The Rule of Reason

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THE RULE OF REASON

Herbert Hovenkamp*

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Introduction

Courts evaluate most antitrust claims under a “rule of reason,” which requires the plaintiff to plead and prove that defendants with market power have engaged in anticompetitive conduct. To conclude that a practice is “reasonable” means that it survives antitrust scrutiny.\(^1\) This is in contrast to antitrust’s “per se” rule, in which power generally need not be proven and anticompetitive effects are largely inferred from the conduct itself.\(^2\) The domain of the per se rule has been narrowing, however.\(^3\) Today it extends to “naked”\(^4\) price fixing and market division agreements, a small subset of boycotts, or concerted refusals to deal, and – by a very thin thread – some tying arrangements.\(^5\)

This article provides a litigation field guide for antitrust claims under the rule of reason – or more precisely, for situations when application of the rule of reason is likely. At the time pleadings are drafted and even up to the point of summary judgment, the parties are often uncertain whether a court will apply the rule of reason. Because the choice of rule presents a question of law, it is generally established prior to trial.\(^6\) The first section examines pleading and summary judgment rules, including the role of stare decisis, arguing that stare decisis should apply to a mode of analysis rather than to a specific class of restraints.\(^7\) Then it discusses numerous problems surrounding the burden of proof and the quality of evidence needed to shift

\(^2\)E.g., Newman v. Universal Pictures, 813 F.2d 1519, 1522–23 (9th Cir. 1987), cert. denied, 486 U.S. 1059 (1988) (per se rule “relieves plaintiff of the burden of demonstrating an anticompetitive effect, which is assumed . . . .”).
\(^3\)See discussion infra, text at notes 197–208.
\(^4\)On the meaning of “naked,” see discussion infra, text at notes 230–231.
\(^5\)European Union Competition Law makes a roughly similar distinction between restraints that are evaluated “by object,” which is roughly similar to the per se rule; and restraints that are evaluated “by effect,” which is roughly similar to the rule of reason. See Guidance on Restrictions of Competition “by object” for the Purpose of Defining Which Agreements May Benefit from the De Minimis Notice, at 3, COM (2014) 198 final (June 25, 2014), http://ec.europa.eu/competition/antitrust/legislation/de_minimis_notice_annex.pdf.
\(^6\)See discussion infra text at notes 40–45.
\(^7\)See discussion infra text at notes 24–71.
the burden. I argue that the plaintiff’s burden for a prima facie case should be relatively stringent for the market power requirement, but relatively light for proof of an anticompetitive act.\(^8\) I also show why a consumer welfare standard for antitrust violations is the only manageable one for evaluating practices under the rule of reason. The alternative, general welfare standard requires that all consumer losses be quantified and compared with producer efficiency gains, as well as likely effects on others. Aside from any substantive reasons for preferring a consumer welfare standard, a general welfare standard is impossible to apply in any but the most obvious cases. The consumer welfare standard queries only whether output will be higher or lower (or prices lower or higher) under the restraint. This query can be difficult enough but is nevertheless much simpler than the proof requirements for a general welfare standard.\(^9\) Finally, this section examines the possibility of truncated, or “quick look,” analysis as an alternative to both the rule of reason and the per se rule, arguing against recognition of any categorical “quick look.”\(^10\) I conclude with a brief discussion of “balancing,” and why the rule of reason’s staged set of queries is legitimately designed so that courts can avoid balancing whenever possible.\(^11\)

The next section turns to identification of the types of conduct to which antitrust’s rule of reason applies.\(^12\) It also examines the question of appropriate remedies, particularly when the basic features of joint activity are unchallenged or conceded to be competitive but a specific provision or practice threatens competition. Then it turns briefly to the special case of antitrust restraints in markets for intellectual property rights.\(^13\) A final section examines the market structure requirements for antitrust rule of reason cases, including the assessment of power and application of the rule of reason to vertical agreements,\(^14\) as well as to agreements that have both horizontal and vertical elements.\(^15\)

*   *   *

The rule of reason was born in the 1911 *Standard Oil* case. Writing for the Court, Chief Justice White reached the pedantic and rather silly conclusion that one cannot decide antitrust cases except by using “reason.” As a result, it followed that a rule of reason should be applied.\(^16\) Actually, as Associate Justice fifteen years earlier White had spoken much more sensibly in the *Trans-Missouri* railroad price fixing case. He dissented from Justice Peckham’s opinion for the

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\(^{8}\)See discussion *infra* text at notes 89–107.

\(^{9}\)See discussion *infra* text at notes 144–50.

\(^{10}\)See discussion *infra* text at notes 151–86.

\(^{11}\)See discussion *infra* text at notes 187–196.

\(^{12}\)See discussion *infra* text at notes 197–271.

\(^{13}\)See discussion *infra* text at notes 272–81.

\(^{14}\)See discussion *infra* text at notes 282–324.

\(^{15}\)See discussion *infra* text at notes 325–34.

\(^{16}\)See *Standard Oil* of N.J. v. United States, 221 U.S. 1, 64–65 (1911):

> As the cases cannot, by any possible conception, be treated as authoritative without the certitude that reason was resorted to for the purpose of deciding them, it follows as a matter of course that it must have been held by the light of reason, since the conclusion could not have been otherwise reached, that the assailed contracts or agreements were within the general enumeration of the statute, and that their operation and effect brought about the restraint of trade which the statute prohibited.
Court holding that the Sherman Act automatically condemned all horizontal restraints. White protested in Trans-Missouri that the Act could not conceivably condemn every restraint on freedom of trade, “whether reasonable or unreasonable.” Rather, “the words ‘restraint of trade’ embrace only contracts which unreasonably restrain trade, and, therefore, that reasonable contracts, although they, in some measure, ‘restrain trade,’ are not within the meaning of the words.”

Justice White clearly had the better of this disagreement with Justice Peckham. Even a simple buy-sell agreement for 100 bricks “restrains trade” to the extent that it removes those bricks from the market. Literally, condemnation of “every” restraint would outlaw ordinary business agreements.

The combination of the Trans-Missouri and Standard Oil decisions produced considerable confusion for some time. The Trans-Missouri majority seemed to say that the Sherman Act reached every restraint on competition, whether reasonable or not. Standard Oil made it seem, however, that all restraints should be governed by the rule of reason. The Supreme Court cleared up some of the confusion in its 1927 Trenton Potteries case. Justice Stone explained that although restraints generally are subjected to a rule of reason, specific types of restraints such as “agreements to fix [and] maintain prices” are automatically deemed unreasonable.

For horizontal restraints, which are agreements among competitors or potential competitors, the classification system suggested by Trenton Potteries roughly resembles the one that we use today. By contrast, the law of vertical practices has been much less stable, mainly because of controversy about their purpose and effect. Already in 1911 the Supreme Court indicated that resale price maintenance—supplier setting of a dealer’s resale prices—was unlawful per se. Dicta in its 1949 Standard Stations decision, an exclusive dealing case,

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17 United States v. Trans-Missouri Freight Ass’n, 166 U.S. 290, 346 (1897). See also Justice Peckham’s counter, id. at 328:

    the plain and ordinary meaning of such language is not limited to that kind of contract alone which is in unreasonable restraint of trade, but all contracts are included in such language, and no exception or limitation can be added without placing in the act that which has been omitted by congress.

Edward Douglass White had served as an Associate Justice from 1894 until 1910. On Dec. 19, 1910, he became Chief Justice.


19 Id. at 396–98.

    The aim and result of every price-fixing agreement, if effective, is the elimination of one form of competition…. Agreements which create such potential power may well be held to be in themselves unreasonable or unlawful restraints, without the necessity of minute inquiry whether a particular price is reasonable or unreasonable as fixed and without placing on the government in enforcing the Sherman Law the burden of ascertaining from day to day whether it has become unreasonable through the mere variation of economic conditions.


21 Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911). Although the Court did not use the term “per se,” it spoke of RPM contracts as a class, and made them automatically illegal without
indicated that tying arrangements should also be treated very harshly. The Supreme Court followed this course in the 1950s, declaring certain ties unlawful per se but requiring proof of market power in the tying product. That requirement makes ties unique among per se offenses. Exclusive dealing itself, however, has always remained under at least a qualified rule of reason.

The Rule of Reason and the Courts

The antitrust statutes provide almost no guidance about the formation of specific antitrust rules of illegality. The Sherman Act says nothing useful on the subject. The Clayton Act proscribes price discrimination, tying and exclusive dealing, and mergers where the effect “may be substantially to lessen competition.” This language requires the court to assess the impact of the challenged restraint on competition, suggesting that per se treatment is not appropriate but saying little else. In fact, the Act does not even define the term “competition” or provide any test for measuring whether it has been lessened.

This spare language makes the courts unusually important in the development of antitrust rules. They are charged both with creating the substance of antitrust and with fashioning appropriate rules of pleading and procedure, including assignment of proof burdens.

Pleading Requirements

In Twombly the Supreme Court very considerably tightened up the pleading requirements for antitrust cases. The plaintiff had alleged that the parallel failure of the regional telephone operating companies to enter one another’s geographic territories evidenced a conspiracy among

regard to power or anticompetitive effects. See id. 399–400. On the per se rule for RPM under Dr. Miles, see 8 AREEDA & HOVENKAMP, supra note 1, at ¶1620.


23See N. Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1956) (“Among the practices which the courts have heretofore deemed to be unlawful in and of themselves are . . . tying arrangements.”); Times-Picayune Pub. Co. v. United States, 345 U.S. 594, 609 (1953) (dicta: tying unlawful per se under Section 1 of Sherman Act whenever the seller has market power in the tying product and a substantial volume of tied product commerce is restrained). The Court hinted at this outcome in 1947, in Int’l Salt Co. v. United States, 332 U.S. 392, 396 (1947) (“It is unreasonable, per se, to foreclose competitors from any substantial market . . . .”).


them not to enter.\textsuperscript{28} The problem with that claim is that firms decline to enter one another’s markets all the time, and for reasons that have nothing to do with antitrust conspiracy. Pet stores do not sell bicycles and bicycle shops do not sell pets, but that fact alone hardly suggests that they have agreed to stay out of one another’s markets.\textsuperscript{29} Twombly turned the problem of a concededly inadequate pleading in a particular case into a globalized set of constraints that are widely viewed as requiring a form of fact pleading rather than simple notice pleading of a claim. In antitrust cases at least, the result has been prolix complaints often running to 100 pages or more,\textsuperscript{30} assuring plaintiffs that they have enough “factual matter” to resist dismissal.\textsuperscript{31}

While parallel pricing suggests interdependence of behavior, parallel failure to move into new markets ordinarily does not.\textsuperscript{32} That is to say, Twombly could have been written much more narrowly as an antitrust decision concerning the types of conduct that suggest conspiracy. Instead, the Court majority wrote a global attack on pleading requirements, reaching far beyond antitrust to all pleadings in the federal courts.

Post-Twombly decisions have consistently held that in antitrust cases pled under the rule of reason a plaintiff must adequately plead market power and the anticompetitive effects of the challenged restraints.\textsuperscript{33} A successful complaint must not simply assert that the defendant has market power, or even that a particular grouping of sales is a relevant market. Rather, it must allege specific reasons, such as lack of substitutability with other products that, if true, would justify such a finding.\textsuperscript{34} That is, under Twombly a pleading must not merely provide notice of the contours of a complaint, it must also provide sufficient allegations from which the judge can infer that if the alleged facts are true the claim is plausible.\textsuperscript{35}


\textsuperscript{29}See Herbert Hovenkamp, The Pleading Problem in Antitrust Cases and Beyond, 95 IOWA L. REV. BULL. 55 (2010).

\textsuperscript{30}See id. at 56–57.

\textsuperscript{31}Twombly, 550 U.S. at 556.

\textsuperscript{32}The plaintiffs had alleged an alternative theory, namely that the geographic market assignments recognized by the Telecommunications Act were appealing, and each knew that upsetting that state of affairs would be bad for all. See id. at 568. In any event, the complaint alleged no facts supporting this theory. On interdependence, see 6 AREEDA & HOVENKAMP, supra note 1, at ¶ 1411; Hovenkamp, Pleading Problem, supra note 28, at 65–66.

\textsuperscript{33}See Robert G. Bone, Twombly, Pleading Rules, and the Regulation of Court Access, 94 IOWA L. REV. 873, 881 (2009).

\textsuperscript{34}See, e.g., Simpson v. Sanderson Farms, Inc., 744 F.3d 702, 710–11 (11th Cir. 2014) (“Under our post-Twombly precedent, rule-of-reason antitrust plaintiffs must always “present enough information in their complaint to plausibly suggest the contours of the relevant geographic . . . market . . . [O]ur antitrust precedent requires plaintiffs to plead factual support for all manner of market claims”….).”

The law of pleading of exclusionary practices is somewhat less developed, but *Twombly* appears to require allegations that, if true, show that the defendant engaged in one or more anticompetitive practices that tended to create or preserve monopoly power, and that the plaintiff was injured by the practice. *A fortiori*, if the challenge is under the per se rule, the complaint must also plead a per se offense.\(^{36}\) Of course, a complaint can have multiple counts, some of which are to be assessed under the rule of reason while others are per se.

*Twombly* pleading standards create a difficult situation for plaintiffs who need access to discovery in order to identify the facts they must allege. This is particularly true for conspiracies or other practices whose success depends on secrecy. Evidence of such conspiracies may be tightly held by the defendants, and a plaintiff ordinarily would not have access to it when the complaint is drafted. A dismissal prior to discovery may entail that the evidence never will be revealed. Some courts have acknowledged this issue and responded that the conspiracy allegations must simply be plausible.\(^{37}\) The question at the pleading stage is whether the allegations are sufficient to entitle the plaintiff to discovery.\(^{38}\)

The pleading problem is generally different for per se cases than for rule of reason cases. In a per se case the question is typically *whether* an anticompetitive agreement such as price fixing exists, and the defendants are strongly motivated to keep such agreements secret. Proof of agreement may be impossible without access to discovery.\(^{39}\) By contrast, in the typical rule of reason case the existence of the agreement is not in dispute, but only whether it is anticompetitive under the circumstances. This approach places a premium on objective tests based on evidence that is typically not in the defendant’s exclusive control. As a general matter, evidence of market structure and product substitutability should be sufficiently available to the plaintiff to support a plausible claim.\(^{40}\) The same thing would ordinarily be true of an exclusionary practice, whose impact must affect someone other than the defendant.

In sum, the test for adequate pleading in a rule of reason antitrust case should be whether objective evidence of market structure and exclusionary effect – both of which can ordinarily be

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\(^{36}\) *Starr v. Sony BMG Music Entm't*, 592 F.3d 314, 321–24 (2d Cir. 2010); *Rick-Mik Enters, Inc. v. Equilon Enters. LLC*, 532 F.3d 963, 971–73 (9th Cir. 2008); *Kendall v. Visa U.S.A., Inc.*, 518 F.3d 1042, 1048 (9th Cir. 2008).

\(^{37}\) *E.g.*, *Anderson News, LLC v. Am. Media, Inc.*, 680 F.3d 162, 189–90 (2d Cir. 2012) (“the question is whether there are sufficient factual allegations to make the complaint's claim plausible . . . . [O]n a Rule 12(b)(6) motion it is not the province of the court to dismiss the complaint on the basis of the court's choice among plausible alternatives.”).

\(^{38}\) *E.g.*, *Evergreen Partnering Group, Inc. v. Pactiv Corp.*, 720 F.3d 33 (1st Cir. 2013). *Cf. NicSand, Inc. v. 3M Co.*, 507 F.3d 442 (6th Cir. 2007) (mere “possibility” of entitlement to relief insufficient).


obtained without access to the defendant’s own records – indicate that an antitrust violation is plausible. Having established that, the plaintiff should be entitled to discovery.

**Question of Law**

While pleadings are dominated by factual allegations, the ultimate question of which antitrust rule applies is one of law.\(^4^1\) In speaking of the decision to apply a per se rule the Supreme Court often refers to “judicial experience” as the determinative factor.\(^4^2\) Juries do not have “judicial experience.” Indeed, most of them do not have any experience at all on the issue. Because experts testify only on issues of fact, this also means that expert testimony on the ultimate question of per se vs. rule of reason assessment is inadmissible,\(^4^3\) although expert testimony on facts can certainly aid the court in determining which rule to apply.

The ultimate question whether to apply the per se rule depends on whether the challenged practice has characteristics suggesting that more elaborate inquiry under the rule of reason will be either unnecessary or counterproductive.\(^4^4\) Juries have no such ability, given that they are examining only the facts of the case before them.

This hardly makes the fact finder irrelevant. *Within* the rule of reason the question whether a restraint is “reasonable” is ordinarily one of fact.\(^4^5\) Juries may be asked to consider several subsidiary questions, such as whether a restraint is naked or is ancillary to other productive activity,\(^4^6\) whether a challenged practice reduces costs or improves product quality, or whether the defendants are actually competitors. For example, while an expert may not testify that a particular practice is unlawful per se, she certainly could testify that there is no integration

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\(^4^1\)E.g., Craftsmen Limousine, Inc. v. Ford Motor Co., 363 F.3d 761 (8th Cir. 2004), aff’d, 491 F.3d 380 (2007), cert. denied, 552 U.S. 1040 (2007) (whether rule of reason applies is question of law).

\(^4^2\)E.g., Nat’l Collegiate Athletics Assoc. v. Bd. of Regents of the Univ. of Okla., 468 U.S. 85, 100–01 (1984) (“judicial experience” determines which rule is to be applied); F.T.C. v. Superior Court Trial Lawyers Ass’n., 493 U.S. 411, 433 (1990) (“Once experience with a particular kind of restraint enables the Court to predict with confidence that the rule of reason will condemn it, it has applied a conclusive presumption that the restraint is unreasonable,” quoting Arizona v. Maricopa Cty. Med. Soc’y, 344 (1982)); Broad. Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 2 (1979) (“It is only after considerable experience with certain business relationships that courts classify them as per se violations of the Sherman Act,” quoting United States v. Topco Assocs., Inc., 405 U.S. 596, 607–08 (1972)); California ex rel. Brown v. Safeway, Inc., 615 F.3d 1171, 1178 (9th Cir. 2010) (“Per se analysis examines whether prior judicial experience with the type of restraint at issue is sufficient to allow a determination that it would always or almost always tend to restrict competition. . . .”); In re Insurance Brokerage Antitrust Litig., 618 F.3d 300, 316 (3d Cir. 2010) (“judicial experience”).

\(^4^3\)In re Cardizem CD Antitrust Litig., 105 F. Supp. 2d 682, 694 (E. D. Mi. 2000), reh’g and reh’g en banc denied, 332 F.3d 896 (2003), cert. denied, 543 U.S. 939 (2004) (excluding economist’s testimony to the effect that certain activity should be analyzed under the rule of reason).

\(^4^4\)See discussion infra, text at note 46.

\(^4^5\)See Arizona v. Maricopa Cty. Med. Soc’y, 457 U.S. 332, 343 (1982) (“the rule of reason requires the fact finder to decide whether under all the circumstances of the case the restrictive practice imposes an unreasonable restraint on competition”).

\(^4^6\)E.g., Wholesale Grocery Prods. Antitrust Litig., 752 F.3d 728, 733–34 (8th Cir. 2014) (while choice of rule presents question of law, “underpinning that purely legal decision are numerous factual questions”); Perceptron, Inc. v. Sensor Adaptive Mach., Inc., 221 F.3d 913 (6th Cir. 2000) (once the court had determined that the rule of reason applied, it was up to the jury to determine whether a five-year noncompetition agreement contained in a patent license was unreasonable).
of business among the defendants, or that a claimed efficiency is really not what it is stated to be. Alternatively, she might provide and support efficiency explanations that, if accepted, would take a case out of the per se rule.

Irrational Summary Judgment Rules

The rough equivalent to Twombly in summary judgment cases is Matsushita, which considerably raised the bar for plaintiffs wishing to get their antitrust claims in front of a jury. The prior law had indicated that summary judgment should be used “sparingly” in antitrust cases, because “motive and intent play leading roles” and the evidence is held by “alleged conspirators” and “hostile witnesses.” As a result, evaluating a case depended crucially on jury evaluation of the truthfulness of testimony. In sharp contrast, Matsushita moved the focus away from witness veracity and toward objective, market-based factors tending to establish whether the plaintiff’s claim together with supporting evidence had crossed a plausibility threshold.

Once a motion to dismiss is granted, the plaintiff has no automatic right to amend, but judges typically permit at least one amended complaint. By contrast, at the summary judgment stage, plaintiffs typically get only one bite at the apple. This can have perverse consequences for antitrust discovery and proof. The problem unfolds like this: an antitrust plaintiff who believes it has a per se case pursues it through discovery that way, making it unnecessary to prove market power or a relevant market, or to show anticompetitive effects. This also makes it unnecessary to invest in expert testimony to establish these things. Later on, when discovery has proceeded to the point that a motion for summary judgment is in order, the court agrees with the defendant that the case should have proceeded under the rule of reason. As a result, it dismisses the complaint because essential elements of a rule of reason case are missing. For example, in the Dagher joint venture case the plaintiff had brought its claim under the per se rule or, alternatively, a “quick look” rule. The district court had granted summary judgment after concluding that the plaintiffs had “disclaimed any reliance on the traditional rule of reason.”

   if the factual context renders respondents’ claim implausible — if the claim is one that simply makes no economic sense — respondents must come forward with more persuasive evidence to support their claim than would otherwise be necessary.
49E.g., Kendall v. Visa, U.S.A., Inc., 518 F.3d 1042 (9th Cir. 2008); In re Capacitors Antitrust Litig., 154 F. Supp. 3d 918 (N.D. Cal. 2015). See also In re Ins. Brokerage Antitrust Litig., 618 F.3d 300, 317 (3d Cir. 2010) (citing AT&T Corp. v JMC Telecom, LLC, 470 F.3d 525, 531 (3d Cir. 2006), “While pleading exclusively per se violations can lighten a plaintiff's litigation burdens, it is not a riskless strategy. If the court determines that the restraint at issue is sufficiently different from the per se archetypes to require application of the rule of reason, the plaintiff's claims will be dismissed.”). Cf. In re Processed Egg Products Antitrust Litig., ____ F.Supp.3d ___, 2016 WL 6993366 (E.D. Pa. Sep. 9, 2016). The court concluded that a plaintiff who mistakenly pleads under the per se rule may have a second chance to plead under the rule of reason, provided that it did not completely disavow its intent to pursue a rule of reason complaint in the alternative.
The Ninth Circuit reversed the district court, finding a fact issue as to application of the per se rule. The Supreme Court then reversed the Ninth Circuit and dismissed the complaint.\(^{52}\)

The problem with this sequence of events is that if there is any reasonable chance that the court will ultimately require the rule of reason, the plaintiff has no choice but to proceed through discovery under that rule even if the chance is small. This means that the value of the per se rule is lost in a significant number of cases, because the plaintiff must do all of the things that rule of reason analysis requires, including developing expert testimony on questions about relevant market, market power, and anticompetitive effects, even though the case may ultimately be decided under the per se rule. At least prior to trial, the greatest cost in litigating a rule of reason case is the cost of developing a record, so most of the cost savings that the per se rule promises will have been lost.

One way to address the problem is for courts to hold that, once the court has granted a defendant’s motion for summary judgment on a per se complaint, the plaintiff should be permitted to amend to include a rule of reason count. Assuming the amended complaint is sustained, it could then develop a record under the rule of reason. Such a rule should naturally be subject to the judge’s discretion. The defendant can of course offer evidence indicating that the plaintiff should have known all along that the case must be tried under the rule of reason.\(^{53}\) The court must decide whether the plaintiff’s initial allegations were objectively justified, even though subsequently found to be mistaken. If so, the case should be remanded for additional discovery addressing the rule of reason issues.

**Stare Decisis**

Stare decisis attaches more strongly to issues of statutory construction than to interpretation of constitutional provisions. Congress can much more easily change statutes when it disagrees with the Supreme Court has done.\(^{54}\) Indeed, the Clayton Act itself was in significant part a response to a Supreme Court decision that Congress found unappealing.\(^{55}\) One effect of this reluctance is that formal antitrust doctrine, such as the per se rules against resale price maintenance and tying, linger long after they have become economically indefensible. For example, relentless economic criticism of the antitrust per se rule against resale price

\(^{52}\)Texaco, Inc. v. Dagher, 547 U.S. 1, 8 (2006). *See also* California Dental Ass’n v. FTC, 224 F.3d 942, 958 (9th Cir. 2000) (having failed to persuade the Supreme Court to evaluate dental association’s restraint under a “quick look,” the FTC would not be permitted to augment the record to show a violation under the rule of reason).

\(^{53}\)For example, in *Dagher*, 369 F.3d at 1117, even the Ninth Circuit chose the wrong rule.

\(^{54}\)Kimble v. Marvel Entm’t, LLC, 135 S. Ct. 2401, 2409 (2015) (“stare decisis carries enhanced force when a decision, like *Brulotte*, interprets a statute…. [C]ritics of our ruling can take their objections across the street….’’); Hilton v. S.C. Pub. Railways Comm’n, 502 U.S. 197, 202 (1991) (“Considerations of stare decisis have special force in the area of statutory interpretation, for … Congress remains free to alter what we have done.”). *See also* Cont’l T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 47–48 (1977) (White, J., dissenting, objecting that minority was not taking seriously the principle that stare decisis applies more strongly in cases of statutory construction).

maintenance, announced in 1911, began in the 1960s. The Supreme Court did not overrule *Dr. Miles*, however, for another half century. In other cases the Court adheres to economically deficient rules, even acknowledging their deficiencies but observing that Congress has chosen not to change the law. Another effect that shows up frequently in antitrust is that the courts take advantage of the very open ended language of the antitrust laws by qualifying former holdings, often severely, without overruling them.

In the antitrust rules dividing per se illegality from the rule of reason, stare decisis operates as a unique one way ratchet. When the Court deviates from earlier decisions and applies the per rule, stare decisis is not a factor. A situation in point is the progression from *White Motor* to *Schwinn* to *GTE Sylvania*. In *White Motor* the Supreme Court found a manufacturer’s nonprice vertical restrictions to be reasonable. That decision was overruled only four years later by *Schwinn*, which applied the per se rule with no discussion of stare decisis. A decade later the Court reversed itself again, applying a rule of reason in *GTE Sylvania*. Now, however, the Court felt compelled to discuss stare decisis concerns, and Justice White raised them in his concurring opinion.

This unbalanced treatment of stare decisis is inherent in the logic of the per se rule. Stare decisis does not attach to a court’s conclusion that it is refusing to apply the per se rule because courts have insufficient experience with the practice at issue. As soon as courts acquire more experience they may change their mind. Going back in the other direction is much more difficult, however, because judicial experience has now presumably been established. The Supreme Court has only infrequently overruled previous antitrust decisions to apply the per se rule. In *Kimble v. Marvel*, a non-antitrust case analogous to patent misuse, the Court held that *stare decisis* forbade it from overruling the widely criticized rule that license agreements calling

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63 *Cont’l T.V., Inc. v. GTE Sylvania*, Inc., 433 U.S. at 47–48, 60, 71. Justice White’s concurrence found the majority’s brief handling of *Schwinn* an “affront to the principle that considerations of stare decisis are to be given particularly strong weight in the area of statutory construction”).
64 Id. at 47–48 (overruling per se rule against vertical nonprice restraints); *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007) (overruling per se rule against resale price maintenance); *State Oil Co. v. Kahn*, 522 U.S. 3 (1997) (overruling per se rule against maximum resale price maintenance).
for patent royalties after expiration of the patent are unlawful per se.\textsuperscript{65} In the \textit{Jefferson Parish} case Justice O’Connor’s concurring opinion suggested that \textit{stare decisis} precluded the Court from overruling the much criticized per se rule against tying arrangements, even though by that point very little economic support for the rule remained.\textsuperscript{66} Later in \textit{Illinois Tool Works}, it danced around the subject, rejecting a “per se rule” that patents automatically confer market power.\textsuperscript{67} But the general per se rule for tying arrangements when market power is present very likely still survives.

Application of \textit{stare decisis} to questions concerning the scope of the per se rule requires the court to classify the arrangement at hand. For example, tying is (irrationally) unlawful per se while exclusive dealing is subject to the rule of reason. Further, distinguishing between the two practices can be difficult.\textsuperscript{68} This same problem has undermined intelligent analysis of vertical intrabrands. For a thirty year period prior to the Supreme Court’s \textit{Leegin} decision vertical “price” restraints were per se unlawful, while nonprice restraints were subject to a rule of reason. As a result parties threw considerable litigation resources into disputes about whether the arrangement before them was a price or a nonprice agreement.\textsuperscript{69} Subsequent to \textit{Leegin} that distinction has become relatively unimportant.

This entire approach to \textit{stare decisis} and the rule of reason is wrong headed because it attaches far too much precedential value to a formal classification rather than to a mode of analysis.\textsuperscript{70} The rationale for per se illegality is well understood. A properly defined rule of \textit{stare decisis} precludes the Court from overruling a highly criticized decision even though that decision had expressly recognized the existence of a per se rule against tying arrangements of unpatented products where market power was found on the basis of traditional market share measurements. See Elhauge, \textit{supra} note 65, at 42–43.


\textsuperscript{66}\textit{Jefferson Parish Hosp. Dist. No. 2} v. \textit{Hyde}, 466 U.S. 2, 9 (1984) (O’Connor, J., concurring, “It is far too late in the history of our antitrust jurisprudence to question the proposition that certain tying arrangements pose an unacceptable risk of stifling competition and therefore are unreasonable “per se.””). However, the Court then went on to approve the tie because the defendant’s market share was too small. The Jefferson Parish rule still garners a small amount of support. See Einer Elhauge, \textit{Rehabilitating Jefferson Parish: Why Ties Without Substantial Foreclosure Share Should Not Be Per Se Legal}, 80 \textit{ANTITRUST L.J.} 463 (2016).

\textsuperscript{67}\textit{Ill. Tool Works, Inc. v. Indep. Ink, Inc.}, 547 U.S. 28, 40 (2006) (rejecting “presumption of per se illegality of a tying arrangement involving a patented product”). However, the Court also explicitly embraced “the standards applied in \textit{Jefferson Parish}, supra, even though that decision had expressly recognized the existence of a per se rule against tying arrangements of unpatented products where market power was found on the basis of traditional market share measurements. See Elhauge, \textit{supra} note 65, at 42–43.


\textsuperscript{69}See, e.g., \textit{Bus. Elec. Corp. v. Sharp Elec. Corp.}, 485 U.S. 717 (1988) (majority concludes that defendant’s restrictions on price cutting were a nonprice restraint; dissent objects that they were a price restraint). See 8 \textit{AREEDA & HOVENKAMP, supra} note 1, at ¶ 1620–1627 (4th ed. 2017) (noting numerous issues in distinguishing price from nonprice restraints).

\textsuperscript{70}For elaboration, see HERBERT HOVENKAMP, \textit{THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION} 120 (2005), Barak Orbach, \textit{Antitrust Stare Decisis}, 15 Oct ANTITRUST SOURCE 1 (identifying a broad range of issues to which \textit{stare decisis} applies).
decisis should apply the per se rule to “naked” restraints, which are restraints whose profitability
depends on the exercise of market power. By contrast, if the case realistically suggests that
profits might come from reduced costs or product improvement, then the rule of reason is proper.
Selection of the appropriate rule should consider whether a robust literature exists showing that
the challenged practice can be beneficial as well as harmful. For tying arrangements, resale price
maintenance, and exclusive dealing this is clearly true. For horizontal agreements affecting
prices, dividing markets, or excluding rivals the defendants must offer evidence of some form of
integration or legitimate activity that makes a procompetitive theory plausible. If they cannot,
condemnation under the per se rule is appropriate.

For example, at this writing stare decisis might be thought to justify the per se rule for tying
arrangements, as the Supreme Court suggested in its 1984 Jefferson Parish decision.71 The fact
is, however, that tying is not a naked restraint. It is a ubiquitous part of business practice,
serving to protect product or service quality, to reduce production or distribution costs, to meter
usage, or support presumptively output increasing price discrimination.72 Further, it is not
sensibly anticompetitive in the absence of tying product market power. As a result it should be
accorded rule of reason treatment. Attaching the per se rule to a mode of analysis rather than a
category of restraints can help courts avoid unilluminating conclusory analysis, such as
distinguishing between tying and exclusive dealing, or between price and nonprice restraints.
Such a rule would be a much better way to use judicial resources efficiently.

**Burdens of Proof, Quality of Evidence, and the “Quick Look”**

**Cost Savings from the Per Se Rule?**

Antitrust policy should strive to reduce the social costs of anticompetitive behavior, which
has two distinct components. One is the net social costs of anticompetitive price increasing or
output reducing conduct and the private measures taken to defend against it, offset by any
economic benefits. Second are administrative costs, including error costs, of operating the
enforcement system.

One must assume that a full blown rule of reason inquiry is significantly more costly than
analysis under the per se rule. Applying the rule of reason typically requires expert testimony
identifying a relevant market or alternative mechanisms for estimating market power, as well as
some evidence that purports to measure actual anticompetitive effects. By contrast, the per se
rule requires only proof that a particular type of conduct has occurred. The rule of reason is thus
justified only to the extent that it provides superior outcomes.

Administrative costs include not only the costs of litigation, whether terminated by
settlement, dispositive motion, or trial, including appeals, but also the cost of detecting
violations, determining whether to sue, as well as of antitrust compliance with whatever the rule
happens to be. Error costs are particularly relevant to compliance costs. For example, an uduly

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72See 9 AREEDA & HOVENKAMP, supra note 1, at ¶¶ 1703, 1711–1718 (3d ed. 2011) (assessing numerous
procompetitive rationales for tying); Erik N. Hovenkamp & Herbert Hovenkamp, Tying Arrangements
and Antitrust Harm, 52 ARIZ. L. REV. 925 (2010).
harsh tying rule may influence firms to avoid socially beneficial tying. By contrast, an overly lenient predatory pricing rule may yield excessive anticompetitive predation.73

Excessive complexity can increase error costs just as much as excessive simplicity. Antitrust cases in the United States are decided by generalist judges, many of whom lack economics training. Further, facts are often determined by juries, who frequently lack any relevant training whatsoever. In such cases increased complexity can produce poorer rather than better outcomes.74 As a result, a per se rule that is easily administered but right only 80 percent of the time may actually be preferable to an open ended rule of reason query with an arbitrary and indeterminate error rate.

Accuracy is also affected by the care with which the boundaries of the per se rule and rule of reason are defined. For example, the poorly conceived per se rules that the Supreme Court adopted for tying arrangements during the 1950s and 1960s,75 or in joint venture cases such as Topco,76 produced very high error costs, certainly far higher than any savings in administrative costs gained by use of a per se rule. By contrast, a well designed per se rule can produce considerable net cost savings even if it is not absolutely perfect. The most prominent example is the per se rule against naked price fixing, which finds illegality simply on evidence that the defendants fixed their prices.

Historically, some per se rules have been so far from perfect that they simultaneously imposed large administrative costs, all the while making markets no more competitive. This occurs when the decision to apply the per se rule was wrong to begin with, yielding significant resistance. Such per se rules gradually become subject to many exceptions, and litigating them can be as costly as litigating under the basic rule of reason.

A case in point is resale price maintenance, or manufacturer specification of the price that a dealer must charge. The Supreme Court adopted a poorly articulated per se rule against it in 1911.77 Eight years later, however, its Colgate decision announced that only “agreements” to impose RPM were unlawful, and a firm that simply refused to deal with price cutters was acting unilaterally.78 That decision produced a ninety-year long litigation nightmare in which the parties devoted many costly efforts to determining whether resale price had been imposed unilaterally or by agreement, rather than whether the pricing practice at issue was really anticompetitive.79 Included in this debate were heavily litigated issues concerning whether the dealer in question was actually a reseller or merely an “agent” whose prices could lawfully be

73On the case for underdeterrent predatory pricing rules, see 3A AREEDA & HOVENKAMP, supra note 1, at ¶723b (4th ed. 2013).
75See discussion infra, text at notes 83, 197.
76United States v. Topco Assocs., Inc., 405 U.S. 596, 607–08 (1972) (condemning competitively harmless joint venture market division agreement under the per se rule).
controlled. In all but a few cases the agency issue had no impact on the competitive effects of the resale price maintenance being challenged. Later, after the Supreme Court had clarified that vertical nonprice restraints should be subject to the rule of reason, a similar battle ensued over whether a particular instance of dealer termination amounted to a “price” restraint (unlawful per se) or a “nonprice” restraint (rule of reason). For example, a dealer who refused to invest in a showroom or trained sales personnel might be able to charge a lower price for the manufacturer’s product. If the manufacturer terminates this dealer, is it for a “nonprice” reason (inadequate showroom and sales staff) or a “price” reason (charging low prices). In retrospect it is hardly clear that a century of per se treatment of resale price maintenance saved significant litigation resources at all, and absolutely no reason for thinking that it led to better outcomes.

Something similar happened with the law of tying arrangements, which were irrationally placed under a per se rule even as the closely related offense of exclusive dealing was analyzed under the rule of reason. The principal difference between tying and exclusive dealing is that tying requires the forced union of “separate products,” so a vast amount of litigation resources were devoted to this question. To be sure, there are some operational differences between tying and exclusive dealing, but the separate products query rarely does anything to illuminate them. Further, notwithstanding the nominally harsher treatment of tying arrangements, exclusive dealing can in fact have more severe consequences for competition. A tying arrangement attaches exclusivity to a particular product while exclusive dealing typically applies to the entire dealership. For example, a tying requirement might force a seller of Lexmark computer printers to stock and sell Lexmark cartridges, but it would still be able to sell non-Lexmark printers and cartridges as well. By contrast, exclusive dealing could prevent the dealer from selling any non-Lexmark products at all. In that case the exclusionary power of the exclusive dealing is greater than that imposed by tying.

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80 E.g., United States v. Gen. Elect. Co., 272 U.S. 476 (1926) (finding consignment (agency) exception to RPM rule); Simpson v. Union Oil Co. of Cal., 377 U.S. 13 (1964) (refusing to find consignment exception). On the consent or agency exception to RPM rules, see 7 AREEDA & HOVENKAMP, supra note 1, at ¶¶1470–1474.
81 One exception is Ill. Corp. Travel v. Am. Airlines, Inc., 806 F.2d 722 (7th Cir. 1986) (economic reasons why airline travel agent is a mere agent whose prices can be set by the airlines, and not a buyer-reseller of tickets).
86See 10 AREEDA & HOVENKAMP, supra note 1, at ¶¶1741–1751 (3d ed. 2011) (devoting 120 pages to the separate products issue).
87Although a few tying cases try to make the tying product the business itself, at least in the context of franchising. See, e.g., Siegel v. Chicken Delight, 448 F.2d 43, 51–52 (9th Cir. 1971), cert. denied, 405 U.S. 955 (1972) (trademarked business and supplies as separate products); Midwestern Waffles v. Waffle House, 734 F.2d 705, 712 (11th Cir. 1984) (similar); Krehl v. Baskin-Robbins Ice Cream Co., 664 F.2d 1348 (9th Cir. 1982) (rejecting argument that trademark and ice cream were separate products).
88See Roy B. Taylor Sales v. Hollymatic Corp., 28 F.3d 1379 (5th Cir. 1994) (dealer required to carry defendant’s hamburger patty paper as a condition of carrying its patty making machine, but customers
Most of these problems could be addressed by our proposal that the per se rule be defined in terms of a mode of analysis rather as a classification of practices. For example, once the rule of reason is applied to both exclusive dealing and tying, the analysis of these practices would be very similar, with the courts searching principally for unreasonably exclusionary conduct.

The Assignment of Evidentiary Burdens

Of all the procedural issues involved in antitrust litigation under the rule of reason, none are more critical than questions about assignment of the burden of proof and production, and the quality of the evidence that must be presented at each stage. The requirements for a rule of reason case -- market power and anticompetitive effects -- can be very difficult to prove. Assignment of the burden is frequently dispositive of the outcome. Indeed, very likely the principal reason that plaintiffs go to such lengths to bring their case within the boundaries of the per se rule or the so-called “quick look” is that they cannot carry an evidentiary burden requiring them to demonstrate power and anticompetitive effects. For example, in the California Dental case the Federal Trade Commission lost in its efforts to have the Court examine the claim under a “quick look” approach. That having failed, the FTC was later unable to make a case under the Supreme Court’s formulation for assessing proof burdens under the rule of reason.

The black letter antitrust rule for proof under the rule of reason is easily stated. The plaintiff has the primary burden of alleging and then providing sufficient evidence both that the defendants have sufficient market power to make an anticompetitive restraint plausible, and also that they have imposed at least one such restraint. Some decisions unfortunately express these requirements in the alternative, suggesting that the plaintiff can prevail by showing either that a restraint is anticompetitive or that the defendant has sufficient market power to pull it off.
While market power is a necessary condition for an anticompetitive restraint under the rule of reason, it is never a sufficient condition. Joint ventures with significant market power may employ restraints that are in fact quite competitive, and thus are “reasonable” under the circumstances. Thus the better rule is the one expressed in the Tops Markets decision:

Even assuming this market share data implies that Quality [the defendant] possessed market power, Tops still would fail to satisfy its burden under the adverse-effect requirement. Market power, while necessary to show adverse effect indirectly, alone is insufficient. A plaintiff seeking to use market power as a proxy for adverse effect must show market power, plus some other ground for believing that the challenged behavior could harm competition in the market...95

If the plaintiff meets this initial burden to establish a prima facie of competitive harm,96 then the burden shifts to the defendant to show a procompetitive justification for the practice.97 If the defendant is unable to defeat the prima facie case and offers no justification, then the plaintiff is entitled to prevail. By contrast, if the defendant does provide evidence of a procompetitive justification the burden may shift a second time.98 The plaintiff will still have an opportunity to

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Even if market power were shown, it would not satisfy the adverse-effect requirement under these circumstances . . . . [A] plaintiff wishing to show adverse effect through indirect means “must at least establish that defendants possess the requisite market power . . . .” [A] showing of market power, while necessary to show adverse effect indirectly, is not sufficient. There must be other grounds to believe that the defendant's behavior will harm competition market-wide, such as the inherent anticompetitive nature of defendant's behavior or the structure of the interbrand market . . . . This position is consistent with the approach of courts that require a showing of market power, but only as one of several steps necessary to establish adverse effect.

96For example, in Cal. Dental the burden never shifted because the majority concluded that the FTC failed to make out a prima facie case. Cal. Dental, 526 U.S. at 775 n. 12. The four dissenters disagreed with this proposition. Id. at 783.


98On the broad acceptance of these burden shifting requirements in rule of reason antitrust cases, see Michael A. Carrier, The Real Rule of Reason: Bridging the Disconnect, 1999 B.Y.U. L. Rev. 1265 (1999)
show that the same justification could have been achieved by a less restrictive alternative, which is one that offers more-or-less the same benefits but without the threat of competitive harm. If no less restrictive alternative is available the court may need to examine both the restraint and the justification and attempt to “balance” them in order to assess net anti-competitive effects.

One important question is whether these “secondary” burdens of proof should be assigned categorically or on a case by case basis. The latter makes more sense given the variability of antitrust rule of reason claims and location of evidence. As a general matter, inferences should be assigned against the person with the least plausible claim. This suggests both that proof burdens should be assigned to a party as its position is less tenable, and also that the “quality” of the proof be increased.

Intertwined with the issue of proof burdens is the question of the quality and amount of evidence that is needed to satisfy a party’s burden. Once again, the less plausible a party’s case the more evidence is needed to create a triable issue. At least for summary judgment purposes, the Supreme Court made this clear in its Matsushita decision, which created an inverse sliding scale between the plausibility of the plaintiff’s allegations and the degree of proof necessary to avoid summary judgment. The defendants, who were Japanese manufacturers of electronic sound equipment, were accused of orchestrating a twenty-year long predatory pricing campaign in order to drive American manufacturers out of business. The accusations were in effect of a predation scheme that had virtually no chance of success. First, a twenty year campaign would have required decades of monopoly prices before the defendants could have recouped their investment in predation. Second, the plaintiffs had offered no evidence


American Express, 838 F.3d at 195 (“If the defendant can provide such proof, then ‘the burden shifts back to the plaintiff[,] to prove that any legitimate competitive benefits offered by defendant[,] could have been achieved through less restrictive means,’” citing Capital Imaging Assocs., P.C. v. Mohawk Valley Med. Assocs., Inc., 996 F.2d 537, 543 (2d Cir. 1993)). See C. Scott Hemphill, Less Restrictive Alternatives in Antitrust Law, 116 COLUM. L. REV. 927 (2016).


See Abraham L. Wickelgren, supra note 73, at 53 (“we require stronger evidence of anticompetitive effects for conduct that we think are less likely to be anticompetitive and are more receptive to procompetitive effects arguments in such cases”).


Id. at 593 (“petitioners would most likely have to sustain their cartel for years simply to break even”). See also Frank H. Easterbrook, The Limits of Antitrust, 63 Tex. L. REV. 1, 26–27 (1984) (recoupment period on the Matsushita facts would have to be infinitely long). For a strongly contrary view, see Christopher R. Leslie, Predatory Pricing and Recoupment, 113 Colum. L. Rev. 1695, 1719 (2013). Leslie observes that Matsushita was a §1 conspiracy case; further, even a long predation period might lead to profitable recoupment if the monopoly returns during the recoupment period are sufficiently high. On the recoupment requirement in predatory pricing law, see 3A AREEDA & HOVENKAMP, supra note 1, at ¶¶726–728 (4th ed. 2015).
indicating that entry into this market was difficult, “yet without barriers to entry it would presumably be impossible to maintain supracompetitive prices for an extended time.”\textsuperscript{105} Such an implausible claim would require a greater amount of evidence in order to avoid summary judgment:

… if the factual context renders respondents’ claim implausible—if the claim is one that simply makes no economic sense—respondents must come forward with more persuasive evidence to support their claim than would otherwise be necessary.\textsuperscript{106}

The quality of the evidence can also affect the burden of proof. For example, once a plaintiff has established a relevant market with a sufficient minimum share, who has the burden of showing that entry is difficult or easy? If entry is easy, then even a high market share fails to establish significant power.\textsuperscript{107} The same thing applies to the question whether two different goods are sufficiently substitutable that they should be in the same market.\textsuperscript{108}

\textsuperscript{105}Matsushita, 475 U.S. at 591–92 n. 15.
\textsuperscript{106}Id. at 588. See also First Nat’l. Bank of Ariz. v. Cities Serv. Co., 391 U.S. 253, 278–79 (1968) (where defendant had no motive to conspire stronger evidence would be required to establish a conspiracy). As Judge Posner later explained:

More evidence is required the less plausible the charge of collusive conduct. In Matsushita, for example, the charge was that the defendants had conspired to lower prices below cost in order to drive out competitors, and then to raise prices to monopoly levels. This was implausible for a variety of reasons, such as that it would mean that losses would be incurred in the near term in exchange for the speculative possibility of more than making them up in the uncertain and perhaps remote future — when, moreover, the competitors might come right back into the market as soon as (or shortly after) prices rose above cost, thus thwarting the conspirators’ effort at recouping their losses with a commensurate profit. But the charge in this case involves no implausibility. The charge is of a garden-variety price-fixing conspiracy orchestrated by a firm, ADM, conceded to have fixed prices on related products (lysine and citric acid) during a period overlapping the period of the alleged conspiracy to fix the prices of HFCS.

\textit{In re} High Fructose Corn Syrup Antitrust Litig. (HFCS), 295 F.3d 651, 661 (7th Cir. 2002), cert. denied, 537 U.S. 1188 (2003). See also Instructional Sys. Dev. Corp. v. Aetna Cas. & Sur. Co., 817 F.2d 639, 646 (10th Cir. 1987) (Matsushita holding was based on twin premises of an alleged conspiracy that was fundamentally irrational and ambiguous circumstantial evidence; as the rationality of the alleged conspiracy increases, the evidentiary burden is lessened). In \textit{H.J.}, the Eighth Circuit went even further, suggesting that Matsushita “does not apply” in a case where the alleged conspiracy seems quite rational. \textit{H.J.}, Inc. v. Int’l Tel. & Tel. Corp., 867 F.2d 1531, 1544 n.10 (8th Cir. 1989) (“There is no claim in this case that the supposed conspiracy makes no economic sense. \textit{Matsushita Electric} does not apply.”).

Other decisions making the same distinction include Petruzz’s IGA Supermarkets, Inc. v. Darling-Delaware Co., Inc., 998 F.2d 1224, 1233 (3d Cir.), cert. denied, 510 U.S. 994 (1993); Ezzo’s Invs., Inc. v. Royal Beauty Supply, Inc., 94 F.3d 1032, 1036 (6th Cir. 1996).

\textsuperscript{107}See 2 AREEDA & HOVENKAMP, supra note 1, at ¶420b (4th ed. 2014); see also United States v. Baker Hughes, Inc., 908 F.2d 981, 983–87 (D.C. Cir. 1990) (rejecting government’s contention that once high market concentration was established in a merger case, the burden shifted to the defendant to show that entry would be “quick and effective” in restoring any monopoly prices to the competitive level).

\textsuperscript{108}HDC Medical, Inc. v. Minntech Corp., 474 F.3d 543 (8th Cir. 2007) (plaintiff had burden to show whether single-use and multiple-use dialyzers were substitutable); FTC v. Arch Coal, Inc., 329 F. Supp. 2d 109, 121 (D.D.C. 2004) (plaintiff had burden to show whether hotter burning and cooler burning coal were in the same market).
Staging Evidentiary Obligations

The Plaintiff’s Prima Facie Case

The plaintiff’s prima facie case is only the first step in assessing a restraint challenged under the antitrust laws. Too many courts proceed as if it constitutes the entire case. In fact, the prima facie case should focus on one question: does the restraint before the court require an explanation, or should the complaint be dismissed without further query? As a general matter the evidence supporting a prima facie case need not be as specific as the evidence supporting a procompetitive justification. If the defendants have a procompetitive justification it must have been a motivating factor for the restraint. They should be able to establish it in most cases rather easily. By contrast, most of the evidence pertaining to the prima facie case concerns the market in which the firms operate and the more obvious tendencies of the restraint at issue, and sometimes much of the evidence is controlled by the defendant.

Thus the quality and amount of the evidence varies at different stages in the production of evidence:

First, the evidence of market power should be sufficiently strong to create an inference that the defendants are capable of producing anticompetitive results by means of the claimed restraint. This entails that the market be well defined or that an alternative method of assessing power be sufficiently robust. In most cases evidence about market structure, entry barriers, or the extent and nature of IP rights is sufficiently available to plaintiffs to enable them to make out a prima facie case. Of course, many details may be more fully known by the defendant firms themselves. In any event, if an important element in assessing power is known exclusively by a defendant, the presumption on that issue should favor the plaintiff.

One reason for requiring strong proof of power is that as power is weaker efficiency explanations tend to predominate. For example, if a group of firms have no power at all, then an anticompetitive output reduction cannot be an explanation for their conduct. The presence of power is what makes an anticompetitive restraint possible.

Second, once sufficient market power is found, a practice that can be reasonably expected to restrain output or increase price should be sufficient to shift the burden to the defendant, without evidence of an actual output restraint or price increase. The question at this stage is only whether power and a sufficiently troublesome restraint exists that the defendants should be expected to provide an explanation. Under the consumer welfare test advocated here, the focus of this proof is on the price or output effects of the restraint, not on some broader conception of general welfare.

The Supreme Court majority in the California Dental case thought otherwise. It found an insufficient prima facie case for competitor-created restraints on advertising that made it virtually impossible for member dentists to advertise their prices, and prohibited quality

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109 On the question of varying the power requirement with the offense, see discussion infra, text at notes 292–300; and Louis Kaplow, On the Relevance of Market Power, 130 Harv. L. Rev. (forthcoming, 2017).

110 See discussion infra, text at notes 144–86.

advertising. Evidence of such practices should require an explanation concerning why such restrictions benefitted rather than harmed consumers. Perhaps more to the point, what additional facts should the FTC have been required to show? Measuring actual output effects would be impossible, and in this case the plausibility argument would clearly seem to favor the plaintiff. By contrast, the defendants, who created the restraints in question, need do no more than provide an explanation that they presumably already knew for why these particular restraints protected rather than harmed consumers, and why these means were superior to other vehicles that would have interfered less with the competitive process. For example, if the purpose of the restraints was to prevent deception, was there a significant record of deception that federal or state consumer protection laws were unable to control?

The majority’s error in California Dental is that it rolled both the prima facie case and the justifications offered for it into one, giving the plaintiff the burden on both. The Supreme Court acknowledged the fragility of the market in question, focusing on imbalances in information as between suppliers and consumers that impeded effective consumer choice. In a quite stunning logical flip, however, it then concluded that a set of rules facilitating collusion among dentists might in fact be an effective way to control the situation. It reasoned that the challenged advertising restrictions “might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition.” That is, the same imbalances of information that made this market more conducive to collusion might serve to justify a set of restraints imposed collusively by sellers.

In part, the Court’s decision may have reflected naivete about professionals – perhaps that they can be expected to act in the public interest rather than as self-serving business persons. The history of professional restraints suggests strongly that professionals are maximizers just as much as other business firms. When they have an opportunity to profit by limiting output or controlling price, they take it. In any event, the question whether a particular professional rule reflects the public interest or self-interested maximization is appropriately a fact to be proved as part of a defense, not simply assumed. For that, the burden should be on the defendants.

Agreements by professional associations with power that virtually eliminate price advertising or

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114CDA, 526 U.S. at 773.

that condemn quality advertising require an explanation. In this case, power, self-interested decision makers, and price-affecting conduct should be sufficient to create an inference.

The approach that the Supreme Court took in the NCAA case is more sensible. The Court found a prima facie anticompetitive restraint in a rule that limited each team’s annual number of nationally televised games. As the court observed, “[b]ecause it restrains price and output, the NCAA’s television plan has a significant potential for anticompetitive effects.” In the presence of market power, that is certainly so. As a result, the NCAA was obliged to provide a defense.

If the challenge is to conduct thought to be exclusionary rather than collusive, a rule of reason plaintiff should be required to show that at least one substantial and presumptively efficient rival or potential rival has been excluded. For example, in SCFC the Tenth Circuit found that the plaintiffs, which issued the competing Discover card, made out a prima facie case of exclusionary practice with respect to Visa’s rule forbidding Visa membership to any bank that also issued a competing card. To be sure, there might be justifications for such a rule, but the important point at this stage is that they are justifications – that is, they serve as explanations for an exclusionary practice, not as an element of the practice itself.

Justifications

Once the plaintiff has made out a prima facie case of competitive harm, the burden shifts to the defendants to provide evidence of a justification. This burden should be stricter than the one applied to the plaintiff’s prima facie case. Restraints are adopted self-consciously, and we must assume that the defendants are rational and knew what they were doing when the challenged restraints were created. To the extent that the defendants’ expectation of profit came from something other than a restriction of competition, they should have evidence and are in the best position to provide it.

Acceptance of justifications presents issues of both proof and policy. Not every proffered justification will save a restraint, even if the justification has factual support. For example, in NCAA the defendants offered the rationales that restrictions on the number of broadcasts per team were necessary in order to level the playing field as between more popular and less popular teams; further, they were needed to protect live ticket-paying attendance, which eroded when televised alternatives were available. The Court properly rejected these, not because the defendant failed to meet its burden to prove them, but rather on policy grounds. As a general matter it is not a defense to collusion that its purpose is to protect weaker participants. Every cartel does that by creating a price umbrella that permits less efficient firms to survive. As to live attendance, a high cartel price always serves to strengthen demand for non-cartelized substitutes. We rely on the market to make these adjustments. For example, an automobile cartel might result in increased demand for pickup trucks, but that fact is not a defense to price fixing.

The most salient point about both of the NCAA’s defenses is that they assumed that the challenged restraint really did reduce output or raise price in the affected market. Only an output limitation could create broadcasting space so that less popular teams could have their games

nationally televised, or force viewers to switch from television to live attendance. An effective defense must be able to show that a practice has social benefits that do not depend on the exercise of market power.  

For challenges to horizontal restraints, the need to control free riding is an often asserted but greatly overused defense. True free riding requires one firm to take advantage of another firm’s investment in ways that reduce the incentive to invest. As a result, where competitively harmful free riding occurs one would expect output to be lower as a result. Further, in order for anticompetitive free riding to occur the free rider must be able to take advantage of someone else’s investment in such a way that the other firm is not capable of pricing it out in the market. This inability to obtain an adequate return reduces the incentive to invest.

Often instances of claimed free riding are really complaints about competition, particularly when there are joint costs. For example, in SCFC the plaintiff made out a prima facie case of competitive harm from a Visa rule that forbade banks issuing Visa cards from issuing competing cards. At that point the burden shifted to the defendant to provide a justification, and the court accepted its defense that permitting competing cards would encourage free riding. But the court never required evidence of actual free riding, explained how it would occur, what were the assets upon which a free ride might be taken, or why Visa could not have taken reasonable steps either to prevent or charge a fee for their use. If there are joint costs, 

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119 Cf. Nat’l Soc. of Prof’l Eng’rs v. United States, 435 U.S. 679, 688, 696 (1978): The Rule [of Reason] does not open the field of antitrust inquiry to any argument in favor of a challenged restraint that may fall within the realm of reason. Instead, it focuses directly on the challenged restraint’s impact on competitive conditions . . . . In sum, the Rule of Reason does not support a defense based on the assumption that competition itself is unreasonable.

120 For vertical restraints the manufacturer, or vertically related firm, has a separate interest that serves to justify many free rider concerns. See, e.g., H.L. Hayden Co. of New York, Inc. v. Siemens Med. Sys., Inc., 879 F.2d 1003 (2d Cir. 1989). If the manufacturer does not have those concerns the free rider argument is best rejected. See, e.g., Toys “R” Us, Inc. v. FTC, 221 F.3d 928 (7th Cir. 2000) (rejecting defendant’s free rider explanation when it was a retailer complaining about free riding by other dealers, but the manufacturers did not have the same view).

121 See, e.g., Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210 (D.C. Cir. 1986) (accepting free rider justification for national van lines requirement that local mover affiliates transfer their interstate shipments exclusively to Atlas’ authority for operation under its name and agreement to its rates); Polk Bros., Inc. v. Forest City Enterp., Inc., 776 F.2d 185 (7th Cir. 1985) (accepting free rider argument for horizontal product division agreement within a single shopping center; necessary to permit each firm to capitalize on its own promotion). See Wesley J. Liebeler, Antitrust Law and the New Federal Trade Commission, 12 Sw. U. L. REV. 166 (1981) (free rider defenses to ancillary product division agreements).

122 See Chicago Prof’l Sports Ltd. P’ship v. NBA, 961 F.2d 667, 675 (7th Cir. 1992) (if an asset can be priced out, then the ride is not free).

123 SCFC ILC, Inc. v. Visa USA, Inc., 36 F.3d 958, 961 (10th Cir. 1994) (The challenged bylaw provided “if permitted by applicable law, the corporation shall not accept for membership any applicant which is issuing, directly or indirectly, Discover cards or American Express cards, or any other cards deemed competitive by the Board of Directors.”).

the venture can usually require cost sharing rather than deny access altogether. For example, it may be that a merchant who takes one credit card receives card swiping machines for that card. If the merchant then took a competitor’s card that made uncompensated use of the same machine, we would have the possibility free riding. But free riding would not be a problem if the second card issuer could be compelled to share the costs of the machine, or if the machine’s costs were borne by the merchant. In a later challenge to the same rule brought by the United States, the court could not identify any Visa asset upon which the competing card issuers (Discover and American Express) were able to take a free ride.125

In other cases claimed “free riding” is nothing more than product complementarity. For example, producers of gasoline sell more of it to the extent that we have a robust market for automobiles, and vice versa. One might describe this as “free riding” because the gasoline producers are earning a profit from the automobile manufacturers’ investment. But the overall effect is to increase rather than decrease overall output, thus making this form of free riding a good thing.126 While product complementarity enables one firm to profit from another firm’s investment, the effect is generally to increase rather than decrease the incentive to invest.

In any event, complete market exclusion is a suspiciously excessive remedy for claimed free riding, even where a certain amount of free riding actually occurs. For example, one Second Circuit decision accepted a free rider argument for a professional baseball league’s consolidation of all intellectual property rights held by member teams into a single organization with exclusive rights to license. The court accepted the “free rider” argument that the value of an individual team’s IP rights was in part a function of the IP rights held by other teams as well. For example, “a Club that was popular because of its on-field success could cash in on its popularity even though its victories obviously could not have been achieved without the participation of other clubs.”127 Factually that is true, but it is tantamount to saying that the value of a winner’s enhanced intellectual property rights must be shared with losers. The output maximizing approach would permit each team to capitalize on its own efforts, without having to share its successes.

On the other hand, free riding is a legitimate concern for joint ventures that involve a high degree of risk at the startup stage. Firms will have an incentive to wait until risks have been

125United States v. Visa USA, Inc., 163 F. Supp. 2d 322 (S.D.N.Y. 2001), modified, 183 F. Supp. 2d 613 (S.D.N.Y. 2001), aff’d, 344 F.3d 229 (2nd Cir. 2003), cert. denied, 543 U.S. 811 (2004). See also United States v. Am. Exp. Co., 88 F. Supp. 3d 143 (E.D.N.Y. 2015) (“anti-steering” rules used by card issuer to deter merchants from accepting rivals’ cards not necessary to limit free riding because record showed that defendant could and did price assets subject to free riding separately), rev’d on other grounds, 838 F.3d 7198 (2d Cir. 2016). Cf. Toys “R” Us, Inc. v. FTC, 221 F.3d 928, 938–39 (7th Cir. 2000) (rejecting Toys “R” Us’ free rider argument that distribution restraints needed to be imposed on rival retailers in order to prevent them from taking advantage of Toy “R” Us’ promotional investments when the manufacturers themselves believed that widespread distribution was the output maximizing strategy; it’s interest was not in more efficient distribution but rather in maximizing its own profits).

126See, e.g., Wilk v. AMA, 895 F.2d 352, 364 & n.2 (7th Cir. 1990) (rejecting free rider argument in defense of ruling prohibiting physicians from referring patients to chiropractors).

127MLB Properties, Inc. v. Salvino, Inc., 542 F.3d 290, 305 (2d Cir. 2008). See also Laumann v. NHL, 56 F. Supp. 3d 280, 298 (S.D.N.Y. 2014) (rejecting free rider defense of inter-team territorial restrictions on TV licensing; proffered defense was that individual teams would be able to take a free ride on the popularity of the league if they were able to license their games nationally).
overcome and then join later rather than earlier. But if the antitrust laws guarantee a right of late entry, each firm will have an incentive to free ride on the risk capital of early participants.

Other types of justifications are both more conventional and more robust, provided that they can be factually supported. For example, joint ventures are often justified by reductions in either production and distribution costs or else market transaction costs. In such cases, however, the costs in question are those borne by the defendants and must have been a motivating factor in creating the joint arrangement in the first place. To that extent the defendant should have the burden of justifying them with probative evidence.

While the defendant has the burden of proving a justification for its restraint, at this stage it should not need to show that the effect of the justification is to offset fully the concerns that led the restraint to be challenged. The entire logic of rule of reason proof is to put off and minimize the occasions for weighting and balancing pro- and anticompetitive effects. To be sure, some proffered justifications may be so strong or so weak that they make further inquiry unnecessary, but that will hardly be true in every case.

Less Restrictive Alternatives

Once the defendant has established a justification, the plaintiff can still show that similar effects could have been achieved by a less restrictive alternative, with that burden ordinarily on the plaintiff. Consistent with the consumer welfare principle, an alternative should be considered less restrictive if it accomplishes most of the defendants’ legitimate goals while also providing lower prices, higher quality, or significantly less exclusion of competition.

The most difficult questions respecting less restrictive alternatives have to do with robustness and quality. On the first, may merely hypothetical less restrictive alternatives be offered, or must the plaintiff show that such an alternative is really being used successfully in some other setting? Second, must the proffered alternative be just as effective as the restraint that the defendants have chosen, or is a somewhat less effective alternative acceptable?

One of the most robust less restrictive alternatives is non-exclusive agreements in lieu of the defendants’ actual exclusive ones. This is particularly true in the case of horizontal arrangements involving IP rights, such as blanket licenses or patent pools. A non-exclusive license generally gives a firm all that it needs to improve its own technology. It needs an exclusive right only to exclude outside practitioners of the IP right in question. The absence of exclusive rights is particularly important in cases involving large numbers of participants. For

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128 See, e.g., United States v. Brown Univ., 5 F.3d 658 (3d Cir. 1993) (on remand, government would have burden of proving that less restrictive alternatives existed to the defendants’ agreement limiting competition in the offering of financial aid to needy students who had been admitted to more than one of the competing institutions).
130 See, e.g., Justice Powell’s dissent in Arizona v. Maricopa Cty. Med. Soc’y, 457 U.S. 332, 360 (1982) (protesting that a large group could not effectively reduce output, given that the arrangement was nonexclusive).
131 E.g., Broad. Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 4 (1979) (observing that the licenses in question were nonexclusive). See Hemphill, supra note 98, at 952.
example, in both *Broadcast Music*¹³² and *Maricopa*¹³³ the defendants numbered in the thousands. In that case giving each cartel member an unlimited right to make non-cartel sales would make price fixing highly unlikely or even unthinkable.

To be sure, exclusivity cannot be dispositive in either direction. Exclusivity may be necessary to avoid free rider problems when the defendants are engaged in a production joint venture or joint innovation. For example, two firms engaging in joint research and development may legitimately seek to preserve their improvements to themselves, thus requiring exclusive licensing.

By contrast, firms pooling the results of their independent research or individually developed IP rights raise different concerns. They clearly have a right to improve their own technology, but exclusion of others can raise significant fears. In *Broadcast Music*, nonexclusivity was important to the result because the copyrighted music in question was independently developed and subsequently licensed by rights holders who were not engaged in any joint productive activity other than the blanket license agreement itself.¹³⁴ In that case nonexclusivity may be necessary to address concerns about collusion, particularly when the venturers as a group have significant power. By contrast, for joint research that is contemplated but not completed, the right to preserve the results to the members is very likely essential to the creation of proper incentives.

In the *Appalachian Coals* case the Supreme Court approved without economic discussion an arrangement in which 134 Appalachian region coal producers designated a single agent to represent them as sales broker.¹³⁵ The designated agent was exclusive for all of the coal that the participating members produced.¹³⁶ There was some doubt about whether the association had much market power.¹³⁷ If it did, however, then a query into less restrictive alternatives should have been necessary. The defendants had grouped themselves together to sell their coal collectively at a single price, which was certainly enough for a prima facie case of collusion threatening conduct. The obvious defense was that a single sales agent could reduce transaction costs. At that point, however, the court should have inquired whether a nonexclusive arrangement could have received substantially the same results, but without permitting output limitations that threatened competition. Free riding might be a problem, but that would be a question of fact to be proven. The defendants’ membership was too large to make a traditional cartel workable. However, an exclusive joint sales agency would create a single price setter and surreptitious non-agency sales could be readily detected. In that case, exclusivity was the factor that might have made collusion possible.

¹³² *Broadcast Music*, 441 U.S. at 5 (BMI contained 20,000 authors and composers, ASCAP contained 22,000).
¹³³ See *Maricopa*, 457 U.S. at 339 (defendants’ association contained 1750 physicians, representing roughly 70% of physicians in the county).
¹³⁵ Appalachian Coals v. United States, 288 U.S. 344 (1933).
¹³⁶ *Id.* at 357–58.
¹³⁷ See *id.* at 357 (defendant’s market share was 74.4%, which was certainly enough, but only 11.96% of a somewhat larger geographic region).
When the proffered defense is free riding, then courts should first ensure that claimed free riding is what the defendants say it is.\(^{138}\) Even if it is, however, less restrictive alternatives may be available. Free rider claims can be difficult to assess because free riding may increase output in the short run while decreasing it in the longer run. This difference is most pronounced in the case of vertical restraints. For example, the price cutting dealer who lacks a showroom offers customers lower prices today, but it also reduces the incentive that full service dealers have to make optimal investments in their business. The manufacturer in this case ordinarily has the correct set of incentives, which are aligned with “optimal” distribution rather than lowest prices in the short run.\(^{139}\) When the relevant participants are competitors rather than vertically related firms, then free rider claims become more difficult to assess because the same practices that purportedly solve free rider problems can also serve to blunt competition.

For many situations, workable less restrictive alternatives falling short of market exclusion should be available to address free rider claims. The most obvious one is mechanisms for pricing out any asset upon which a free ride is claimed.\(^{140}\) In other cases, provision of information might be more effective than coercive enforcement by market exclusion.\(^{141}\)

In other situations, such as anticompetitive tying, quality specifications might be a less restrictive alternative.\(^{142}\) Here, however, one must ensure that the alternative actually addresses the particular defenses that have been offered. Considering quality specification as a less restrictive alternative makes sense if quality control is the claimed justification for a tie. But specifying quality can be used for other purposes, however, for which the quality control defense is inapt. For example, in Siegel a non-dominant franchisor required its franchisees to purchase certain consumable supplies from itself rather than simply specifying their quality and permitting the franchisees to purchase them elsewhere.\(^{143}\) The court also acknowledged, however, that the tie

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140 See discussion supra, text at notes 120–121. But see Barry v. Blue Cross of Cal., 805 F.2d 855 (9th Cir. 1986) (reimbursing non-network physicians at the same rate as network physicians not a viable less restrictive alternative because under it no physicians would have an incentive to join the network).
141 Wilk v. AMA, 895 F.2d 352, 356, 363, 364 & n. 2 (7th Cir. 1990) (“education” would be less restrictive than absolute exclusion of chiropractic); Kreuzer v. Am. Acad. Of Periodontology, 735 F.2d 1479 (D.C. Cir. 1984) (requiring minimum number of hours of practice would be less restrictive alternative to rule that limited periodontics practice to those who practiced periodontics exclusively).
142 See, e.g., Jefferson Par. Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 26 & n. 42 (1984) (acknowledging quality specification as an occasional alternative to tying); Siegel v. Chicken Delight, Inc., 448 F.2d 43, 51 (9th Cir. 1971) (specification of quality of tied product would be less restrictive alternative than mandating that buyers purchase it from the defendant); Mozart Co. v. Mercedes-Benz of North Am., Inc., 833 F.2d 1342 (9th Cir. 1987) (similar). See also Hemphill, supra note 98 at 941–42.; 9 & 10 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW §§1716d, 1717d, 1760d, e (3d ed. 2010) (discussing quality or source specifications as less restrictive alternatives in tying cases).
143 Siegel, 448 F.2d at 49 (The court addressed the market power requirement by concluding that ownership of a trademark conferred sufficient power. That portion of the decision was effectively overruled by Ill. Tool Works, Inc. v. Indep. Ink, 547 U.S. 28 (2006)). See Rick-Mik Ent’p, Inc. v. Equilon Ent’p, LLC, 532 F.3d 963, 971–72 (9th Cir. 2008) (recognizing that Ill. Tool Works effectively overruled Siegel).
was being used as a metering device for measuring the franchisee’s sales.\textsuperscript{144} To that extent, quality specifications would not be a satisfactory less restrictive alternative. At the same time, of course, it suggested that the tie was not anticompetitive to begin with, particularly in light of the defendant’s small market share.

Identifying Anticompetitive Restraints: Administrability and Consumer Welfare

In rule of reason analysis, the point of using a sequence of prima facie case, offsetting justifications, and less restrictive alternatives is to assess whether the challenged restraint reduces output or increases price from the non-restraint level. This approach is consistent with antitrust’s consumer welfare principle, which identifies antitrust’s goal in terms of consumer welfare, which is generated by low prices and high output, whether measured by quantity or quality. It is not necessarily consistent, however, with a general welfare principle, under which a restraint that actually produces higher prices or lower output is permissible, provided that efficiency gains to producers are at least as large as consumer losses.

This is not the place to debate whether consumer welfare or general welfare ought to be the goal of the antitrust laws.\textsuperscript{145} Suffice it to say that, whatever its ultimate value, the consumer welfare approach has one enormous advantage over a general welfare principle -- administrability. In order to assess a restraint under the consumer welfare principle one need query only whether prices are higher (or output lower) as a result of the restraint. This is far easier than quantifying all consumer losses and producer gains, and netting them out against each other.

Netting out consumer and producer welfare changes requires information about the shape of the demand curve as well as the defendants’ costs and a prediction of how the challenged restraint will change those figures.\textsuperscript{146} Measuring consumer harm under a general welfare test requires not only predicting whether the price will rise or fall, but also what will be the size of the “deadweight” loss cause by inefficient consumer substitutions. There are almost no cases that have ever attempted to assess general welfare in reasonably close situations,\textsuperscript{147} and very likely no

\textsuperscript{144}See Siegel, 448 F.2d at 46 (noting that the defendant tied the supplies in lieu of charging a variable franchise fee or royalty). See id. at 52 (in damages measurement, requiring an offset for the value of the franchise fee).


\textsuperscript{147}Of course, there are some easy cases that are not close. For example, in a highly competitive market where the defendants lack any power, consumer harm will be zero and any producer gain will serve to make the impact of the challenged restraint positive.
By contrast, applying the consumer welfare tests asks only whether the price impact of the restraint will be upward or downward.

To illustrate, consider Figure One below. The Figure, which is a variant of Oliver Williamson’s famous welfare tradeoff model, illustrates the measurement differences between the consumer welfare and general welfare tests for a joint venture restraint that yields both efficiencies and increased market power. Prior to the implementation of a challenged restraint this market exhibited prices \( P_1 \) equal to costs \( C_1 \). The challenged restraint does two things. First, it increases the firms’ collective market power, raising the price from \( P_1 \) to \( P_2 \) and reducing output from \( Q_1 \) to \( Q_2 \). Secondly, however, it generates productive efficiencies that reduce the firms’ costs from \( C_1 \) to \( C_2 \). Triangle \( A_1 \) represents the traditional deadweight loss caused by this change; it consists of sales lost to consumers and thus not producing profits to the defendants either. Rectangle \( A_2 \) represents the efficiency gains that result from the challenged practices, and rectangle \( A_3 \) represents a transfer of wealth from consumers to producers.

Under a consumer welfare test the restraint is illegal if \( P_2 \) is higher than \( P_1 \), or \( Q_1 \) is larger than \( Q_2 \). The amount does not matter. All we need to know is that \( P_2 \) exceeds \( P_1 \), which tells us that, whether or not the restraint yields efficiencies, they are not significant enough to offset the price increase fully. We do not need to know the size of the price increase \( P_2 - P_1 \) or output reduction \( Q_2 - Q_1 \). Nor do we need to know anything about the size of \( A_3 \), the wealth transfer, which is a function of both the amount of the price increase and the range of output over which it occurs. The size of \( A_1 \), the deadweight loss, is also irrelevant.

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By contrast, a general welfare test for illegality requires a showing that consumer losses exceed producer gains. For that we must quantify producer gains, rectangle A₂, which means that we must measure the per unit size of efficiency gains, which is the height of the rectangle, and the output over which those gains will be realized, which is its width. We also need to identify and segregate those savings that affect marginal (variable) costs, which show up in the price. In addition, we must quantify the consumer deadweight loss, A₁. For that we need to know the size of the price increase in question (P₂-P₁), and the number of units by which the restraint reduces output (Q₂-Q₁). These are the two legs of the deadweight loss “triangle.” As for the “hypotenuse,” in the ordinary case this figure is not a triangle at all because the demand curve is nonlinear. So we also need to know the demand curve’s shape and location in the demand range covered by the deadweight loss. The set of measurements necessary to compute a general welfare change makes the task heroic in all but the most obvious cases.

This is not to say that identifying competitive harm under a consumer welfare test will always be easy. For example, a restraint might be a collective exercise of market power that puts upward pressure on prices, but it might result in efficiencies so substantial that the resulting price will be lower than it was prior to the restraint. Such a restraint would be lawful under both the consumer welfare test and a general welfare test. But given that market power has been established, the defense would require evidence that the efficiency effect outweighed the market power effect by enough to hold prices to pre-restraint levels. Even so, assessing net price effects would be much simpler than assessing net welfare effects.

Should use of a consumer welfare test be presumptive rather than absolute? Perhaps there are cases in which the amount of market power created by the restraint is relatively small while the efficiency gains are both provable, extremely large, and cannot be achieved by a less

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150 Under a general welfare test we do not need to compute the size of A₃, which benefits producers and harms consumers by the same amount and is thus a wash.

151 This is the approach to efficiencies applied to mergers assessed under the 2010 Merger Guidelines. See Hovenkamp, Antitrust and Efficient Mergers, supra note 145.
restrictive alternative. The important qualifier, however, is that in such cases prices under the restraint are also likely to be lower rather than higher. The case of a total-welfare-increasing restraint that actually raises prices must be regarded as extremely rare and should never be accepted without the clearest proof. I am not aware of a single United States antitrust decision that has found an actual output reduction and price increase resulting from a restraint, but then went on to approve the restraint because productive efficiency gains exceeded consumer losses.

Approaches to the Prima Facie Case: Bipartite, and the Tripartite “Quick Look”

The entire debate about antitrust “modes of analysis” is at bottom about presumptions, burdens of proof, and appropriate judicial responses to concerns about plausibility and location of the evidence. Antitrust cases are complex, and judges depend critically on presumptions and other evidentiary shortcuts. As relatively fewer things are presumed in the plaintiff’s favor and the evidentiary demands become greater, we are moving into rule of reason territory. We move in the opposite direction when a greater number of things are presumed in the plaintiff’s favor and the evidentiary demands are less. The extreme is the per se rule, under which both power and anticompetitive effects will be presumed upon proof that a certain type of conduct has occurred.

“Quick Look” vs. “Sliding Scale”

Beginning with the Trenton Potteries decision, the Supreme Court divided antitrust analysis into two modes, the per se rule and the rule of reason. These two modes were generally treated as creating silos, with a large amount of empty space between them, particularly if one contrasts the blunt expression of the per se rule in Trenton Potteries with the expansive, open ended statement of the rule of reason that Justice Brandeis articulated in Chicago Board of Trade.

The high cost and indeterminacy of antitrust litigation under the rule of reason led to exploration of that empty space for useful shortcuts. Even if a restraint is not clearly within the per se category, perhaps a full blown analysis of power and anticompetitive effects is unnecessary as well. Lower courts, the FTC, and commentators have often suggested that antitrust analysis in fact occupies three silos: the rule of reason, per se illegality, and an intermediate “quick look,” which has been described in different ways by different courts. These intermediate quick look cases are said to bear some of the characteristics of per se unlawful restraints, but there may be an additional complicating factor that deserves additional examination. In some cases the restraint is sufficiently unique that judges lack sufficient judicial

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153 Id. at 397–98:  
The aim and result of every price-fixing agreement, if effective, is the elimination of one form of competition. The power to fix prices, whether reasonably exercised or not, involves power to control the market and to fix arbitrary and unreasonable prices. The reasonable price fixed today may through economic and business changes become the unreasonable price of to-morrow. Once established, it may be maintained unchanged because of the absence of competition secured by the agreement for a price reasonable when fixed. Agreements which create such potential power may well be held to be in themselves unreasonable or unlawful restraints, without the necessity of minute inquiry whether a particular price is reasonable or unreasonable as fixed and without placing on the government in enforcing the Sherman Law the burden of ascertaining from day to day whether it has become unreasonable through the mere variation of economic conditions.  
154 Id., text at note 157.
experience with it. In that situation further examination is required, although perhaps not a full blown rule of reason inquiry.

The Supreme Court has never embraced a three-silo quick look. While the Court has not rejected the idea categorically, its various statements have been quite critical. Only three Supreme Court decisions have explicitly acknowledged the quick look, and then only to reject it under the circumstances.\textsuperscript{155}

An alternative view, initially developed in the Antitrust Law treatise, is that the modes of antitrust analysis represent a continuum, or “sliding scale,” with different fact finding requirements for different situations.\textsuperscript{156} The Supreme Court majority embraced that idea in Justice Breyer’s opinion for the Court in Actavis,\textsuperscript{157} as well as Justice Souter’s opinion in California Dental,\textsuperscript{158} from which Justice Breyer dissented.\textsuperscript{159} The California Dental discussion of the issue is more elaborate, making clear that the Supreme Court did not intend some form of tripartite analysis:

As the circumstances here demonstrate, there is generally no categorical line to be drawn between restraints that give rise to an intuitively obvious inference of anticompetitive effect and those that call for more detailed treatment. What is required, rather, is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint. The object is to see whether the experience of the market has been so clear, or necessarily will be, that a confident conclusion about the principal tendency of a restriction will follow from a quick (or at least quicker) look, in place of a more sedulous one. And of course what we see may vary over time, if rule-of-reason analyses in case after case reach identical conclusions. For now, at least, a less quick look was required for the initial assessment of the tendency of these professional advertising restrictions.\textsuperscript{160}

Justice Breyer did not disagree with the majority’s rejection of a quick look approach. Neither did he agree, however, that a broad query was necessary in order to determine whether “the restraints at issue are anticompetitive overall.”\textsuperscript{161} Rather, he would have broken the query into

\textsuperscript{155}F.T.C. v. Actavis, Inc., 133 S.Ct. 2223, 2237 (2013) (declining to apply “quick look” but then holding that the restraint could be unlawful under the rule of reason); Texaco, Inc. v. Dagher, 547 U.S. 1, 5 (2006) (observing, and not questioning, that the district court had refused to apply quick look doctrine; going on to approve the joint venture agreement at issue); Cal. Dental Ass’n v. Fed. Trade Comm’n, 526 U.S. 756 (1999) (declining to grant FTC’s request for “quick look” analysis and requiring full rule of reason; FTC subsequently dismissed the complaint).

\textsuperscript{156}A REEDA & HOVENKAMP, supra note 1, at ¶1507. The same position was expressed in the three previous editions, all in ¶1507. See also Cal. Dental, 526 U.S. at 780 (“[T]he quality of proof required should vary with the circumstances,” quoting ¶1507 in a previous edition).

\textsuperscript{157}Actavis, 133 S.Ct. at 2237–38, citing an earlier edition of Antitrust Law, ¶1507.

\textsuperscript{158}Cal. Dental, 526 U.S. at 780–81 (1999).

\textsuperscript{159}Id. at 780–94.

\textsuperscript{160}Id. at 780–81.

\textsuperscript{161}Id. at 782.
four classical subsidiary antitrust questions: (1) What is the specific restraint at issue? (2) What are its likely anticompetitive effects? (3) Are there offsetting procompetitive justifications? (4) Do the parties have sufficient market power to make a difference?\footnote{162}

Even a superficial glance at the case law reveals very little justification for a categorical “quick look” silo. In fact, courts vary evidentiary requirements for both power and anticompetitive practices depending on the strength of the plaintiffs case, the plausibility of various assumptions, and the availability and possession of evidence.\footnote{163} A case in point is \textit{Actavis}, where the Court simultaneously said that the rule of reason rather than any “quick look” should apply, but then went on to indicate that sufficient market power and anticompetitive effects could be inferred from the size of an exclusion payment.\footnote{164}

The Court is not saying one thing and doing another. Rather it is doing what courts have always done in these settings. If the plaintiff’s prima facie case for anticompetitive effects is particularly strong, then it makes sense both to assign offsetting burdens to the defendant and also to require a stronger showing of benefit. Just the opposite applies when the plaintiff’s case is weak. By most measures, for example, the FTC’s case against the California Dental Association was particularly strong, involving an explicit price and quality advertising restraints by self-interested members of an association with market power.\footnote{165} However, the rule of reason itself could accommodate such a case simply through proper adjustment of evidentiary burdens. Under the consumer welfare test the question would be whether the CDA rules tended to raise the price or reduce the quality of dental services.


\footnote{163}{\textit{E.g., New York v. Julius Nasso Concrete, 202 F.3d 82, 88–89 (2d Cir. 2000) (“dearth of market information” may lighten plaintiff's evidentiary burden).}}


One problem of sliding scale approaches is the demand they make on judges. If only Hercules can decide an antitrust case sensibly, then sliding scales will not work. A siloed “quick look” approach is not likely to make them any easier, however. To the contrary, the task is simpler to the extent the judge can divide the inquiry into smaller pieces, assessing evidentiary burdens at each stage. In fact, Justice Breyer in Actavis was quite optimistic about the ability of federal district judges to structure the query in a way that was relevant for the case at hand:

As in other areas of law, trial courts can structure antitrust litigation so as to avoid, on the one hand, the use of antitrust theories too abbreviated to permit proper analysis, and, on the other, consideration of every possible fact or theory irrespective of the minimal light it may shed on the basic question—that of the presence of significant unjustified anticompetitive consequences.166

In any event, one serious deficiency of the three-silo approach is that it inclines judges to require a full blown rule of reason whenever they reject a truncated query. That is what happened in California Dental and Safeway167 although not in Actavis.

Another problem with the co-called “quick look” is that it lacks definition. No single set of requirements defines it. Rather, the courts purporting to apply a quick look do what they should be doing under the rule of reason, which is fashioning the assignment of proof burdens piecemeal and making individual legal judgments about the quality of the evidence. The principal thing distinguishing the quick look from the other modes of analysis is the number of presumptions and evidentiary shortcuts. For example, in both Indiana Dentists and Actavis the Court purported to apply the rule of reason but nevertheless permitted truncated proof of both power and anticompetitive effects.168 In the 1984 NCAA case the Supreme Court held that the rule of reason must be applied, because joint conduct was necessary to make delivery of the product possible.169 However, then the Court also held that the defendant’s restriction on the number of nationally televised games was anticompetitive “on its face,”170 thus not requiring an estimate of output effects. It also held, however, that although the NCAA had market power with respect to the challenged broadcasts, “we have never required proof of market power in such a case.”171 Then it later diluted the market power requirement, holding that evidence that intercollegiate football was “uniquely attractive to fans” justified limiting NCAA football to its own market.172 In sum, while expressing its mode of analysis as rule of reason, the Court in fact took numerous shortcuts individually adopted for the case at hand.

166 Actavis, 133 S. Ct. at 2238 (citing 7 ANTITRUST LAW ¶ 1508c).
167 California ex rel. Brown v. Safeway, Inc., 615 F.3d 1171 (9th Cir. 2010), rev’d en banc sub nom, California ex rel. Harris v. Safeway, Inc., 651 F.3d 1118 (9th Cir. 2011).
170 Nat’l Collegiate Athletics Assoc., 468 U.S. at 113.
172 NCAA, 468 U.S. at 112.
While the FTC has generally supported an identifiable “quick look” approach to antitrust, the Antitrust Guidelines for Collaborations Among Competitors, which were issued in 2000 by both Agencies, say this:

Rule of reason analysis entails a flexible inquiry and varies in focus and detail depending on the nature of the agreement and market circumstances. The Agencies focus on only those factors, and undertake only that factual inquiry, necessary to make a sound determination of the overall competitive effect of the relevant agreement. Ordinarily, however, no one factor is dispositive in the analysis.173

That sounds more like “sliding scale” than “quick look.” The Guidelines then elaborate:

In some cases, the nature of the agreement and the absence of market power together may demonstrate the absence of anticompetitive harm. In such cases, the Agencies do not challenge the agreement. Alternatively, where the likelihood of anticompetitive harm is evident from the nature of the agreement, or anticompetitive harm has resulted from an agreement already in operation, then, absent overriding benefits that could offset the anticompetitive harm, the Agencies challenge such agreements without a detailed market analysis.174

Resolution of the market power issue should affect the strength of the prima facie case. For example, a joint venture that controls 80-100% of a well defined market should face close scrutiny of price-affecting or potentially exclusionary conduct. By contrast, if shares are more in the 50% range or the market is not well defined, then the burden of making out a prima facie anticompetitive practice should be higher. The all important question is the venture’s ability to control the market with respect to the restraint in question. If ample opportunities exist for market participation outside the venture, a restraint is to that extent less threatening.

As noted before, exclusive rights such as those involved in the Appalachian Coals decision, should tip the balance in favor of illegality.175 By contrast, the nonexclusive rights granted in both the Broadcast Music (BMI) and Maricopa cases176 strongly suggest that the restraints in those cases were competitively harmless.

In sum, the proposition that the “quick look” creates a distinctive silo somewhere in the isolated space between a rule of reason and a per se rule does not bear close analysis. The aggregate of decisions involving truncated proof clearly establish the contrary. For example, the Engineers case condemned a professional association’s restriction on competitive bidding. The proffered defense, which was that aggressive bidding would force engineers to cut corners and risk safety, was tantamount to an admission that the restraint was naked: its success depended on

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174Id.
its ability to control price cutting. In the Supreme Court concluded that the rule of reason would not countenance such a defense. In the process the prohibition on competitive bidding became the unrebutted prima facie and thus final case. While the Court did not speak of a “quick look” or even state which mode of analysis it was applying, it was clearly applying something that fell between per se and full rule of reason analysis.

Both Engineers and California Dental involved agreements that increased customer search costs significantly, while Maricopa involved an arrangement that decreased them. In the Engineers case the ban on competitive bidding effectively meant that an engineer could not discuss pricing until after he or she had already been engaged and gotten started on a project. In California Dental the limitation on advertising effectively meant that the dentist could not quote a price until he or she already had the patient under examination. In both cases the consumer was free to price shop for an alternative, but by that time there was substantial commitment to a particular seller, plus an uncertain search for a better deal from a rival. By contrast, the agreement in Maricopa reduced consumer search costs by giving patients a price list of physicians who guaranteed a particular price well in advance of immediate need, when they were still in a position to engage in comparison shopping. The Court erroneously applied the per se rule.

The “Quick Look” and Suspicious Joint Venture Activity

Most of the antitrust cases that have seriously considered a “quick look” approach involved restraints within the context of a joint venture, professional association, network, or other joint association whose legitimacy was not in question. The significance of this should be obvious. A naked restraint involving competitors who are not engaged in any form of joint production or legitimate rule making is fairly easy to evaluate. Everything about the arrangement is suspicious and there are no offsetting benefits. A court can readily apply the per se rule.

178 Id. at 696.
179 Id. at 682–84.
181 Others have made this or a somewhat similar observation. See Alan J. Meese, In Praise of All or Nothing Dichotomous Categories: Why Antitrust Law Should Reject the Quick Look, 104 GEO. L.J. 835, 882 n.165 (listing quick look decisions); James Keyte, “Quick Looks” and the Modern Analytical Framework for Assessing Legitimate Competitor Collaborations, 30 ANTITRUST 23 (2016); Michael A. Lindsay & Erik D. Ruda, Antitrust Analysis of Joint Ventures: A Simple Progression, 30 ANTITRUST 12 (2016). See also Southeastern Milk Antitrust Litig., 739 F.3d 262 (6th Cir. 2014) (quick look analysis for price fixing and related practices in milk distribution venture); N.C. State Bd. of Dental Exam’rs v. FTC, 717 F.3d 359 (4th Cir. 2013) (approving FTC’s quick look approach to naked restraint in context of professional association), aff’d on other grounds, 135 S. Ct. 1101 (2015); Princo Corp. v. Int’l Trade Comm’n, 616 F.3d 1318 (Fed. Cir. 2010) (production joint venture involving IP cross licensing to be subject to full rule of reason rather than a quick look); Rossi v. Standard Roofing, Inc., 156 F.3d 452 (3d Cir. 1998) (applying per se rule to boycott; rejecting defendant’s argument for quick look when there was no distribution venture in place); California ex rel. Harris v. Safeway, Inc., 651 F.3d 1118 (9th Cir. 2011) (rejecting the quick look approach in favor of a more detailed inquiry regarding a revenue-sharing provision between competitors during the term of a labor dispute).
Restraints created in the context of otherwise lawful joint associations are more problematic. The court needs to figure out how the challenged restraint functions within the larger collaboration. For example, few would dispute that the public can benefit from an association of professionals such as dentists with some involvement in the regulation of the quality of care, as well as some power to regulate unauthorized practice or improper commercial behavior. Further, meaningful regulation of quality necessarily entails some exclusion of substandard services. Much the same can be said of production joint ventures. Seen in this way, the “quick look” operates mainly as a device for looking more deliberately at suspicious restraints that are created in such ventures. A restraint on price advertising such as the one in California Dental\textsuperscript{182} may require a little more searching examination than a similar restraint among completely unaffiliated but competing retailers, such as grocers. This may be appropriate for no other reason than to give the defendants a chance to explain why this particular restraint is reasonably necessary to the operation of otherwise legitimate joint activity. If no explanation is accepted and it is clear the restraint is profitable only because it reduces output and raises prices, then summary condemnation is in order, typically with no inquiry into power.

A good illustration involving a production joint venture is the Polygram case.\textsuperscript{183} At issue was an agreement between two firms who were jointly producing a recording of three popular classical tenors\textsuperscript{184} that they would no longer promote separate recordings they had previously made of the same artists. Ordinarily an agreement between rivals not to advertise their competing products would be per se unlawful market division.\textsuperscript{185} In this case, however, the parties were also involved in the joint production of a new recording of the three tenors, and some of the individual recordings in the new product were the same as those in the original separately produced products. The defendants claimed that an agreement restraining promotion of their separately developed products was necessary to give the new, jointly-developed product a chance, citing a danger that the separate products would take a free ride on the jointly developed product.\textsuperscript{186} As the court observed, however, to the extent there was a danger of free riding it flowed in the other direction. The independently developed products had been on the market first. If there was a free rider danger it was that the new product would ride on the built up consumer recognition of the older separate productions. In any event, the “free riding” that the defendants described was really nothing more than legitimate competition between the earlier separate products and the new jointly developed product.\textsuperscript{187}


\textsuperscript{184}Luciano Pavarotti, Placido Domingo, and Jose Carreras.

\textsuperscript{185}E.g., Blackburn v. Sweeney, 53 F.3d 825 (7th Cir. 1995) (agreement among former but now separate law partners not to advertise in one another’s markets unlawful per se).

\textsuperscript{186}Polygram, 416 F.3d at 37.

\textsuperscript{187}See also N. Tex. Specialty Physicians v. Fed. Trade Comm’n, 528 F.3d 346, 366–67, 370 (5th Cir. 2008) (physicians’ association that negotiated jointly for insurer contract engaged in “inherently suspect” activity by collaborating on prices); United States v. Brown Univ., 5 F.3d 658 (3d Cir. 1993) (approving quick look approach to Ivy league university’s agreement limiting financial aid competition with respect to students who had been admitted to more than one of the participating schools); Realcomp II, Ltd. v. Fed. Trade Comm’n, 635 F.3d 815 (6th Cir. 2011) (approving FTC’s quick look analysis to real estate association rule that excluded price cutters and nontraditional selling agencies); United States v. Realty
Nothing about this approach requires a third “quick look” silo. It indicates only the fairly obvious proposition that when a presumptively efficient joint venture includes a suspiciously anticompetitive looking restraint, the court should take a little extra care to see how the challenged restraint relates to the overall venture. That is fundamentally a rule of reason inquiry, but one that may be truncated if the facts so warrant.

Balancing

General statements of the rule of reason sometimes say that it routinely requires “balancing” of pro- and anti-competitive effects.\textsuperscript{188} Courts make these statements notwithstanding decades of litigation showing such balancing to be unworkable and actual attempts at it to be rare.\textsuperscript{189} Once a

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\textsuperscript{188}See, e.g., United States v. Apple, Inc., 791 F.3d 290, 321 (2d Cir. 2015), \textit{cert. denied}, 136 S. Ct. 1376 (Mar. 7, 2016) (need to balance is element of rule of reason case); ZF Meritor, LLC v. Eaton Corp., 696 F.3d 254 (3d Cir. 2012) (suggesting that creation of price-cost tests in exclusive discounting cases was an effort at “balancing of the procompetitive justifications of above-cost pricing against its anticompetitive effects…”); United States v. Microsoft Corp., 253 F.3d 34, 59 (D.C. Cir. 2001) (“courts routinely apply a balancing approach” requiring plaintiff to “demonstrate that the anticompetitive harm \ldots outweighs the procompetitive benefit”); Am. Ad Mgmt., Inc. v. GTE Corp., 92 F.3d 781 (9th Cir. 1996) (rule of reason requires a showing that “the restraint is unreasonable as determined by balancing the restraint and any justifications or pro-competitive effects of the restraint”). \textit{See also} Eastman Kodak Co. v. Image Tech. Serv., Inc., 504 U.S. 451, 486–87 (1992) (Scalia, J., dissenting; difference between rule of reason and per se rule is that former requires balancing).

\textsuperscript{189}On the infrequency of balancing in the decisions, \textit{see} Carrier, \textit{Bridging the Disconnect}, supra note 97 (finding that actual balancing occurred in 4% of rule of reason cases); Carrier, \textit{An Empirical Update}, \textit{supra} note 97 (updating previous article; rate of balancing declined to 2%).
court purports to engage in balancing it is almost always acting outside of its competence except in the most obvious cases. Balancing under a consumer welfare test is significantly easier than under a general welfare test, because the former requires prediction only of price or output effects. This is not to say, however, that balancing is easy, particularly for restraints that have survived the burden shifting analysis that occurs prior to balancing.

Sixth Circuit Judge Taft noted over a century ago in Addyston Pipe that some courts misconceived the role of antitrust analysis as determining “the proper limits of the relaxation of the rules for determining the unreasonableness of restraints of trade.” These courts “have set sail on a sea of doubt” by assuming the power to determine “how much restraint of competition is in the public interest, and how much is not.”

Taft’s caution was in sharp contrast to Justice Brandeis’ oft criticized statement of the rule of reason in the Chicago Board of Trade decision, which put everything up for balancing:

The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint is imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation or the reverse; but because knowledge of intent may help the court to interpret facts and to predict consequences.

A test that makes everything relevant provides nothing useful, because it gives no calculus for weighting or even identifying the important factors. In a complex world it is essential that antitrust tribunals keep their eyes on the ball, which under the consumer welfare test refers to restraints that realistically restrict output and increase price, and that are not essential to carrying on a joint venture’s legitimate functions.

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192 Chi. Bd. of Trade v. United States, 246 U.S. 231, 238 (1918). See also In re Sulfuric Acid Antitrust Litig., 703 F.3d 1004 (7th Cir. 2012) (“[t]he rule of reason directs an assessment of the total economic effects of a restrictive practice that is plausibly argued to increase competition or other economic values on balance.”). In the context of vertical restraints, see Cont’l T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 49 (1977) (“Under this rule, the factfinder weighs all of the circumstances of a case . . .”).
Balancing is not even conceptually possible without a unit of measurement. That is, purely ordinal methods of balancing work only when the value on one side is zero. When both sides have some weight, however, we must have a way of netting them out. To the best of my knowledge, outside of the merger context no court has ever even attempted to put an actual number, such as dollars of economic loss or gain, on either the anticompetitive effects of a restraint or the justifications offered against it. A far better way to view the rule of reason is as a series of sequential steps intended to avoid balancing whenever possible. When balancing must be performed, the consumer welfare principle insists on a measurable unit, which is either price or output.

The area that comes closest to permitting balancing is merger analysis practiced under the Merger Guidelines. What makes this possible is that the given test for merger illegality is price effects, not general welfare effects. The relevant question in merger cases is, after both competitive harm and offsetting efficiencies are taken into account, are prices likely to go up or not? As noted above, using a test that focuses on prices or output rather than general welfare is essential if the rule of reason is to be administered rationally. Even in these cases, however, measuring the requisite effects is very difficult.

Some decisions describe the rule of reason’s burden shifting framework itself as a sort of “balancing,” but they are hardly the same thing. For example, in determining whether the plaintiff has made out a prima facie case the court relies on evidence and a certain amount of intuition to determine whether the plaintiff’s evidence of power and an anticompetitive practice has crossed a threshold. At that point the burden shifts to the defendant to show a justification, although without determining magnitudes. None of this requires or even contemplates a cardinal weighing of pro- and anti-competitive effects. Indeed, the sequence of evidentiary steps, with its shifting burdens, is an attempt to avoid balancing. The “less restrictive alternative” step which comes near the end shows that we attempt to make this decision without having to quantify net competitive harm in dollars or welfare. The point is to show the existence or not of a less restrictive alternative without having to put a value on the difference.

A better way to view balancing is as a last resort when the defendant has offered a procompetitive explanation for a prima facie anticompetitive restraint, but no less restrictive alternative has been shown. At that point the basic burden shifting framework has taken us as far as it can. The court must then determine whether the anticompetitive effects made out in the prima facie case are sufficiently offset by the proffered defense. Even here, a hard look at the quality of the evidence is important. The court needs to make sure that the market is well defined, with convincing evidence of power, and that the threat of higher prices or anticompetitive exclusion is clear. The same thing is true of evidentiary support for the offered justification. Hopefully, few cases will survive this hard look and still require balancing, although the possibility cannot be excluded.

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195 Id. at 382.
196 See discussion supra, text at notes 144–50.
197 In re NCAA Student-Athlete Name & Likeness Licensing Litig., 37 F. Supp. 3d 1126 (N.D. Cal. 2014) (describing the “burden-shifting framework” to conduct “balancing” in order to determine “if the restraint’s harm to competition outweighs its procompetitive effects.”).
The Scope of the Rule of Reason

The Declining Domain of the Per Se Rule

The high point of per se antitrust illegality occurred in the 1950s and 1960s, when some joint ventures of competitors that were almost certainly efficient were determined to be unlawful per se, either because they divided markets or else constituted concerted refusals to deal. Among vertical practices, both minimum and maximum resale price maintenance were declared unlawful per se, as were most tying arrangements. For a decade vertical nonprice restraints were thought to be unlawful per se. Under the Philadelphia Bank test even mergers were subject to a quasi-per se rule if the market shares of the merging parties exceeded a certain threshold.

While not all of this antitrust jurisprudence has been expressly overruled, nearly all of it is dubious today. The per se rules against maximum and minimum resale price maintenance and the per se rule against vertical nonprice restraints have all been explicitly overruled. The boycott rule has been limited to situations that involve at least two competitors; that is, purely vertical boycotts are subject to the rule of reason. In other areas, such as antitrust treatment of joint ventures and tying arrangements, the Supreme Court and lower courts have chipped away at the per se rule, although the basic decisions have not been expressly overruled. The strong structural presumption of merger illegality reflected in the Philadelphia Bank case has been very considerably diluted, although market structure remains relevant.

205 See notes 199–200, supra.
206 On the structural determinants of merger legality, see 4 & 4A AREEDA & HOVENKAMP, supra note 1.
Naked vs. Ancillary Restraints

Correct application of the per se rule depends critically on a judgment that certain practices are unreasonable as a “class,” or family group. As a result, condemnation requires that they be correctly placed within that group. Extensive study of certain classes of practices has shown, however, that many have alternative explanations that are competitively beneficial or benign. Most notable are resale price maintenance, tying arrangements, and horizontal restraints in joint ventures.

Mistaken Factual Judgments

Per se illegality is appropriate if judicial experience indicates that a particular class of restraints rarely has any effect but to reduce output and increase price. This is fundamentally an economic judgment. The judgment is also heavily factual, even though the ultimate choice of a rule presents a question of law. Because it is factual, it can also be wrong. For example, consider Justice Frankfurter’s widely quoted dicta in his opinion for the Court in the Standard Stations case that “important economic differences” exist between tying and exclusive dealing, revealing that “[t]ying agreements serve hardly any purpose beyond the suppression of competition.”

Justice Frankfurter’s supposed factual observation was woefully mistaken. First of all, the principal case he relied on in making that judgment, International Salt, involved tying by a nonmonopolist in the sale of salt injecting equipment. International Salt’s market share in the market for salt injecting machines (the “Lixator” and the “Saltomat”) was never determined because the Court held that ownership of a patent was sufficient to establish power. The tied product was salt, a common commodity incapable of being monopolized. The best estimates are that the defendant’s sales accounted for two to four percent of the salt market – not enough to foreclose anyone. The tie was very likely being used either to effect quality control or perhaps to engage in a form of price discrimination that is often beneficial to consumers as a class. Whatever the “suppression of competition” in International Salt was, Justice Frankfurter never identified it. Perhaps it was the fact that the tie removed many dollars worth of salt from the open market, but a simple contract to sell a large volume of salt would have done that.

Justice Frankfurter’s error serves as a warning to judges not to jump too quickly to categorical rules of law. The historical record on tying has always been mixed. Even by the time he wrote, some ties imposed by dominant firms very likely had unreasonably exclusionary

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210 See ANTITRUST LAW ¶1509 (class unreasonableness).
211 See discussion infra, text at notes 212–38.
212 See discussion supra, text at notes 40–71.
215 Id. at 395–96.
218 See Hovenkamp & Hovenkamp, Tying Arrangements and Antitrust Harm, supra note 71, at 944.
effects. Others were almost certainly harmless or benign, however, while yet others had uncertain effects. Nothing about this history suggested that tying arrangements “serve hardly any purpose” other than suppressing competition. At most it suggested that as of the 1940s tying arrangements were not yet well understood.

Restraints Embedded in Legitimate Joint Activity

Joint ventures, trade associations, competitor-managed networks and other collaborative organizations usually contribute net social and economic benefits, but that does not necessarily mean that every agreement their members make is competitively harmless. A great deal of antitrust case law under the rule of reason has concerned specific agreements in the context of joint activities whose existence or general legitimacy was not being challenged. This has important implications for antitrust remedies. It also means that we need tools for identifying when these challenged restraints are legitimate or competitively harmful. The ancillary restraints doctrine addresses this need. It can operate to exonerate agreements that facially appear to restrict output but that are also reasonably necessary to the venture’s effective functioning.

The requirement that a restraint be “ancillary” to an organization’s legitimate activities applies only if the restraint itself threatens competition. If a particular agreement is competitively harmless, then it is lawful under the antitrust laws whether or not it is ancillary. For example, suppose an organization such as the California Dental Association decides to require its executives to wear business suits with neckties to all organization functions. One might doubt that such a provision is reasonably necessary to the proper functioning of a professional association, but the answer to that question is irrelevant unless we can come up with a credible reason for thinking that requiring suits and ties threatens competition.

One important contribution to rule of reason analysis was Robert Bork’s extended development of the ancillary restraints doctrine, which he attributed largely to Sixth Circuit Judge Taft’s decision in the Addyston Pipe case. In fact, Bork read a great deal into Taft’s discussion, which concerned mainly why price fixing among unintegrated members of a cartel is unlawful per se, while “price fixing” among the members of a legally recognized entity such as a

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221IBM Corp. v. United States, 298 U.S. 131 (1936) (tying of defendant’s data cards to leased computers); Pick Mfg. Co. v. GM Corp., 299 U.S. 3 (1936) (GM’s insistence that dealers use only original GM parts for automobile repair found lawful); Henry v. A.B. Dick co., 224 U.S. 1 (1912) (tying of defendant’s patent mimeograph machine to stencils, paper and ink, probably for metering purposes).
222See discussion infra, text at notes 239–69.
224United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1898). Taft later became Vice President and President of the United States, and after that a Justice on the Supreme Court.
partnership is not. Taft pointed out that within the partnership the setting of a common price might be necessary, but it would be “ancillary” to the true business of the partnership. Bork later developed this distinction further when he was a judge on the D.C. Circuit.

The ancillary restraints doctrine is not a complete method for applying the rule of reason, but rather an early stage decision about which mode of analysis should be applied. First, it requires that the plaintiff identify a particular restraint, such as price fixing, output limitation, or concerted exclusion, that is causing competitive harm. The defendants then try to show that their collective business arrangement has a legitimate purpose, such as joint provision or other integration or networking, and that the challenged restraint is ancillary to that purpose. For example, once two large oil producers have developed a jointly owned refinery, the fungible gasoline that it produces must be sold to both participants’ dealers at the same price. By contrast, the ancillary restraints doctrine was never applied in the NCAA case because the defendants never made a convincing argument that the limitation on nationally televised games was reasonably necessary to the functioning of the venture. Rather, the defenses they offered indicated that the restraint was naked.

Once ancillarity has been invoked the plaintiff can respond by showing that (1) the claimed integrative activity is either untrue or a sham; (2) even if the claimed integrative activity is legitimate, the challenged restraint is not reasonably ancillary to it; or (3) although the challenged activity might be reasonably ancillary to the venture’s overall activity, the anticompetitive effects are substantial and a less restrictive alternative is available.

A restraint is “naked” if its profitability depends on the exercise of market power. Beginning with that definition, the best first thing is to make the defendant explain why the restraint is profitable? If it provably improves product or performance, facilitates innovation or distribution, or otherwise pleases customers, then the restraint should be treated as ancillary. If its profitability depends on its ability to reduce output (measured by quantity or quality) and increase price, it is naked. Note that a restraint might do both of these things at the same time, but that simply makes it grist for rule of reason analysis. That is, the rule of reason applies where both set of effects are plausible and we have to sort out which one dominates. If the only impact of the restraint is to improve a product, then it is legal.

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225Id. at 290–91.
226Id. at 291 (citing Richardson v. Buhl, 43 N.W. 1102 (Mich. 1889); Arnot v. Coal Co., 68 N.Y. 558 (1877); People v. Milk Exchange, 39 N.E. 1062 (N.Y. 1895); People v. North River Sugar Refining Co., 7 N.Y.S. 406 (1889); State v. Nebraska Distilling Co., 46 N.W. 155 (Neb. 1890); State v. Standard Oil Co., 30 N.E. 279 (Ohio 1892); American Biscuit & Mfg. Co. v. Klotz, 44 F. 721 (E.D. La. 1891); Distilling & Cattle Feeding Co. v. People, 41 N.E. 188 (Ill. 1895); Pittsburgh Carbon Co. v. McMillin, 23 N.E. 530 (N.Y. 1890); National Harrow Co. v. Hench, 83 F. 36 (3d Cir. 1897); Pacific Factor Co. v. Adler, 27 P. 36 (Cal. 1891); Santa Clara Valley Mill & Lumber Co. v. Hayes, 18 Pac. 391 (Cal. 1898).
231See discussion supra, text at notes 127–43.
The Supreme Court’ Dagher decision added some confusion to the ancillary restraints doctrine by attempting to distinguish venture from extraventure activities, and suggesting that the doctrine applied only to the latter.\(^{232}\) The court approved a two-party joint refining venture’s setting of a common price for its output, which was sold to dealers for both venture participants, Texaco and Shell. In the Court’s eyes, the setting of a price was a “venture activity,” and as a result must be regarded as lawful without regard to the ancillary restraints doctrine because the activity was effectively that of a single firm.\(^{233}\) That would of course suggest that the limitation on nationally televised games in the NCAA case was not a “venture activity,” because there the Court found a naked restraint of trade.\(^{234}\) However, an inherent part of the delivery of intercollegiate football over television is the negotiating of television contracts, and a single entity would also have to decide how many games it wished to televise in behalf of each team.

A better way to view Dagher is as a joint venture that produced a fungible product, gasoline, to which each firm subsequently supplied its own distinctive additives. A common product coming out of a common refinery would have to be sold to the initial buyer at a single price, and there was no suggestion that the dealers, who were separate entities, were fixing prices in subsequent transactions. That made Dagher a classic ancillary restraints case.

To be sure, Judge Taft’s examples in Addyston Pipe, which Dagher did not cite, did suggest a joint venture’s restrictions on nonventure activities as an example of an ancillary restraint. Thus, for example, a partnership might impose noncompetition agreements on its members, forbidding them from engaging in separate business in competition with the partnership.\(^{235}\) But such restrictions are only a small subset of the requirements that might be treated as ancillary, or not, to a joint venture.

In the context of joint ventures, a sensible starting definition of an ancillary restraint is one that is either arguably procompetitive on its own terms, or that is reasonably necessary to the proper functioning of the venture. As such, the restriction can be either on the venture’s own business (such as limits on the number of NCAA games), or else limitations on extra-venture business (such as rules limiting the ability of conference athletes to play non-conference games). By characterizing the restraint on the number of games in NCAA as naked,\(^{236}\) the Court was in fact saying two things: first, that there was little or no evidence that the NCAA joint venture really depended on this particular restraint for its success; second, this restraint was profitable because of its effect in cartelizing a market by reducing output.

Rules that are nominally “output reducing” are frequently necessary to the proper functioning of a joint venture. For example, the NCAA must limit the number of conference games per team per season, the number of players who can be on a squad or on the field, or the number of minutes in a football game. A game with two hours of clock time, running perhaps six hours of real time rather than the current three, would create greater advertising opportunities.

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\(^{232}\) Texaco, Inc. v. Dagher, 547 U.S. 1, 7–8 (2006) (“we agree with petitioners that the ancillary restraints doctrine has no application here . . . .”).

\(^{233}\) Id. at 6.


\(^{235}\) See United States v. Addyston Pipe & Steel Co., 85 F. 271, 280 (6th Cir. 1898) (“Restrictions in the articles of partnership upon the business activity of the members, with a view of securing their entire effort in the common enterprise, were, of course, only ancillary to the main end of the union . . . .”).

\(^{236}\) NCAA, 468 U.S. at 110.
These rules are ancillary, however, because some limits must be set on the game itself. For example, limits must be set on the time of student athletes. This is also true of more traditional production joint ventures. For example, having decided to produce automobiles jointly, General Motors and Toyota must still settle on the number to produce and any number they choose could be assailed for not being larger.\textsuperscript{237}

Price-affecting agreements promulgated by joint ventures or other legitimate associations have always been particularly difficult for courts. Often the key is fungibility of the product produced by the venture’s members. A price agreement is properly regarded as ancillary when the joint venture is involved in production and produces a fungible product. That was the case in \textit{Dagher}, where the venture refinery produced gasoline.\textsuperscript{238} It was also true for the coal selling joint selling agency involved in \textit{Appalachian Coals}.\textsuperscript{239} A common dealer representing several dozen coal mining companies would sell coal as a unitary product, perhaps without even identifying the particular mine from which the coal came. While the price at any moment would depend on market conditions, it could not depend on which member’s coal was being sold. If it did, then the low price seller would sell all of its coal first, the second lowest next and so on.

By contrast, when products are differentiated individual pricing might be quite consistent with the operation of the venture. For example, several manufacturers of automobiles may build a common testing or R&D facility, or perhaps even a production facility for certain components. But once each has produced its own, differentiated automobiles, there is no obvious reason that they would have to fix their prices. So in some cases shared production of inputs requires the setting of a joint price but in others it does not. In addition, fixing of downstream prices two or more transactions removed from the venture are more suspicious. For example, the \textit{Dagher} joint venture’s setting of a common price for fungible gasoline made perfect sense for the initial transaction from the venture to the dealers. But the dealers themselves are separate entities and, absent some good argument to the contrary, competition should determine their downstream markups and prices.

\textbf{Remedies}

The antitrust equity statutes are very broad, giving the government authority to “prevent and restrain” antitrust violations\textsuperscript{240} and authorizing private parties to obtain an injunction against “threatened loss or damage” from an antitrust violation.\textsuperscript{241} One important difference between these two provisions is that equitable relief for private parties is limited to those antitrust violations that actually threaten to injure the private plaintiffs themselves, while the government has a more global enforcement authority to restrain violations without showing injury to itself.

In both cases, however, the power to obtain equity relief from a court is limited to violations of the antitrust laws. The statutes do not authorize mandatory dissolution of a complex entity or combination simply because some small facet encompasses an antitrust

\textsuperscript{238}Texaco, Inc. v. Dagher, 547 U.S. 1 (2006).
\textsuperscript{239}Appalachian Coals, Inc. v. United States, 288 U.S. 344 (1933).
\textsuperscript{241}15 U.S.C. §26 (“Any person, firm, corporation, or association shall be entitled to sue for and have injunctive relief . . . against threatened loss or damage by a violation of the antitrust laws . . . .”).
violation. Statutory language aside, an efficient enforcement rule should to the extent possible leave the socially valuable provisions of a joint venture intact, at least in cases where these can safely be segregated from the competitively harmful provisions. So when the restraint is part of a more elaborate joint venture, a properly designed remedy should enable the venture to function and preserve all or most of its socially valuable activity, while limiting or eliminating the harmful activity.

Delimiting Remedies Against Complex Activity

The power to devise and limit remedies judicially has evolved very considerably over the history of antitrust. For example, the first case that the United States Supreme Court decided on the merits involved a joint venture that was very likely efficient but that also fixed railroad freight rates, perhaps anticompetitively. As both the Interstate Commerce Commission and the Eighth Circuit observed, the principal purpose of the joint venture was to facilitate long distance shipment when most of the railroads operated within a single state. Interstate shipments had to be transferred from one line to the next and this necessitated agreements on such things as scheduling, cargo transfer, track gauges, and perhaps even freight rates. In the 1890s agents computed freight rates manually with pencil and paper. If a package had to be shipped down multiple roads the agent at the beginning would have to calculate a rate for the entire trip. As a result, both the Interstate Commerce Commission and the Eighth Circuit agreed that the railroads needed a “common authority” to set rates and facilitate inter-railroad transfers and scheduling. Nevertheless, the government requested a complete dissolution of the venture, and the Supreme Court complied. This meant, of course, that all the benefits of the venture were lost together with any anticompetitive effects.

Moving forward nearly a century, the Supreme Court’s NCAA decision is in sharp contrast. At issue was an NCAA rule limiting the number of nationally televised football games that any team could offer in one year. All parties and the Court conceded that the NCAA overall was essential to the operation of intercollegiate sports, and also that this required a great deal of coordinated rule making. Indeed, the plaintiff University of Oklahoma was an NCAA

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242By contrast, consent decrees, a form of settlement, can include practices that have not been condemned and are very likely lawful under the antitrust laws. See Joshua D. Wright and Douglas H. Ginsburg, The Costs and Benefits of Antitrust Consents (OECD working paper, June 2016), available at http://www.law.gmu.edu/assets/files/1642.pdf (criticizing practice of obtaining consent decrees that prevent lawful behavior as an abuse of agency power).


245Trans-Missouri, 166 U.S. at 297, 300 (noting Government’s request to have the association dissolved).


247See, e.g., id. at 103: Respondents concede that the great majority of the NCAA’s regulation enhance competition among member institutions. Thus, despite the fact that this case involves restraints on the ability of member institutions to compete in terms of price and output, a fair evaluation of their competitive character requires consideration of the NCAA’s justification for the restraints.
member with a highly successful football team. It hardly wanted the NCAA dissolved. Rather, it was attacking a single provision limiting the number of nationally televised games per team. The requested remedy was a narrow injunction against enforcement of the four game limitation.248 The more recent O’Bannon case is similar. No one was seeking dissolution of the NCAA. Rather the plaintiffs wanted to force modification of NCAA rules pertaining to how NCAA athletes are compensated, and to force schools to share with athletes a portion of the revenue from licensing of names and likenesses of the more successful athletes.249

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The narrowing of equitable remedies in such cases is based on the premise that the venture as a whole is socially valuable and worth keeping. Before granting such a remedy the court must also determine whether the challenged provision appears to affect price or output and, if yes, whether it is reasonably “ancillary” to the functioning of the venture. The NCAA Court found that the restriction was not necessary,250 and expressed this by calling the challenged restraint “naked” – that is, a naked restraint contained in an otherwise beneficial joint venture.

As noted previously, many of the antitrust cases in which the FTC or a lower court has accepted “quick look” analysis involve restraints attached to other conduct that is either concededly or arguably procompetitive.251 The court must identify those aspects of the defendants’ conduct that are anticompetitive and attempt to sever those agreements from the venture as a whole.252

In such cases, should the remedy be an injunction, damages, or both? As a general matter, in cases where transaction costs are relatively low an injunction rule is thought preferable because the parties can bargain around it to an efficient result.253 By contrast, if transaction costs are high, then damages are preferable, assuming that the court has a rational basis for computing them. Whether this approach is appropriate in antitrust cases is an interesting question.254 Competition injuries typically affect many interests who are not parties in the antitrust litigation. For example, in NCAA the rationale for antitrust condemnation was an output reduction and consumer injury in the market for televised football. But the case itself was an internecine dispute limited to members of the NCAA organization. No party even purported to speak for consumers.255

249O’Bannon v. Nat’l Collegiate Athletics Assoc., 802 F.3d 1049 (9th Cir. 2015), cert. denied, 137 S. Ct. 277 (2016).
250After rejecting the NCAA’s proferred defenses. See discussion supra, text at notes 117–18.
251See discussion supra, text at note 180.
252For example, even the decree in Polygram, which involved a production joint venture, did not attempt to enjoin the joint production of a new album, but only the ancillary agreement not to promote the earlier, separate albums. See In Re Polygram Holding Co., 136 F.T.C. 310, 2003 WL 21770765, at *2–3 (FTC, 2003).
255The parties were the University of Oklahoma and a class action by the College Football Association, which was composed of 61 other NCAA colleges. No one identified as a consumer was a party. See
Nevertheless, optimal damages in such a case must be large enough to compensate all injured parties, including consumers. Optimal damages for a joint venture antitrust case that raises the possibility of both harm and benefit equals the amount of any monopoly overcharge plus the deadweight loss. If the conduct is efficient then the defendant’s gains will be enough to pay both the overcharge and deadweight loss and have something left over, but not otherwise.\textsuperscript{256} Computing these numbers is extraordinarily difficult, suggesting an administrative preference for an injunction.\textsuperscript{257}

Further, mandatory trebling strengthens the case for an injunction-only remedy. Trebling distorts the efficiency calculus very considerably. For example, suppose the harm caused by the defendants’ practice is $1000 per year (deadweight loss plus overcharge) and yields the defendants $1200 in profits per year. A simple damages rule would permit the conduct to continue because the defendants could pay them and still make a $200 profit. In a well functioning market the parties would bargain around an anticipated injunction and the defendant would pay some amount between $1000 and $1200 and continue the practice. Both of these outcomes are efficient. But with mandatory trebling the value of the damages goes to $3000. The defendant will very likely halt the practice, even if it is efficient.\textsuperscript{258}

Taking existing law as given, treble damages and all, it appears that the optimal approach would be to permit an injunction that is narrowly tailored to suppress the competition-injuring behavior, but not more, along with damages to injured parties for past harm done.

Equitable Remedies: Unilateral vs. Collaborative Conduct

Collaborative conduct is inherently more conducive to tailored equitable remedies than is unilateral conduct. This makes it critical to distinguish the two types of conduct, an issue that is more complex than appears on first glance. As a general proposition we treat organizations whose owners are multiple shareholders or whose assets are multiple incorporated subsidiaries as single entities unreachable by §1 of the Sherman Act.\textsuperscript{259} By contrast, actors who are joined together by contract and whose individual members retain significant business decision making power are treated as individuals and §1 applies.\textsuperscript{260}

\textsuperscript{256}See HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY §17.2 (5th ed. 2015); William M. Landes, \textit{Optimal Sanctions for Antitrust Violations}, 50 UNIV. CHI. L. REV. 652 (1983). Whether the damages rule would be different under a consumer welfare test presents another interesting question. The damages would have to be large enough to compensate actually-purchasing consumers for their losses, but consumers within the deadweight loss triangle are also injured to the extent they have been forced out of the market. If their losses are taken into account, damages under a consumer welfare test would be the same as those under a general welfare test.

\textsuperscript{257}See discussion \textit{supra}, text at notes 145–150.

\textsuperscript{258}Cf. Kaplow, \textit{On the Relevance of Market Power}, \textit{supra} note 108, at *49 & n. 143. Kaplow criticizes the \textit{Antitrust Law} treatise and enforcement agencies, both in the U.S. and the EU, for their preference for injunctions for unilateral exclusionary practices, but mentions neither the difficulty of computing optimal fines or treble damages, which is mandatory in all private actions in the United States. Of course, the treble damages rule is legislative and could be repealed.

\textsuperscript{259}Copperweld Corp. v. Independence Tube corp., 467 U.S. 752 (1984); see 7 AREEDA & HOVENKAMP, \textit{supra} note 1, at ¶¶1462–1465.

\textsuperscript{260}American Needle, Inc. v. NFL, 560 U.S. 183 (2010).
Firms might take advantage of the legal system in order to disguise their activities or structure, making multilateral agreements appear to be unilateral. For example, the members of a joint venture might become shareholders in a common corporation that directs portions of their business, but this does not change the fact that they are independent profit-maximizing entities. The Supreme Court recognized this nearly fifty years ago in the Sealy and Topco cases, both of which applied §1 of the Sherman Act to incorporated joint ventures whose members were also their shareholders.261 This also happened in the case of network charge card entities Visa and Mastercard, who incorporated as single entities even as they carried out policies made by their shareholder members, who were competing banks.262 It was also true of the Supreme Court’s American Needle decision, where a single corporation operated as exclusive licensee of all of the NFL teams’ separately owned intellectual property rights and then licensed them out exclusively.263 Corporate status did not serve to change this agreement from collaborative to unilateral as long as it was guided by or affected the individual business decisions of the teams. Importantly, this result does not necessarily make the conduct unlawful, but rather serves to make it amenable to the more aggressive standards of §1 of the Sherman Act.

The remedial consequence of treatment as a single entity rather than an agreement of multiple entities is readily apparent. The optimal penalty against unilateral conduct is a fine or damages rather than an injunction.264 For multilateral conduct, however, the case for an injunction is far stronger.265

For both types of conduct, the trick is to devise an injunction that does not require ongoing regulation of the defendant’s business. For example, in an anticompetitive exclusion case involving a single entity an injunction would have to specify the scope and terms of the defendant’s duty to deal, effectively placing the court in the role of public utility regulator. This fact has played a particularly powerful role in the Supreme Court’s reluctance either to recognize an “essential facility” doctrine or else to expand the monopolist’s unilateral duty to deal with rivals.266

These problems typically do not arise when the challenged action is that of a collaborative venture. In that case the venture’s members are individual maximizers. The court can simply enjoin the practice found to be unlawful, and individual venture members can then compete to the competitive outcome. Using the NCAA case as an example, if the NCAA was a single entity and a court found the four-national-televised-game-per-season rule to be anticompetitive, then it would have to devise and supervise an optimal remedy, requiring ongoing supervision of the NCAA’s internal affairs. But given that the NCAA was a joint

262See Osborn v. Visa, Inc., 797 F.3d 1057, 1066 (D.C. Cir. 2015), cert. dismissed as improvidently granted, 137 S. Ct. 289 (2016) (organization into a single parent entity controlling the behavior of member banks did not serve to make their conduct unilateral).
265See discussion infra, text at notes 266–268.
266See 3B AREEDA & HOVENKAMP, supra note 1, at ¶¶771, 772g (4th ed. 2015).
venture whose members were individual profit maximizers, a simple injunction against enforcement of the four-game rule would very likely suffice. Free from this constraint, each team could then negotiate for as many national television events as the market would bear. More popular teams would obtain more contracts to be sure, but that is the way competition works.

An example that speaks to the issue is the Supreme Court’s *American Needle* decision.\(^{267}\) The NFL required all member teams to grant an exclusive license to individual team trademark and related rights to a central organization, NFL Properties, which then gave an exclusive license to a single firm to manufacture logoed headgear for retail sale. The defense, recognized by the Seventh Circuit but reversed by the Supreme Court, was that the NFL was a single entity subject only to §2 of the Sherman Act.\(^{268}\)

Under the Seventh Circuit’s analysis the case involved nothing more than an internal dispute about how a multi-divisional single entity would allocate intellectual property rights among its subsidiaries. For example, a decision by Ford Motor Company to refuse to license out the name “Lincoln,” referring to one of Ford’s wholly owned subsidiaries, would be a unilateral act. United States antitrust law almost never compels a firm acting unilaterally to license its intellectual property rights.\(^{269}\) If it did, a court would have to determine the scope and terms of the duty to deal.

By contrast, if the NFL was a multi-actor joint venture, as the Supreme Court concluded, a simple injunction against enforcement of the exclusive licensing provision would be preferable on both substantive and enforcement grounds. As for the substance, while unilateral refusals to license are virtually immune from antitrust challenge, concerted refusals are not.\(^{270}\) As for enforcement concerns, an injunction would simply free up each NFL member team to make its own decision about the maximizing way to license its IP right. Further, if they colluded §1 of the Sherman Act could be brought to bear.

**Naked Restraints Embedded in Legitimate Joint Ventures; Inherent Rule of Reason?**

As the *NCAA* case makes clear, even socially beneficial joint ventures may embody naked restraints. In this setting a restraint is naked if it makes no contribution to the proper functioning of the joint venture *and* is profitable only because of its tendency to reduce output and raise price. The first of these elements suggests why a hard core per se rule might not be in order: the tribunal needs to determine the relationship between the restraint and the overall venture. Once it has determined that a restraint is not essential to the venture’s legitimate functioning and that its profitability depends on power over price, then there is no reason for the court to delay. The restraint can be condemned without inquiry into power.

All of this would be straightforward enough were it not for *NCAA*’s one additional holding – namely, that the rule of reason must be applied to all restraints when a joint venture is


\(^{268}\) *See American Needle, Inc. v. NFL*, 538 F.3d 736 (7th Cir. 2008).

\(^{269}\) *Cf. id.* at 744 (“As a single entity for the purpose of licensing, the NFL teams are free under §2 to license their intellectual property on an exclusive basis, even if the teams opt to reduce the number of companies to whom they grant licenses”).

\(^{270}\) *See 13 HERBERT HOVENKAMP, ANTITRUST LAW ¶¶2202, 2203 (3d ed. 2012).*
essential to producing the product at all.\footnote{Nat'l Collegiate Athletics Assoc. v. Board of Regents, 468 U.S. 85, 101 (1984): … it would be inappropriate to apply a per se rule to this case. This decision is not based on a lack of judicial experience with this type of arrangement, on the fact that the NCAA is organized as a nonprofit entity, or on our respect for the NCAA's historic role in the preservation and encouragement of intercollegiate amateur athletics. Rather, what is critical is that this case involves an industry in which horizontal restraints on competition are essential if the product is to be available at all. See also American Needle, Inc. v. NFL, 560 U.S. 183, 202 (2010) (relying on NCAA and holding that the rule of reason must be applied).} Applying this rule of reason, the Court then held that the particular restraint before the Court was not necessary to delivery of the product.\footnote{Id. at 114.} That made the output affecting restraint at issue naked, but it had to be condemned under the rule of reason anyway.

The Court did not attempt to justify the link between situations where joint activity is essential to operations and global use of the rule of reason, and its seems inconsistent with the established ancillary restraints doctrine. A network industry such as cell phones may need standards and cross licensing in order to be able to deliver its product, but that hardly serves to explain why its members would need an agreement to fix smartphone prices. Or suppose an NCAA restraint fixes the prices of stadium hot dogs or parking?

Viewed more narrowly, however, the Court’s language may have meant only that because the venture itself was not being challenged, at least a brief second look must be given to those restraints incorporated into the joint venture agreement – for no other reason than to ensure that they are reasonably necessary to the functioning of the venture. That brief look would be enough to ensure that the “rule of reason” is being applied, even though condemnation might be appropriate on a very truncated analysis once the restraint was found to be inessential and naked.

**Agreements Concerning Intellectual Property Rights**

How should antitrust tribunals treat the fact that collaborative activity includes agreements concerning intellectual property rights? Factually, technology transfers and joint research and development are essential elements of innovation and technological progress. At the same time, however, agreements that nominally license IP rights, particularly patents, can be just as anticompetitive as agreements involving unprotected products.\footnote{See Hovenkamp, Patent System, supra note 54, at 525–27.}

One important set of tools for approaching this problem is the language of the intellectual property statutes themselves. To the extent that the IP statutes expressly authorize a particular practice, it should be immune from antitrust attack. For example, the Patent Act provides that a unilateral refusal to license cannot be either patent misuse or an antitrust violation,\footnote{35 U.S.C. §271(d)(4).} or that tying of patented goods is unlawful only in the presence of tying market power.\footnote{35 U.S.C. §271(d)(5).} Care must be taken that the statute not only authorizes certain conduct, but also anticompetitive instances of such conduct. For example, while the Patent Act authorizes the transfer of patents,\footnote{See 35 U.S.C. §261 (“Applications for patent, patents, or any interest therein, shall be assignable in law by an instrument in writing.”).} this does
not entail that they can be sold anticompetitively. Thus an acquisition of patents can still be an unlawful asset acquisition for purposes of the merger laws.\textsuperscript{277} Congress changes the Patent Act frequently, and can always create or resize an immunity if it sees fit.\textsuperscript{278}

When a practice is not authorized by the Patent Act, then the best approach is to let antitrust do what it ordinarily does, condemning naked agreements under a per se rule and applying the rule of reason to legitimately ancillary activity. Of course, the fact that a challenged restraint is part of an intellectual property licensing scheme can certainly be relevant to questions about ancillarity. Most technology transfer agreements contemplate joint research or joint production, making them grist for ancillary restraints doctrine and the rule of reason. By contrast, product price fixing is usually a naked restraint, particularly if the products were separately developed.

The same thing is true of pay-for-delay settlements such as the one at issue in Actavis.\textsuperscript{279} During the period covered by the agreement – that is, until licensed production actually occurs – there is typically no integrated productive activity to which such an agreement is reasonably ancillary. That makes it a form of naked product market division. In addition, a payment that delays entry to some point later than the expiration of the patent should be unlawful per se. During the post-expiration period such an agreement is a naked restraint unprotected by any language in the Patent Act.\textsuperscript{280} A delayed entry payment that permits entry prior to the patent’s expiry raises different issues and requires more elaborate treatment, as the Supreme Court’s Actavis majority developed. Nominally, the Court’s decision required the rule of reason, but it also permitted both power and anticompetitive effects to be inferred upon seriously truncated proof.\textsuperscript{281} Clearly, an agreement that delays generic production into the future and effectively prohibits other firms from coming in is a naked restraint, profitable only because it reduces output during the exclusion period.

All purely vertical intellectual property agreements should be assessed under the rule of reason, consistent with the evaluation of vertical agreements generally.\textsuperscript{282} Such agreements involve a rights holder as licensor who is not in competition with any licensee. Pools and other forms of technology sharing should presumptively be assessed under the rule of reason, but with some warnings. One is when they purport to control products rather than IP rights. Another is when they are exclusive, particularly when the patents in question were separately developed. By contrast, joint development ventures may require exclusivity in order to create sufficient incentives and control free rider problems. In any event, exclusivity is generally harmless in the absence of power.

\textsuperscript{277} Areeda & Hovenkamp, supra note 1, at ¶1202f (4th ed. 2016).
\textsuperscript{279} FTC v. Actavis, Inc., 133 S.Ct. 2223, 2232 (2013).
\textsuperscript{280} EU law condemns such agreements “by object,” which is roughly equivalent to the per se rule. See Case T-472/13, Lundbeck v. Commission, 2016 E.C.R. Celex No. 613TJ0472 (condemning pay-for-delay agreements, at least one of which extended beyond the expiration of the relevant patent).
\textsuperscript{282} See discussion infra, text at note 205.
Applying the Rule of Reason: Structural Issues

Under the rule of reason the plaintiff must show that the defendants have market power, which generally refers to the power held by the organization as a collective. For example, if traditional market share measurements are used, the relevant share is usually the sum of the shares of the individual members of a joint venture or other organization whose conduct is in issue.283

The brief discussion below does not attempt to recount all of the technical issues involved in assessing market power under the antitrust laws.284 Rather, it defends two propositions. First, for most horizontal collaborations assessed under the rule of reason, the market power requirement should be less than it is for a single dominant firm engaged in similar activity. Relatedly, alternative measures that do not depend on computation of a market share may be more appropriate in the context of a joint venture. Second, however, and in some conflict with existing law, for purely vertical agreements involving the threat of exclusion (mainly exclusive dealing and tying) the power requirement should be closer to the requirement for single firm monopolization.

Assessing the Power of Horizontal Collaborators

The formation of a joint venture of competitors or potential competitors creates power by agreement, often in an instant. For example, if three firms each having 25% of the market should form a joint production venture, their aggregate output will immediately be 75%.285 If an open membership venture such as a real estate multiple listing organization is attractive to new firms because it promises high profits, new entrants will have an incentive to join. In sum, joint venture power is typically created by fusion, and much more easily and quickly than by unilateral conduct. While the relationship between the monopolist and its rivals is inherently hostile, the relationship between an open membership venture and other firms may be much more inviting.

In addition and as noted before, nonstructural remedies are typically easier to administer against a joint venture. For example, the remedy in a case such as NCAA is simply an injunction against the four game limitation on nationally televised productions.286 Each team is then free to choose the number of games it wishes to televise. In the wake of the Supreme Court’s decision the number of nationally televised football games increased dramatically.287 If the NCAA were a single entity, however, then administering relief would require a regulator to determine the optimal number of games that each firm could televise nationally. The relative non-invasiveness

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283 ARDEDA & HOVENKAMP, supra note 1, at ¶574 (4th ed. 2014).
284 For this, see id., Ch. 5.
285 If the venture results in an anticompetitive price increase market share could fall below this number, as some buyers respond to the higher price by substituting away. If the venture produces cost reductions or a superior product, its share could rise as its output becomes more attractive.
of antitrust remedies against complex but procompetitive joint ventures suggests that overdeterrence is a smaller problem than for unilateral conduct.

The rule of reason for both unilateral and collaborative activity requires proof of market power sufficient to warrant the inference that the challenged conduct is anticompetitive. The requisite minimum depends on the type of activity that is being challenged. For example, unilateral predatory pricing is generally thought to be a successful exclusionary strategy only if the predator already has a dominant position in the market.\textsuperscript{288} There is little reason to deviate from that premise when the defendant is a collaboration rather than a single entity. By contrast, filing a patent infringement suit on an improperly obtained patent\textsuperscript{289} could, if successful, enable a firm with a relatively modest market share to acquire a significant monopoly.\textsuperscript{290}

Reflecting these considerations, under current antitrust doctrine single firm exclusionary practices bear the highest market power requirement, depending on whether the challenged offense is monopolization or attempt to monopolize.\textsuperscript{291} Generalizing about horizontal joint ventures is more difficult and variations are much wider than for unilateral conduct, but the minimum stated in the case law is clearly less than for unilateral exclusionary practices.\textsuperscript{292}

**Power Requirements for Vertical Exclusionary Conduct**

One important difference between horizontal and vertical restraints is that the former can create power merely by the agreement itself. For example, the contractual union of seven firms

\textsuperscript{288}See 3A AREEDA & HOVENKAMP, supra note 1, at ¶¶725, 728 (4th ed. 2014).
\textsuperscript{290}Generally in accord is Kaplow, On the Relevance of Market Power, supra note 108, who would vary the market power requirement with conduct as well, but more elaborately than suggested here.
\textsuperscript{291}See 3B AREEDA & HOVENKAMP, supra note 1, at ¶807c,d,e (4th ed. 2014) (collecting decisions and observing considerable variation in market share requirements).
\textsuperscript{292}United States v. Visa U.S.A., Inc., 344 F.3d 229, 240 (2d Cir. 2003) (evidence that Visa’s credit card accounted for 47% of dollar volume of sales and Mastercard approximately 26% sufficient to sustain §1 claim against each of them: “We agree ... that Visa U.S.A. and MasterCard, jointly and separately, have power within the market for network [charge card] services”); Advanced Health-Care Serv., Inc. v. Giles Mem. Hosp., 846 F.Supp. 488, 493–94 (W.D. Va. 1994) (“Numerous cases and commentators have suggested that absent extraordinary circumstances, a market share over fifty percent is required to show market power” and that the joint venture’s market share “peak[ed] at 44.1% in 1989 and average[d] 32.9% over the 1986–1989 period of its existence. Thus, defendants’ market share was significantly below the established floor for showing monopoly power.”); Delaware Health Care Inc. v. MCD Holding Co., 957 F.Supp. 535, 541 (D. Del. 1997) (hospital and home health care provider joint venture, “a market share of less than 55 percent, without other evidence tending to show monopoly power, is insufficient as a matter of law”); New Mexico Oncology & Hematology Consultants, Ltd. V. Presbyterian Healthcare Serv., 54 F.Supp.3d 1189, 1219–20 (D.N.M. 2016) (denying defendant’s motion to dismiss plaintiff’s claim under section two of the Sherman Act where defendant held an alleged market share of 46% and had an exclusive contract with a second hospital that held an alleged market share of 10% because “[t]he combined market share of both entities ... totals more than 50% and is not insignificant. Moreover, the Tenth Circuit has held that cooperation between two would-be competitors ... deprives the marketplace of the independent decision making that are essential to a competitive system.”); Re/Max Intern., Inc. v. Realty One, Inc., 173 F.3d 995 (6th Cir. 1999) (reversing the district courts grant of summary judgment for the defendants where the two largest real-estate brokerages in northeast Ohio had a combined market share in excess of 50% and had allegedly boycotted selling properties to buyers represented by Re/Max agents in order to maintain their monopoly).
with ten percent market shares each can create a joint arrangement with a market share of 70 percent. By contrast, a purely vertical agreement does nothing to increase market shares. Of course, the large market share may already be there, but the vertical agreement itself does not add to it. As a result, purely vertical agreements require an additional explanation of how harm to competition comes about. This fact makes vertical agreements presumptively less offensive to competition than horizontal restraints. For example, if seven 10 percent firms joined in a joint distribution arrangement we might legitimately require a further explanation why the arrangement, which now controls 70% of distribution, is reasonable under the circumstances. By contrast, when a single firm with a 70% market share engages in restricted distribution we would not ordinarily require an explanation on that basis alone. There would have to be some additional element, such as upstream exclusion or downstream foreclosure, or perhaps facilitation of collusion.

Vertical interbrand restraints, which include tying and exclusive dealing, are more closely akin to exclusionary practices by dominant firms than to joint ventures. Indeed, many of the things challenged as monopolistic practices under §2 of the Sherman Act are actually a form of tying, exclusive dealing, or related practice.\(^{293}\) When a classic tie or exclusive deal raises anticompetitive concerns, it is because a single upstream firm is using the arrangement as an exclusionary practice directed at rivals in its own market. The entities upon which the tie or exclusive deal is imposed are simply conduits. For example, by forcing computer makers or customers to accept the Internet Explorer browser as a condition of obtaining Windows, Microsoft was attempting to exclude Netscape, a rival in the browser market.\(^{294}\)

One significant difference between intrabrand and interbrand restraints is that established dealers typically profit from intrabrand restraints such as resale price maintenance or location clauses. The dealers who are most generally affected tend to be newcomers and discounters. As a result practices such as resale price maintenance are often collaborative, in the sense that both manufacturer and established dealers profit from them. Indeed, the original *Dr. Miles* RPM case involved a druggists’ cartel using their supplier Dr. Miles to impose resale price maintenance in order to discipline discounters.\(^{295}\) Even the “classical” defenses of RPM, such as free riding, involve a set of established dealers who have agreed to provide a full set of supplier-mandated services, and a set of less established discounters who seek to avoid them.\(^{296}\) The one vertical interbrand restraint that is likely to encounter significant opposition from established dealers is maximum resale price maintenance, because it limits dealers’ ability to take full advantage of their pricing power in their service areas. But this is so because maximum RPM is virtually


\(^{295}\)See HERBERT HOVENKAMP, ENTERPRISE AND AMERICAN LAW, 1836-1937 at 331–48 (1991) (showing that cartel of retail druggists forced Dr. Miles to impose RPM on its products in order to do away with retail discounters).

\(^{296}\)E.g., Lester G. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86 (1960); see HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY: THE LAW OF COMPETITION AND ITS PRACTICE §11.3 (5th ed. 2015)
always procompetitive. Indeed, it is difficult even to articulate a coherent anticompetitive explanation for it other than the possibility that it might be disguised minimum price fixing. 297

By contrast, dealers are more likely to resist tying or exclusive dealing, which limit their own freedom. To be sure, there are exceptions to both of these rules, but they do prevail in most cases. As a result, tying and exclusive dealing do not represent an “aggregative” use of power in the way that a cartel or joint venture does. 298 Tying and exclusive dealing are both unlawful when they exclude rivals unreasonably, principally rivals in the downstream or tied product market. When they have this effect the practice typically injures not only consumers and rivals, but also the dealers or other intermediaries upon whom the restraint is imposed. For example, the claim in Dentsply, a §2 case, was that Dentsply’s exclusive dealing rule denied dentists lower cost alternative teeth materials that the market would otherwise have made available. 299 That practice injured Dentsply’s rivals, its own dealers, and consumers. The tying claim in Microsoft was that the Windows/Internet Explorer tie denied market access to rival browsers such as Netscape, a product variation that presumably would have made computer sellers as well as consumers better off. 300

To be sure, many tying arrangements are efficient, benefitting consumers and presumably also dealers by increasing output, improving product quality, or simplifying distribution. But the important point is that when tying is anticompetitive, competitors, dealers and customers can all be expected to resist it. As a result, a firm imposing a tie is “on its own,” so to speak and it makes little sense to aggregate its shares or assess a lighter burden on the power issue. When ties or exclusive deals are legitimately exclusionary they are so on more-or-less the same conditions as the general run of unilaterally-imposed exclusionary practices. As a result, Sherman Act §2 monopoly power standards should apply to them.

**Vertical Agreements and the Rule of Reason**

The classic joint venture is made up of competitors or potential competitors, and the threat posed by the venture is that it threatens to diminish competition between them, either by facilitating price fixing or excluding certain rivals. Many of these ventures additionally contain vertical elements to the extent that some important asset is being bought and sold. For example, NFL teams may negotiate exclusive contracts to license their IP rights to a common broker, 301 or the members of a patent pool or blanket license arrangement may license their rights to one another or to a common holder. 302

The rule of reason for vertical restraints addresses the same set of issues as for horizontal restraints, with one important qualifier: While agreements among competitors are relatively

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297 See 8 AREEDA & HOVENKAMP, supra note 1, at ¶¶1634–40.
exceptional and require some scrutiny, ordinary buy-sell and licensing agreements are an essential part of ordinary business, right down to the consumer level. As a result, simply alleging a vertical agreement gets a plaintiff nowhere. Vertical restraints should be found unlawful only when they facilitate an output reduction that serves to increase prices in relation to costs. To that extent, every anticompetitive vertical restrain must contain at least an implicit horizontal element, whether it be collusion or exclusion. The vast majority of purely vertical agreements pose no such threat. These conclusions are largely borne out by the case law. Once the rule of reason is applied to a vertical practice, few instances of it are condemned.\footnote{For surveys of the case law, see Carrier, Bridging the Disconnect, supra note 97; Carrier, An Empirical Update, supra note 97.}

The exceptions tend to be for exclusive dealing or quasi-exclusion dealing, but that is precisely because the threat posed by these practices relates to horizontal exclusion.\footnote{E.g., McWane, Inc. v. FTC, 783 F.3d 814 (11th Cir. 2015); United States v. Dentsply Intern., Inc., 399 F.3d 181 (3d Cir. 2005); ZF Meritor, LLC v. Eaton Corp., 696 F.3d 254 (3d Cir. 2012) (market share discounts likened to exclusive dealing).}

When considering vertical restraints and a possible per se rule, the first question is whether one can even conceive of a purely vertical agreement that is “naked” in the sense that its only likely effects are anticompetitive? Even assuming the answer is yes, would such agreements exist in sufficient numbers to warrant categorical treatment?

After years of ambiguity, the Supreme Court finally stated a strong and categorical rule that purely vertical agreements should be assessed under the rule of reason.\footnote{NYNEX Corp. v. Discon, Inc., 525 U.S. 128 (1998).} Previously, however, it had believed otherwise. Minimum resale price maintenance was unlawful per se from the Supreme Court’s 1911 \textit{Dr. Miles} decision\footnote{Dr. Miles Med. Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).} to its 2007 \textit{Leegin} decision, when the Supreme Court overruled nearly a century of authority and applied the rule of reason.\footnote{Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877 (2007).} Maximum RPM's per se rule had a shorter life. Manufacturer setting of a dealer’s maximum price first became unlawful per se in the Supreme Court’s \textit{Albrecht} decision in 1968,\footnote{Albrecht v. Herald Co., 390 U.S. 145 (1968).} until Albrecht was overruled by \textit{Khan Oil} in 1997.\footnote{State Oil Co. v. Khan, 522 U.S. 3 (1997).} Since \textit{Khan Oil}, no decisions have condemned maximum RPM.\footnote{See D. Daniel Sokol, The Transformation Of Vertical Restraints: Per Se Illegality, The Rule Of Reason, And Per Se Legality, 79 ANTITRUST L.J. 1003, 1010 (2014).}

Vertical nonprice restraints generally involve such things as assignment of dealer locations or territories, and rules forbidding these dealers from making sales outside their appointed area. They can also involve other things, such as dealer warranty service requirements, showroom requirements, prohibitions on the sale of used goods, or even restrictions on how the dealer’s business holds itself open to customers. They have been addressed under the rule of reason for most of the life of the antitrust laws. The one exception was a single decade between 1967 and 1977 when the Supreme Court applied the per se rule to vertical nonprice restrictions.
The Court’s meandering journey on vertical nonprice restraints is a stage play for the Court’s uncertainty about antitrust treatment of vertical agreements generally. In the government-brought *White Motor* case in 1963 the Court refused to decide the issue of per se illegality for vertical territorial restraints one way or the other, concluding that it was too early to identify the principal purpose or effects of such restraints.\(^{311}\) Then, four years later in 1966 it believed it knew enough, declaring dealer locational restrictions unlawful per se in the *Schwinn* case, and for a firm that had less than 13% of the market.\(^{312}\) The Court concluded that “it is unreasonable without more for a manufacturer to seek to restrict and confine areas or persons with whom an article may be traded after the manufacturer has parted with dominion over it.”\(^{313}\) The Court confusingly mixed common law concerns about restraints on alienation with competition policy. Only a decade later, however, it overruled *Schwinn* in *GTE Sylvania*.\(^{314}\) The Court suggested that while vertical locational restrictions might restrain “intrabrand” competition -- that is, among dealers in the same brand -- they can promote “interbrand” competition with dealers in other brands. Balancing these effects required rule of reason treatment.\(^{315}\) Vertical nonprice restraints have been evaluated under a rule of reason ever since, and few instances have been condemned.\(^{316}\)

Interbrand restraints, including exclusive dealing and tying, have also experienced doctrinal inconsistency. Under tying a buyer is permitted to purchase one product only if it agrees to take a second product from the same seller as well. Under exclusive dealing a dealer is prohibited from dealing in the goods of a competitor. For example, a Ford automobile dealership’s franchise agreement might prohibit it from selling new cars other than Fords.

A per se rule may still survive for some tying arrangements, provided that the defendant has sufficient tying market power to force a choice that the purchaser does not want. In *Illinois Tool Works* the Supreme Court somewhat confusingly declared that it was eliminating a per se rule that a tie was unlawful simply because the defendant’s tying product was patented.\(^{317}\) However, it also embraced the Court’s holding in *Jefferson Parish*, which clearly had not overruled per se precedents but declared only that the defendant’s market share was too small to give it the power to force a buyer to make a choice that it would not otherwise have made.\(^{318}\) Indeed, *Jefferson Parish* declared that “if the existence of forcing is probable,” then “per se prohibition is appropriate.”\(^{319}\) The case involved a tying product that was not patented.

Presuming that the *Illinois Tool Works* Court intended to overrule precedent on the narrowest

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\(^{311}\)White Motor Co. v. United States, 372 U.S. 253, 265 (1963):

We do not know enough of the economic and business stuff out of which these arrangements emerge to be certain. They may be too dangerous to sanction or they may be allowable protections against aggressive competitors or the only practicable means a small company has for breaking into or staying in business….


\(^{313}\)Id. at 379.


\(^{315}\)Id. at 54–55.


\(^{319}\)Id. at 16.
possible grounds, the best interpretation is that it was overruling any per se presumption based simply on the fact that the tying product was patented.\footnote{Initially established in International Salt Co., Inc. v. United States, 332 U.S. 392 (1947).} Indeed, later in the Court’s opinion Justice Stevens spoke of the need to reexamine “the presumption of per se illegality of a tying arrangement involving a patented product….”\footnote{\textit{Ill. Tool Works}, 547 U.S. at 40.} Instead, invocation of the per se rule against tying requires proof of tying market power as traditionally defined.

To be sure, tying in the presence of power and sufficient foreclosure can exclude rivals. Whether it does so anticompetitively is a question for the rule of reason, because tying can also reduce costs, improve product quality, or facilitate price discrimination. As for the latter practice, some instances are anticompetitive while others are not. Nearly everyone agrees that the so-called “leverage” theory for non-foreclosing ties is defunct.\footnote{For an exception, see Einer Elhauge, \textit{Rehabilitating Jefferson Parrish: Why Ties Without a Substantial Foreclosure Share Should Not Be Per Se Legal}, 80 \textit{ANTITRUST} L.J. 463 (2016).}

Exclusive dealing has always been acknowledged to be a rule of reason offense. As noted previously, however, sometimes its foreclosure effects can reach more broadly than tying does. A tie applies to a tying product, while exclusive dealing applies to an entire store or dealership.\footnote{See discussion \textit{supra}, text at notes 86–87.} Exclusive dealing can even compel the same type of second degree price discrimination that tying does. For example, an ice cream franchisor that requires franchisees to sell its products exclusively might build an overcharge into the products and use it in lieu of a volume based franchise fee. In an attempt to take advantage of the harsher rule against tying, some plaintiffs have attempted to characterize such arrangements as ties, in which the tying product was the franchise or business name, and the tied product was the products made subject to the exclusive deal.\footnote{\textit{E.g.} Siegel v. Chicken Delight, 448 F.2d 43, 51–52 (9th Cir. 1971), cert. denied, 405 U.S. 955 (1972) (supplies tied to trademarked business); Midwestern Waffles v. Waffle House, 734 F.2d 705, 712 (11th Cir. 1984) (similar); Krehl v. Baskin-Robbins Ice Cream Co., 664 F.2d 1348 (9th Cir. 1982) (similar).} Of course, to the extent that is true all exclusive dealing could be turned into ties, simply by characterizing the sales contract, a licensed trademark, or some other common incident of business as the tying product. In general, however, there is no categorical reason why ties should be treated more harshly than exclusive dealing. All should be treated under the rule of reason and – because they are fundamentally exclusionary practices that drive rivals out rather than pulling them in, they should be subject to monopolization law’s market power requirements.\footnote{See discussion \textit{supra}, text at notes 297–99.}

\textbf{Compound Vertical-Horizontal Practices}

By far the best approach to \textit{purely} vertical restraints is a categorical rule of reason. Setting tying aside, the only other recognized exception concerns dealer cartels, which means that these restraints are not purely vertical at all. A powerful dealer in a certain market may insist on either maintained prices or vertical dispersion in order to reduce competition from other dealers, thus permitting a unilateral price increase.\footnote{See \textit{8 AREEDA & HOVENKAMP}, \textit{supra} note 1, at ¶1604.} A subset of colluding dealers can do the
same thing, as the *Dr. Miles* litigation itself established.\(^{327}\) In both of these situations the success of the strategy depends on the power held by downstream firms, but also on the strength of the manufacturer’s brand vis-à-vis alternatives. The dealer cartel situation is an easy one: if it is naked it should be illegal *per se*.\(^{328}\) Of course, not every joint dealer complaint about a price cutter is necessarily anticompetitive, because the offending dealer may be ignoring other legitimate, costly requirements that the manufacturer has imposed. As a result the court needs to determine whether dealer collusion or the manufacturer’s wishes to promote distribution efficiency accounts for the restraint.

In his opinion in *NYNEX*,\(^{329}\) Justice Breyer took some pains to distinguish the Supreme Court’s much earlier *Klor’s* decision on concerted refusals to deal.\(^{330}\) *NYNEX* involved an agreement between a single upstream firm and a single downstream firm, and the Court concluded that this must be subject to the rule of reason. By contrast, the allegations in *Klor’s* were that its rival retailer Broadway-Hale conspired with several otherwise competing appliance manufacturers to boycott Klors.

In *Leegin* the Court added a wrinkle, speaking of a dealer that accedes to the wishes of a manufacturer’s cartel, or inversely, a manufacturer that accedes to a dealer’s cartel:

A horizontal cartel among competing manufacturers or competing retailers that decreases output or reduces competition in order to increase price is, and ought to be, *per se* unlawful. To the extent a vertical agreement setting minimum resale prices is entered upon to facilitate either type of cartel, it, too, would need to be held unlawful under the rule of reason. This type of agreement may also be useful evidence for a plaintiff attempting to prove the existence of a horizontal cartel.\(^{331}\)

In other words, the horizontal relationship, if naked, might be unlawful per se but the participation by a vertically related collaborator would have to be addressed under the rule of reason. The Court’s rationale is perplexing. If the cartel is naked then wouldn’t the vertically related firm’s participation be naked as well? One might say that the RPM in question actually served the manufacturer’s interest by controlling free riding. But in that case the RPM in question would be an output increasing strategy and the dealers’ arrangement should be addressed under the rule of reason as well. The Court might have been suggesting leniency for a vertically related firm that participated in the cartel against its will, but the rule of reason is the wrong vehicle for doing that.

In its *Apple* decision the Second Circuit added a sensible qualification: if the vertically related firm is the one who actually initiates or facilitates the cartel, then the per se rule applies to its own conduct as well.\(^{332}\) A dissenter complained that the majority’s approach was inconsistent

\(^{327}\)E.g., Toledo Mack Sales & Serv., Inc. v. Mack Trucks, Inc., 530 F.3d 204 (3d Cir. 2008) (refusing to dismiss RPM claim alleging that it was instigated by a dealers’ cartel). On the *Dr. Miles* retail druggists’ cartel, see note 294, supra.

\(^{328}\)Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 893 (2007) (stating in dicta that such a dealer cartel would be *per se* unlawful).


\(^{330}\)Id. at 135–36.


\(^{332}\)United States v. Apple, Inc., 791 F.3d 290 (2d Cir. 2015).
with the above quoted language from *Leegin*, requiring rule of reason evaluation for the conduct of the vertically related firm.\(^{333}\)

The *Leegin* dicta aside, Apple’s participation (and solicitation of) the restraint was naked, making it difficult to see what could be accomplished by requiring the rule of reason. The facts were that Apple wished to launch an ebook store simultaneously with the release of its iPad electronic device. Amazon, a rival ebook seller, was charging prices that Apple believed were too low to make its own entry profitable. As a result it solicited from the major publishers an agreement under which they would adopt a new model calling for higher prices to be set by each publisher and imposed on Amazon.

We can call this rule of reason if we want, but the fact remains that the power was clearly there, to be inferred from the fact that Amazon acceded to the wishes of the publisher cartel. The resulting price umbrella made Apple’s entry profitable, and it was the only reason offered for the horizontal agreement. To be sure, some of Amazon’s prices may have been below its acquisition costs.\(^{334}\) That fact might justify Apple in bringing a predatory pricing action against Amazon in court, but hardly in orchestrating a cartel of book sellers with the power to force Amazon to raise its prices. The dissent also complained that Apple was in fact removing a barrier to entry into the market against Amazon, the dominant firm.\(^{335}\) Low prices are always a “barrier to entry” against someone who cannot afford to meet them, but once again that is not a justification for collusion.

**Conclusion**

The complexities of antitrust’s rule of reason have provoked complaints that its use inevitably produces arbitrary results that are inconsistent with due process norms.\(^{336}\) Justice Brandeis’ extraordinarily broad and indeterminate formulation in the *Chicago Board* case posed just such a threat.\(^{337}\) Evaluation of the legality of restraints under a general welfare test is also so difficult and indeterminate that it can threaten rational adjudication.\(^{338}\)

While rule of reason antitrust cases will always be complex, we can limit arbitrariness by focusing on price and output effects rather than general welfare effects. The triumph of the consumer welfare principle in antitrust has served to limit the query to consumer harm rather than attempting to measure the much more difficult tradeoffs involved in assessing welfare generally. While the Supreme Court’s *Twombly* decision on pleading requirements went further than it needed to,\(^{339}\) it has performed the useful function of getting plaintiffs to focus on the

\(^{333}\)Id. at 341.

\(^{334}\)See id. at 299, although the prices were described by the majority as “loss leaders,” which are almost always legal because their profitability does not depend on subsequent recoupment of monopoly profits. See 3A AREEDA & HOVENKAMP, supra note 1, at ¶742f (loss leaders), ¶¶726–727 (4th ed. 2015).

\(^{335}\)Id. at 350.


\(^{337}\)Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918). See discussion supra, text at note 191.

\(^{338}\)See discussion supra, text at notes 145–50.

\(^{339}\)See discussion supra, text at notes 26–39.
correct issues when they bring antitrust complaints. They need to allege an output-reducing or price-increasing restraint and enough factual allegation to get the ball rolling. Ideally, both Twombly’s approach to antitrust complaints and Matsushita’s approach to summary judgment should make antitrust under the rule of reason more rational by focusing on those factors that make output reducing restraints more likely in the context at hand. An additional way to reduce arbitrary decision making is to make the per se rule apply to a mode of analysis rather than to a classification of restraints. Properly used, that would limit the problem of irrational per se rules. 340

Finally, through proper management of presumptions and burden shifting the courts have proven quite capable of assessing restraints without the need to “balance” positive and negative effects – an activity that almost always forces them out of their area of competence.

340 See discussion supra, text at notes 69–72.