of the same general class . . . *Provided further*, That the preceding proviso shall not make lawful any contract or agreement, providing for the establishment or maintenance of minimum resale prices on any commodity herein involved. . . .

15 U.S.C. § 1 (1970) (emphasis in original) (Provisos repealed by Act of Dec. 12, 1975, Pub. L. No. 94-145, 89 Stat. 801 (1975)).

131. Silver v. New York Stock Exch., 373 U.S. 341, 355-60 (1963).

132. The insurance exemption, however, at one time was nonstatutory. Insurance was defined as a noncommercial activity in Paul v. Virginia, 75 U.S. (8 Wall) 168 (1869). Therefore, since the regulatory power of Congress on which the antitrust laws constitutionally depend is limited to commerce among the several states, language echoed in the Sherman Act itself, an insurance exemption was widely assumed. United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533 (1944), overruled *Paul*'s noncommercial characterization and created the demand for passage of a statutory exemption. That demand was met in 1945. 15 U.S.C. §§ 1, 1011-1015 (1976).

The antitrust exemption for actions pursuant to a state policy also may be nonstatutory. In a federal system, where states retain sovereignty, attribution to Congress of an intent to lessen a state's control over its officers will not be made without strong indication in the text of the statute to that effect. Parker v. Brown, 317 U.S. 341, 350-51 (1943). Generally, then, those exemptions which are not statutory are grounded in the Constitution. *Maricopa County* may be seen as hinting at the possibility of a common-law exemption from normal antitrust rules in some fields. There is no precedent for this.

At the district court level defendants argued that the activities of the FMC's were within the statutory exemption for the business of insurance. The district court stayed a decision on a motion to dismiss on this ground pending the decision of a case then before the Supreme Court.[133] In that case, *Royal Drug Co. v. Group Life & Health Insurance Co.*,[134] Blue Shield of Texas was alleged to have entered into agreements fixing the retail prices of pharmaceuticals. The trial court granted summary judgment to defendant on the ground that the McCarran-Ferguson Act[135] exempted the business of insurance from the federal antitrust laws to the extent it is regulated by state laws. The Supreme Court eventually found, while *Maricopa County* was still in litigation at the district court level, that the pharmacies had not acquired Blue Shield's insurance exemption by association and that, on the contrary, Blue Shield had lost the benefit of McCarran-Ferguson by acting in concert with the pharmacies.[136]

The holding of the court in *Group Life & Health Insurance Co.*[137] is determinative of the insurance exemption issue on the *Maricopa County* facts. Insurance companies are involved in the operation of the FMC's, and the foundations themselves might be said to have been functioning as insurers. The exemption, though, is to be narrowly construed and will not cover such cases.[138]

C. *Extent of Judicial Experience*

Possibly the single most important factor in the *Maricopa County* reasoning was the unwillingness to impose a per se rule in the absense of greater judicial experience with the competitive conditions of the health care market. The court regretted that "we know very little about the impact of this and many other arrangements within the health care industry. *This alone* should make us reluctant to impose a per se rule with respect to the challenged

133. State of Arizona v. Maricopa County Medical Soc'y, [1979-1] TRADE CASES (CCH) ¶ 62,415, at 76,490 (filed December 27, 1978).

134. 556 F.2d 1375 (5th Cir. 1977), *aff'd*, 440 U.S. 205 (1979).

135. *Id.* at 205.

136. *Id.* at 231.

137. *Id.* at 232-33.

138. Justice Brennan dissented, arguing that when an agreement with a provider of benefits promised in a policy constitutes a critical element of risk prediction and directly affects the cost of providing the desired protection, such an agreement is a part of the business of insurance and is immune from the prohibitions of the Sherman Act. *Id.* at 252-53 (Brennan, J., dissenting). *See generally* Comment, *The McCarran-Ferguson Act: A Time for Procompetitive Reform*, 29 VAND. L. REV. 1271 (1976).

arrangement."[139] Yet the newness of judicial experience with an industry should not be the determinative factor in the choice between a per se rule and the rule of reason.

In *Continental T.V., Inc. v. GTE Sylvania Inc.*[140] the Supreme Court reasoned that the extent of the per se rules ought to be determined entirely by their probable economic impact rather than by concerns for retailer autonomy or other social considerations.[141] In order to make a determination on economic grounds, a court should take into account both the structural features of the industries to which the per se rules will be applied and the effects of the practices to be prohibited upon those structural features. Justice Brandeis remarked, in a frequently quoted passage, that the rule of reason must be applied with an eye upon "facts peculiar to the business to which the restraint is applied."[142]

Likewise, if courts are to judge the validity of per se rules in particular businesses, which is the *Maricopa County* approach, the *Sylvania* economic impact approach requires a review of facts peculiar to the business with which one is concerned. *Sylvania* overturned a per se rule prohibiting vertical consumer restraints, that is, restraints imposed by a manufacturer seeking to reduce competition among the various retail outlets for its brand of a product. A per se prohibition against this kind of restraint upon intrabrand competition[143] had been announced in *United States v. Arnold, Schwinn & Co.*[144] The *Sylvania* court, in overturning *Schwinn*, decided that the decrease in intrabrand competition may well be compensated for by an increase in interbrand competition, that is, Sylvania's increased effectiveness as a rival of other television manufacturers.[145] A rule of reason seemed better adapted than a per se rule to deal with the inescapable trade-offs between intrabrand and interbrand competition.[146] Justice White, concurring in *Sylvania*,

139. [1980-1] TRADE CASES (CCH) at 78,154 (emphasis added).

140. 433 U.S. 36 (1977).

141. *Id.* at 56.

142. Chicago Bd. of Trade v. United States, 246 U.S. 231, 238-39 (1918).

143. Intrabrand competition arises between franchisees selling the same brand of a product.

144. 388 U.S. 365 (1967).

145. 433 U.S. at 51-52.

146. *Id.* at 52 n.19.

In the wake of *Sylvania*, a serious question has arisen as to whether the per se rule against horizontal market division may now be subject to erosion. *See* Calkins & Polden, *Intrabrand Territorial Allocations and the Per Se Rule*, 30 DRAKE L. REV. 1 (1980-81).

noted that the *Schwinn* and *Sylvania* holdings might have been reconciled had the majority concerned itself with the differences between Schwinn's position in the bicycle market and Sylvania's position in the television market. Dominant firms need not be treated according to the same rules as fringe firms, and "Unlike Schwinn, Sylvania clearly had no economic power in the generic product market."[147]

The specific facts discussed in this note with regard to the health care industry are very clear. The FMC's had economic power within their geographic markets. Restrictions on entry posed by state licensing systems and an AMA veto over new facilities for medical education limited potential competition. The interlocking of the AMA and the drug industry gave the former an extra incentive to maintain that limit. Finally, the threat of malpractice litigation has further increased health care costs. A per se rule against price fixing, which would increase the efficiency of the policing of actual price competition,[148] is especially important in contemporary health care.[149]

IV. Conclusion

Price fixing has long been regarded as per se illegal. A series of cases provides authority for an exception to that rule when an agreement's effect upon prices is an accidental and necessary ancillary restraint resulting from an agreement among competitors who have another, lawful, principal purpose and effect. *Broadcast Music* was an ancillary restraint case which authorized the application of a rule of reason to an agreement among composers to pool their copyrights. The *Maricopa County* decision mistakenly cited *Broadcast Music* as authority for a softening of the traditional per se prohibition of intended price fixing.

The per se illegality of price-fixing arrangements does not de-

147. 433 U.S. at 63 (White, J., concurring).

148. In Northern Pac. Ry. Co. v. United States, 356 U.S. 1 (1958), the Court reasoned that the per se rule is justified by the need to avoid "an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries, in an effort to determine at large whether a particular restraint has been unreasonable. . . ." *Id.* at 5.

149. The Supreme Court has at least hinted that entry barrier problems are a factor in determining whether and in what degree the antitrust rules apply in the legal profession, although in the case in which it dropped this hint, Bates v. State Bar, 433 U.S. 350, 378 (1977), the challenged practice was held to be protected by the state action doctrine of Parker v. Brown, 317 U.S. 341 (1943).

pend upon whether those arrangements result in an increase in prices. Price lowering arrangements are per se illegal as well because competition is believed to be the most efficient method of allocating resources in regard to all elements of a bargain. Limit price theory defends the economic rationality of this belief because it asserts that immediate price lowering arrangements may inhibit entry by competitors and thus in the long run may preserve a price above that which competition would permit.

The FMC's involved as defendants in *Maricopa County* are in a position to unfairly prevent HMO's from recruiting subscribers. If the entry costs of an HMO are somewhat above the operating costs of an established physician, the established physicians, when acting in concert, are able to agree to a price above the competitive level but low enough to discourage the development of the HMO as an alternative form of health care. The law ought to regard this as an anticonsumer threat.

Maricopa County asserts that the special characteristics of the medical profession deserve unique antitrust treatment. There is no precedent for such treatment of clearly commercial activities within a profession. Furthermore, this claimed professional exemption cannot be brought within any of the statutory exemptions including, on these facts, that for the business of insurance.

The court was unwilling to impose a per se rule in the absence of greater judicial experience with the competitive conditions of the health care industry. This argument implies that the degree of judicial experience with a field ought to be the sole criterion governing the applicability of per se rules. Precedent and common sense, however, suggest that the presence of barriers to the entry of new competitors ought to be another factor in that determination of applicability.

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