NEW YORK STATE BAR ASSOCIATION

1984 Antitrust Law Symposium

A report from the Annual Meeting of the Antitrust Law Section
February 1, 1984

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Foreword

The 36th Annual Meeting of the Antitrust Law Section of the New York State Bar Association was held on February 1, 1984 at the New York Hilton, New York City.

The annual business meeting was held at 9:20 a.m. Upon motion duly made and seconded, the Section by-laws were amended to increase the number of members of the Executive Committee from eight to nine. Chairman Kimba M. Wood then read the report of the Nominating Committee, which was composed of Henry L. King, Stephen M. Axinn and Eleanor M. Fox. Pursuant to the Nominating Committee's report and upon motions duly made and seconded, the following Section members were unanimously elected to the indicated offices for the year 1984-85:

Chairman . . . . Walter Barthold
Vice Chairman . . . . Sanford M. Litvack
Secretary . . . . Barry J. Brett

Eleanor M. Fox, James T. Halverson, Henry L. King, Barry E. Hawk, Kimba M. Wood and Stephen M. Axinn were elected members of the Executive Committee.

We are delighted to share with you, once again, the proceedings of the Antitrust Law Section Annual Meeting.

The Section wishes to express its appreciation to the editor of this Symposium, Barry E. Hawk of Fordham Law School, and his assistant, Thomas Mitchell.

Kimba M. Wood

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CHAPTER 1
WELCOME AND INTRODUCTION

Kimba M. Wood
Walter Barthold

CHAIRMAN KIMBA M. WOOD: Welcome to our annual meeting of the New York State Bar Association Antitrust Section.

I am Kimba Wood, Chairman of the Section this year. It is my great pleasure to turn the floor over to Walter Barthold, who, as Vice Chairman of this Section, has given me immeasurable help this year. Walter is Program Chairman for today's program entitled "A New Era in Antitrust."

WALTER BARTHOLD: Thank you very much, Kimba. Good morning everyone. We have a full program today that we are going to start immediately.

You should all know of a couple of changes in the program today. Mr. Baxter has, as I am sure you are aware, resigned as Assistant Attorney General in charge of the Antitrust Division. We have with his gracious consent replaced him as our dinner speaker by Mr. J. Paul McGrath, the current incumbent in that position. Mr. McGrath will be our dinner speaker today.

Closer to home, we have a substitution in the morning program. Our first announced speaker, Stephen Axinn, was called away by a superior power, namely the *Texaco-Getty* merger litigation, and is unable to be present. We have, however, recruited a pinch hitter — and what a pinch hitter. With his gracious cooperation, we have persuaded Robert A. Skitol of the Washington firm of Wald, Harkrader & Ross to launch the program today with a discussion of recent decisions by the Supreme Court in the area of antitrust.

Bob Skitol is well known as a lecturer on antitrust and trade regulation. He is a graduate of NYU Law School, and has been chairman of the Legislation Committee of the Antitrust Law Section of the American Bar Association. This is Bob's first starring role with our section. I repeat — we are exceedingly grateful to him for filling in at this later date.

CHAPTER 2
RECENT SUPREME COURT ANTITRUST DECISIONS: A REAGAN-BAXTER LEGACY IN THE MAKING

Robert A. Skitol+

The interplay of economics, jurisprudence and politics has shaped the evolution of antitrust law and policy over the ninety-four years since enactment of the Sherman Act. There are notable examples of this process at work in the Supreme Court's antitrust decisions in the period since the Reagan Administration came into office, appointed William Baxter to the Antitrust Division and began filing amicus briefs designed to persuade a receptive Burger Court to bow to all of the latest Chicago-Stanford antitrust thinking.

Seven decisions in 1982, six decisions in 1983 and five cases pending and to be decided in the next five months all evince the making of a real Reagan-Baxter antitrust legacy. The recent transition to Paul McGrath's stewardship of the Antitrust Division makes it timely to offer some thoughts on the legacy to date, crystal-balling on the case this term, and musings about what it all means for the coming years.

The reality is that over this period the Court has been far more pro-antitrust than the pundits would have us believe. *Seven* out of thirteen decisions have markedly enlarged the scope and application of the antitrust laws; the remaining six have had, at most, an equivocal impact on the law.

To begin, here is a quick run-down on the pro-enforcement side of the ledger:

1. In *Community Communications Co. v. City of Boulder,*[1] the court decided that a municipality's status as a "home rule" entity under state law provided no defense to a Sherman Act challenge to its cable television regulatory scheme. The *Parker v. Brown*[2] "state action" shield was inapplicable to *any* municipality or other government entity below the state itself absent a showing that the challenged actions were in furtherance of a "clearly articulated and affirmatively expressed state policy"[3] to replace competition with regulation or monopoly public service. This ruling is responsible for the filing of close to *one hundred* treble damage suits against local governments in the two years since it came down.

2. In *Jefferson County Pharmaceutical Association v. Abbott Laboratories*[4] the Court decided that purchases by state, county and municipal hospitals for resale through in-house pharmacies are covered by the Robinson-Patman Act, subjecting these entities and their suppliers to price discrimination claims by competing privately-owned pharmacies. In flatly rejecting the long-held assumption that sales to state and local government entities are outside the scope of the Robinson-Patman Act, the Court exposed to treble damage suits more than just government-owned hospitals; the most obvious new Robinson-Patman targets in the wake of this ruling are public university campus bookstores and their suppliers.

3. In *American Society of Mechanical Engineers v. Hydrolevel Corp.,*[5] the Court upheld a Sherman Act claim against a nonprofit standard-making organization for injury to one of its member companies resulting from a competitor's improper use and manipulation of the organization's processes —

notwithstanding the organization's lack of participation in or knowledge of the wrongdoing and the fact that it received no direct or indirect benefit from that wrongdoing. In so holding, the Court opened nonprofit entities and trade associations of all kinds to a broad range of potential antitrust liabilities under a theory of "vicarious" liability for conduct by others acting with "apparent" authority — whatever that may mean. One consideration proffered by the Court in support of its holding was that it would advance antitrust policies to have a rule of law that "encourages" associations of this kind to monitor and police the use of processes and thereby deter anticompetitive uses in the future.

4. In *Arizona v. Maricopa County Medical Society*,[6] the Court condemned as illegal per se a medical insurance plan under which physicians agreed on *maximum* reimbursement levels; that, in the Court's view, was nothing less than a "naked" horizontal price fixing agreement. The Court rejected arguments that a rule of reason analysis was more appropriate in a case involving maximum rather than minimum price levels and involving the health care industry with which the Court had little experience. The Court also gave short shrift to arguments that the fee schedules at issue involved price fixing "in only a literal sense"[7] and that the plan as a whole was a form of productive integration generating procompetitive efficiencies and services. The ruling sent shock waves through health care providers throughout the country, raising antitrust concerns with regard to a host of similar arrangements aimed at cost containment through prepaid or group health plans.

5. In *Union Labor Life Insurance, Co. v. Pireno*,[8] the Court held that a medical insurer's peer review process for determining the necessity of services and reasonableness of charges on policyholder claims for chiropractic treatments was not the "business of insurance" within the meaning of the McCarran-Ferguson antitrust exemption. The chiropractor plaintiffs were thus allowed to proceed with their charge that the peer review process was an unlawful price fixing arrangement, raising new worries about the legality of peer review processes throughout the insurance industry.

6. In *Kaiser Steel Corp. v. Mullins*,[9] the Court allowed an employer to repudiate contractual obligations to make payments into a union's pension fund by raising antitrust objections to the contract after having received the full benefit of the union's compliance with it. This was notwithstanding the hoary principle previously followed in antitrust as well as other contexts that an illegality defense to a breach of contract claim "is a very dishonest one, and it lies ill in the mouth of the defendant to allege it"[10] after having received the benefit of the bargain. The ruling gives employers new ways to use the antitrust laws as an anti-union weapon and gives pension fund trustees a whole new set of problems in collecting monies owing to their funds.

7. In *Blue Shield v. McCready*,[11] the Court upheld the standing of a consumer of psychotherapy services to maintain a class action challenging Blue Shield's refusal to provide reimbursements for the services of psychologists unless they were billed through physicians. The thrust of the challenge was that the restrictions on reimbursement were part of a conspiracy to exclude psychologists from the psychotherapy market. The district court dismissed the complaint on the ground that the plaintiff consumer was

not "within the sector of the economy competitively endangered"[12] by the defendants' alleged violations, making her injury too indirect for standing purposes. The Supreme Court rejected that test as being contrary to Congress' "'expansive remedial purpose'" in creating private remedies under the antitrust laws; the proper test was simply whether there is a reasonable nexus between the alleged injury to the plaintiff and "those forms of [competitive] injury about which Congress was likely to have been concerned in making defendant's conduct unlawful."[14] In so redefining antitrust standing, the Court enlarged the universe of potential private attorneys general and class representatives able to pursue antitrust claims.

There you have them, seven remarkable "pro-antitrust" rulings in this period, all of which open new and enticing profit opportunities for the treble damage plaintiffs' bar. Admittedly, that is not the entire story; there were six other rulings in which the defendants' side came out ahead.

1. In *Associated General Contractors v. California State Council of Carpenters*,[15] the Court held that a union did not have standing to pursue charges against a multi-employer association allegedly engaged in a conspiracy to coerce third parties not to deal with union contractors and subcontractors. While recognizing that the alleged conspiracy might well constitute an antitrust violation, the Court denied standing essentially because "the union was neither a consumer nor a competitor in the market in which trade was restrained"[16] and the alleged injury to the union and its members was simply not the kind of injury the antitrust laws were intended to prevent.

(This decision came eight months after the pro-standing decision in *McCready*. Reading these two decisions together, it would appear that as of today antitrust standing is broadly available to consumers and competitors but skimpily if at all for unions or other kinds of interests.)

2. In *Rice v. Norman Williams Co.*,[17] the Court considered a claim that a California statute prohibiting liquor wholesalers from handling any brand for which they were not "designated" to do so by the brand owner was void on its face as inconsistent with the Sherman Act. The Court rejected the claim, holding that the statute simply facilitated imposition of vertical non-price restraints which were not "necessarily"[18] unlawful as a matter of antitrust law. It recognized, however, that the manner in which a brand owner used the status in practice would be subject to Sherman Act analysis under the *Sylvania*[19] rule of reason.

3. In *Falls City Industries v. Vanco Beverage, Inc.*,[20] the Court importantly clarified and broadened the section 2(b) meeting competition defense to liability under the Robinson-Patman Act. Of most interest is the Court's holding that the section 2(b) defense could be used to justify areawide prices aimed at meeting general competitive conditions, thus interring a line of prior cases suggesting that a seller's section 2(b) burden was to show he was meeting a competitor's lower price on an individualized customer-by-customer basis. This enlarged scope for the section 2(b) defense is "anti-enforcement" in the sense that it will make successful prosecution of Robinson-Patman claims materially more difficult in a wide range of circumstances; whether it is also "anti-antitrust" depends on your own sociopolitical, jurisprudential and theological views about the Robinson-Patman Act and its relationship to the central concerns of the antitrust laws.

We can dispose of the last three rulings briefly since, while they were of obvious importance to the litigants, they do not bear significantly upon antitrust policy development: (4) in *Pillsbury Co. v. Conboy*,[21] the Court scuttled the efforts of private antitrust plaintiffs to compel testimony from witnesses granted immunity during related grand jury proceedings; (5) in *Illinois v. Abbott & Associates*,[22] the Court dashed the hopes of state attorneys general for easy access to federal antitrust grand jury materials; and (6) in *Bankamerica Corp. v. United States*,[23] the Court rejected the Government's bold undertaking (initiated during the Carter Administration but fully supported by the Baxter Division) to apply Clayton section 8 prohibitions to interlocks between defendant banks and insurance companies.

It seems clear to me that the six pro-defendant rulings as a group are far less important or indicative of future directions than the seven pro-plaintiff decisions. Those seven have large ramifications for the next several years of antitrust policy development, as the dissenters so darkly forecast.

Thus, we have Justices Rehnquist, Burger and O'Connor telling us how the *City of Boulder* decision will "impede, if not paralyze, local governments' efforts to enact ordinances and regulations aimed at protecting public health, safety, and welfare, for fear of subjecting the local government to liability under the Sherman Act;"[24] Justices Rehnquist, Burger and O'Connor complaining that the *Pireno* decision "will vastly curtail the peer review process" and thereby eliminate "an aspect of the American insurance industry which has long redounded to the benefit of insurance companies and policyholders alike;"[25] Justices Powell, Rehnquist and White telling us how the *Hydrolevel* decision adopts "an unprecedented theory of antitrust liability . . . with undefined boundaries that could encompass a broad spectrum of our country's nonprofit associations" and impose a "potentially crippling burden of treble damages;"[26] Justices Powell, Burger and Rehnquist fretting that the decision in *Maricopa* condemns a pro-consumer, cost-containment arrangement and thus "loses sight of the basic purposes of the Sherman Act;"[27] and Justice O'Connor, Brennan, Rehnquist and Stevens telling us how the *Jefferson County* decision "will engender significant disruption" including the "possible termination of [medical] services and supplies to needy citizens . . . ."[28] So this Burger Court sure has been stirring things up in an activist way on the antitrust front.

Before cutting through the hyperbole and deciphering what it all means, let us take a look at Mr. Baxter's amicus record, representing his highest priority effort to promote a more enlightened antitrust jurisprudence. The Antitrust Division filed amicus briefs in eight of the cases before the Court in the past two full terms, and its position prevailed in six: in *Hydrolevel* and *Maricopa*, supporting liability holdings; in *Pireno*, opposing McCarran-Ferguson exemption status; in *Rice*, supporting validity of a statute facilitating vertical distribution restraints; in *Associated General Contractors*, opposing the union's antitrust standing; and in *Falls City*, supporting greater flexibility for meeting competition under section 2(b). The two losses are revealing. In *Kaiser*, Baxter opposed allowing the assertion of antitrust claims as a means of repudiating union contracts; this wholly uncharacteristic *pro-union* posture (in a brief filed jointly with the Department of Labor and the NLRB) placed him in the same camp as dissenters Brennan and Marshall who in this instance found themselves caught between their longstanding pro-labor and pro-antitrust leanings. In *Illinois-Abbott*, Baxter urged that freer access for state attorneys general to antitrust grand jury materials is consistent with congressional intent to promote state antitrust enforcement activity; the Court unanimously rejected that view.

Thus, in these cases, Baxter — in ironic contrast to his popular image — was more often than not firmly out in front on the pro-enforcement side of the issues; his strong support for liability holdings in *Hydrolevel* and *Maricopa* and for denial of the insurance exemption in *Pireno* makes him a dangerous gung-ho pro-antitruster in the eyes of the various dissenting Justices. Similarly, while Baxter did not participate in *Boulder*, he has repeatedly applauded the result and dismissed the concerns of mayors across the country about the ensuing avalanche of suits against their localities.

But Baxter's record is not yet closed; heading West, he left behind amicus briefs in the five cases pending this term. And in those papers we get a different and much fuller picture not only of his personal view of what antitrust law and policy should be but, more importantly, of the evolution of antitrust jurisprudence in recent years and its likely continued evolution. The five are *Spray-Rite*,[29] placing in issue the per se rule on resale price maintenance; *Jefferson Parish*,[30] placing in issue the per se rule on tying arrangements; *Copperweld*,[31] attacking the intra-enterprise conspiracy doctrine; *Ronwin*,[32] reviewing the applicability of the state action doctrine to bar examination grading procedures; and *NCAA v. Board of Regents*,[33] raising questions about the applicability of the per se rule to horizontal collaborative activity involving potential efficiency justifications.

These are cases of wide importance; it is useful to understand their historic and policy context. The so-called "Baxter Revolution" of popular renown is *not* a revolution and is also *not* any bunch of new ideas. Baxter is simply the most provocative spokesman for a general philosophy about the antitrust laws that has evolved over several years, in sharp conflict with some central themes in the jurisprudence of the Warren Court. It has steadily gained new adherents and, most significantly, made real headway with the Burger Court. (Note *Sylvania* in 1977 and *Broadcast Music*[34] in 1979; witness the Burger-Rehnquist-Powell-O'Connor dissents in the course of the past two terms; reflect on how further Reagan appointments, say for example a Posner or Bork, would promptly turn that coalition into a strong working majority.)

This general philosophy is at war with "populist" notions about political, social or other non-economic purposes of the antitrust laws. It holds that antitrust's *sole* purpose is protecting and promoting consumer welfare, which in turn necessitates a focus on maximizing allocative and productive efficiency. Proponents believe with a vengeance something the Warren Court often preached but did not follow — that the antitrust laws should "protect competition, not competitors." Competition, they avow, is a spur to efficiency — maximizing output, minimizing costs and stirring innovation. Accordingly, any artificial or unnecessary restraints on competition are anti-efficiency and anti-consumer.

Thus Baxter was a tiger on bid rigging because horizontal collusion dulls incentives to become more efficient; and he strongly supported a liability holding in *Hydrolevel* because industrywide association activities can become cloaks for suppressing competition and industry standards can stifle innovation. On the other hand, he has urged easing the bans on vertical restraints because vertical controls by a manufacturer over its distributors often facilitate aggressive competition with other manufacturers and, therefore, should not be condemned unless shown to lessen competition among those manufacturers. In Baxter's view, antitrust rules hostile to vertical controls of that kind are misguided efforts to protect competitors (dealers and others along the distribution chain) rather than the competitive process.

Under this philosophy all forms of horizontal collaboration require close scrutiny, but care must be taken to distinguish between "naked restraints" like pure price fixing and other arrangements involving efficiency promoting integration of productive or distributive functions (mergers and joint ventures but also looser collaborations as well). Unthinking or kneejerk applications of rules of per se illegality to horizontal arrangements in general are considered a misdirected attachment to labels without appreciation of underlying economic realities.

This concern is evident in Baxter's amicus brief in *Maricopa*; while he urged the Court to strike down the physician collaboration involved in that case, he reached that result only after what he described as a "*limited* rule of reasons analysis" convinced him that the collaboration was unnecessary to any efficiency-producing integration of productive capacity. Thus, he may well have been less than happy with the Court majority's per se approach. He surely disapproved the majority's repeated citations to *United States v. Topco Associates*[35] (the 1972 decision condemning as per se illegal a market division among grocery chains marketing private label products); in 1979, then-Professor Baxter pilloried *Topco* as "one of the most perverse [decisions] in the history of antitrust" because, in his view, it involved the kind of horizontal arrangement likely to produce *both* procompetitive and anticompetitive effects and thus deserved careful scrutiny under a rule of reason balancing process. That, in fact, was the posture taken by Chief Justice Burger in his *Topco* dissent; and in *Maricopa* he and Justice Rehnquist joined with Justice Powell in arguing for a rule of reason approach to the horizontal price collaboration there at issue.

It is of some interest that Justices Blackmun and O'Connor did not participate in the *Maricopa* case; one and perhaps both might well have gone along with the dissenters, thereby changing the outcome or at least the tone of the decisions. Justice Blackmun, incidentally, filed a concurring opinion in *Topco* reflecting discomfort with the rigidity of a per se approach to arrangements of that kind, so he as well as Justice O'Connor would seem more in sympathy with the dissenters than the majority in *Maricopa*. All of which is worth some considerations if you are inclined to bet on the outcome of the *NCAA* case this term, as discussed below.

While proponents of this philosophy would make the substantive rules of the game a lot more flexible than indicated in many of the past precedents, they would like to see those more flexible rules applied on a universal basis with only rare exceptions involving market imperfections or "natural monopoly" situations. Thus, Mr. Baxter and his fellow travelers have strongly supported deregulation in the transportation, telecommunications and financial service sectors, believing antitrust exemptions for these industries no longer justified (if indeed they were ever justifiable). Similarly, they support narrowing the scope of other statutory exemptions, like the McCarran-Ferguson exemption for insurance; that explains why Baxter was a strong booster of the outcome in *Pireno*. (It is worth noting that this *Pireno* brief emphasized that the Department believes peer review processes for insurance claims should be assessed under a rule of reason analysis, so that denial of exemption status would not necessarily make them illegal; the brief did, however, strongly object to exemption status for such activities.)

Baxter and his brethren also regard government bureaucurats at all levels as mortal enemies of both efficiency and competition. This explains their approval of the *Boulder* decision and lack of sympathy for the plight of mayors suddenly brought into the antitrust world. Baxter did not participate in *Jefferson County* and I have not seen any indication of his views on the Court's ruling but I suspect he was ambivalent; on the one hand he would not like the idea of government-owned hospital pharmacies competing with private pharmacies but not being subject to the same set of antitrust strictures; on the other hand he has made no bones about his antipathy to the Robinson-Patman Act. His amicus brief in *Falls City-Vanco* made that clear; and the expansion of the meeting competition defense in that case is consistent with the general view that a strict construction of the Robinson-Patman Act gets in the way of vigorous, unrestrained and efficiency-enhancing price competition.

Now to the five all-important cases to be decided this term. Here is my Fearless Forecast:

1. *Monsanto Co. v. Spray-Rite Service Corp.* has received most of the attention of the bar and the press because it is Baxter's vehicle for urging that the Court overrule the hoary *Dr. Miles*[36] per se rule on resale price maintenance. You will recall that late last year Congress attached a rider to the budget for the Department of Justice having the effect of a gag order — barring Baxter from repeating at the oral argument in this case what he said in his brief several months earlier: that resale price maintenance is not really all that bad and may in fact be procompetitive (generating *efficiencies* in distribution and thus advancing interbrand competition and consumer welfare), and that the existing state of the law under which nonprice vertical restraints receive rule of reason treatment while price-related vertical restraints receive per se treatment is anomalous and mischievous. Since that position *is* laid out in the Department's amicus brief, there is no need to fear that the gag order somehow deprives the Court of the benefit of Baxter's thinking. On the other hand, the gag order does underline the fact that Congress still thinks *Dr. Miles* was a bad guy and a good decision. This latest expression of congressional intent with regard to that per se rule probably tips the scales against its repudiation by the Court at this time.

On the other hand, I believe it likely that the Court's disposition of other issues involved in the *Spray-Rite* case will beneficially clarify the law and eliminate application of the per se rule in situations where it makes the least sense. The facts in the case are simple: Monsanto refused to renew Spray Rite's contract a year or so after receiving price-related complaints from competing distributors. Based on those facts, the lower courts permitted a jury to find "concerted" action to eliminate price cutting and an overall conspiracy to maintain prices. The Department and Monsanto contend that the bare facts of a termination at some point after receipt of complaints should *as a matter of law* be deemed insufficient evidence of concerted action for purposes of section 1; and, in addition, that the bare allegation that a termination was price-related should as a matter of law be deemed an improper basis for allowing a jury to find resale price maintenance and per se illegality. My Fearless Forecast is that the Court will buy those points; the per se rule will stay in place but its misuse by the lower courts will be curbed.[37]

2. *Jefferson Parish Hospital District No. 2 v. Hyde* is the other "vertical" case on the docket. Here the Department asks the Court to overrule the per se standard for tying arrangements. (There has been no Congressional fuss over this one.) Again, the facts are simple. The Hospital defendant entered into an exclusive contract for anesthesia services with an outside group of anesthesiologists and the plaintiff independent anesthesiologist was thereby denied staff privileges. He challenged the contract as an unlawful tie-in — the tying product being hospital surgery and operating facilities and the tied product being anesthesiology services. The Fifth Circuit bought that characterization and, after finding that the hospital possessed "market power" in the tying product (based on a questionable market definition), held the arrangement to be illegal per se.

The Department's amicus position, as well as the hospital's position on these issues, is that the arrangement at issue was mischaracterized; it is nothing more than exclusive dealing and thus subject to analysis under the rule of reason. Moreover, they note, even if the tie-in label is accepted, the Fifth Circuit misapplied existing tie-in law; the standard is per se in name only, because *Fortner II*[38] requires an assessment of "market power" in the tying product within a realistically defined relevant market and also requires economic analysis and consideration of possible justifications before determining that there are two separate products involved. The Department would, however, also bypass all such convoluted analysis; it invites the Court now to repudiate the whole per se rule. In the Department's view, this case exemplifies how nominal tie-ins can be procompetitive, enhancing efficiency and consumer welfare. It also shows, the Department asserts, why it is senseless to have a rule of reason for exclusive dealing but a harsher per se rule for functionally and conceptually similar tie-ins.

My Fearless Forecast here is that this case will end up like *Spray Rite*; the Court will refrain from radical surgery on the per se rule but will beneficially clarify the law to eliminate perverse applications of it to facts like those involved in this case. The Court will agree that the specific arrangement at issue should be analyzed as exclusive dealing subject to rule of reason treatment; it will also comment upon the tie-in analysis applied by the lower court and, in so doing, amplify upon the *Fortner II* requirement that there be a *meaningful* showing of market power in the tying product as a prerequisite to finding illegality.

3. *Copperweld Corp. v. Independence Tube Corp.* is the occasion for a frontal attack upon the "intra-enterprise conspiracy doctrine." It comes to the Court from a Seventh Circuit affirmance of a jury finding that Copperweld and one of its wholly-owned subsidiaries conspired to block another firm's

entry into their market in violation of section 1 of the Sherman Act. A line of Supreme Court decisions that began with *Yellow Cab*[39] in 1947 permit a jury to find that a parent and subsidiary are capable of "conspiring" for section 1 purposes, at least in some circumstances such as when the entities operate with a high degree of independence from each other. That was the story in this case.

The Department's amicus brief urges that the Court re-examine and reject that doctrine. In the Department's view, the doctrine has fomented confusion and mischief, mainly by allowing section 1 standards for concerted activity to be applied to conduct that should be governed by the more flexible section 2 standards for unilateral conduct. Once again the Department's main concern is that efficiency-generating conduct is being deterred to the consumer's detriment because of misguided application of strict section 1 standards to *so-called* "conspiracies" between two or more parts of a single economic enterprise. That, to the Department, is a classic instance of form over substance and disregard of economic realities.

My Fearless Forecast is that the Court will follow the Department in this case. At a minimum it will clarify when the intra-enterprise conspiracy doctrine applies and when it does not, thereby alleviating the confusion among the lower courts. Actually, I believe the doctrine will be largely gutted, left for application to situations involving *loose* affiliations between or among entities with significant independent existence and interests.

4. *Hoover v. Ronwin* is a bar applicant's challenge to an admission committee's alleged manipulation of examination grading procedures for anticompetitive purposes, artifically limiting annual admissions on grounds unrelated to applicants' competence. The district court dismissed the complaint on the ground that the Committee's grading policies were immune state action. The Ninth Circuit reversed on the ground that it was not shown that the Committee's alleged restraint of trade was "clearly articulated and affirmatively expressed as state policy."[40] In the Supreme Court, the Department's amicus brief strongly endorses the Ninth Circuit's ruling. Its brief reflects strong agreement with the *Boulder* decision and a desire to see the *Boulder* standard enforced in full. On the apparent facts of this case, denial of immunity seems unarguable. The only state policy evident in the record is a policy of ensuring attorney competence; that hardly translates into authority to limit competition in the interests of protecting the pecuniary interests of the incumbant bar. My Fearless Forecast is that the Court will affirm the Ninth Circuit and reaffirm the limitations on state action immunity specified in *Boulder.*

5. *NCAA v. Board of Regents* is the occasion for a reexamination of the standards applicable to horizontal arrangements possessing potential efficiency justifications, or "loose" joint ventures. This is a murky area, particularly in the wake of *Maricopa* with its per se holding three years after *Broadcast Music* with its rule of reason holding for arrangements in this category. The case comes up on a challenge to the whole process under which the NCAA sells broadcast rights for college football; the association acts as the common and exclusive selling agent for all member schools, selling package deals and then distributing revenues to the members on a uniform basis. Under the rules of the association, individual schools are barred from

selling rights to any of their games outside the official NCAA package or from negotiating higher or lower prices for games within that package.

After a full trial on the merits of section 1 claims by two member schools seeking freedom from these restraints, the district court held the arrangement to be illegal per se; alternatively, after examining the evidence offered in support of asserted justifications relating to the need to maintain team balance and promote live attendance, the court found the restraints also unlawful on rule of reason grounds. The Court of Appeals affirmed, and the Supreme Court now has before it both the per se and the rule of reason holdings below.

In the first amicus brief filed by the McGrath Antitrust Division, the Government urges the Court to repudiate per se treatment for horizontal arrangements of this kind while at the same time avoiding full-blown, open-ended rule of reason inquiries for them. Instead of either of those extremes, the McGrath brief suggests various intermediate approaches to assessing what are described as facially suspect but potentially justifiable price collaborations and output restrictions. Limited or "truncated" rule of reason inquiries, "initial looks" at proffered efficiencies, rebuttable presumptions and burden-shifting, "abbreviated" assessments of whether the restraints are "reasonably necessary" to efficiency-promoting elements of the plan, all express the concept that efficiency arguments should be considered in some way but need not engender lengthy trials. The Department supports invalidation of the NCAA rules at issue because the evidence shows they are not necessary to efficiency-enhancing association activities; but it disapproves of the per se holdings below and also believes that an open-ended rule of reason approach in such cases is unnecessary and undesirable.

My Fearless Forecast again is that the Court will endorse the thrust of the Department's position on the issues. That is to say, the Court will fashion a standard more flexible than per se but less all-encompassing than rule of reason, building upon the hints and suggestions of that approach in its prior cases. And in the process, the Court will "reinterpret" *Maricopa* to make it consistent with the new standard adopted in this case. That will happen because all nine Justices are now addressing these issues, including Justices O'Connor and Blackmun who recused themselves from *Maricopa* but who almost surely share the *Maricopa* dissenters' discomfort with per se treatment of novel joint venture arrangements.

I conclude with one sweeping conclusion: The Burger Court is avowedly and firmly pro-antitrust, but its conception of what antitrust law and policy should be and should not be is increasingly influenced by and consistent with the Baxter-McGrath, Posner-Bork, Chicago-Stanford, efficiency-based, consumer welfare view of the world. And its decisions in the five cases pending this term will reflect that philosophy more fully and openly than have any rulings since *Sylvania*, the Magna Carta of this ascendant school.

FOOTNOTES

\+ Wald, Harkrader & Ross, Washington, D.C.
1. 455 U.S. 40 (1982).
2. 317 U.S. 341 (1943).
3. *City of Boulder*, 455 U.S. at 52.
4. 103 S. Ct. 1011 (1983).
5. 456 U.S. 556 (1982).
6. 457 U.S. 332 (1982).
7. *Id.* at 355.
8. 458 U.S. 119 (1982).
9. 455 U.S. 72 (1982).
10. *Id.* at 90 (Brennan, J., dissenting((quoting McMullen v. Hoffman, 174 U.S. 639, 669 (1899)).
11. 457 U.S. 465 (1982).
12. *Id.* at 470 (emphasis deleted).
13. *Id.* at 472 (quoting Pfizer Inc. v. Government of India, 434 U.S. 308, 313 (1978)).
14. *Id.* at 478.
15. 103 S. Ct. 897 (1983).
16. *Id.* at 909.
17. 458 U.S. 654 (1982).
18. *Id.* at 661.
19. Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977).
20. 103 S. Ct. 1282 (1983).
21. 103 S. Ct. 608 (1983).
22. 103 S. Ct. 1356 (1983).
23. 103 S. Ct. 2266 (1983).
24. 455 U.S. at 60.
25. 458 U.S. at 140.
26. 456 U.S. at 578-79.
27. 457 U.S. at 367.
28. 103 S. Ct. at 1032.
29. Monsanto Co. v. Spray-Rite Serv. Corp., 52 U.S.L.W. 4341 (U.S. Mar. 20, 1984).
30. Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 104 S. Ct. 1551 (1984).
31. Independence Tube Corp. v. Copperweld Corp., 691 F.2d 310 (7th Cir. 1982), *cert. granted*, 103 S. Ct. 3109 (1983).
32. Ronwin v. State Bar, 686 F.2d 692 (9th Cir. 1981), *cert. granted sub nom.* Hoover v. Ronwin, 103 S. Ct. 2084 (1983).
33. Board of Regents v. National Collegiate Athletic Ass'n, 707 F.2d 1147 (10th Cir.), *cert. granted*, 104 S. Ct. 272 (1983).
34. Broadcast Music Inc. v. Columbia Broadcasting Sys., 440 U.S. 1 (1979).
35. 405 U.S. 596 (1972).
36. Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).
37. On March 20, 1984 the Supreme Court denied the *Spray-Rite* case, 52 U.S.L.W. 4341. The court refused to consider the issue of the continuing validity of the *Dr. Miles* rule condemning resale price maintenance as per se illegal, noting that this issue was not raised by either of the actual parties to the litigation, and had not been argued or decided below. *Id.* at 4343 n.7. As Mr. Skitol predicted, the Court held that mere proof of dealer termination following complaints by other dealers to the distributor or price cutting by the terminated dealer was not sufficient as a matter of law to allow a jury to find an unlawful resale price maintenance conspiracy. In order to justify such a finding, the Court stated that there must be "evidence that tends to exclude the possibility that the manufacturer and non-terminated distributors were acting independently," *id.* at 4344, which evidence "reasonably tends to prove that the manufacturer and others had a conscious commitment to a common scheme designed to achieve an unlawful objective." *Id.* at 4345. The Court held that although the Seventh Circuit had applied the wrong standard in judging Monsanto's actions, there was nonetheless sufficient evidence to justify the jury's finding that Monsanto had been engaged in an illegal conspiracy with its dealers under the correct standard, and thus affirmed the decision below. [EDITOR'S NOTE]
38. United States Steel Corp. v. Fortner Enters., 429 U.S. 610 (1977).

39. United States v. Yellow Cab Co., 332 U.S. 218 (1947).
40. Ronwin v. State Bar, 686 F.2d 692, 697 (9th Cir. 1981), *cert. granted sub nom.* Hoover v. Ronwin, 103 S. Ct. 2084 (1983).

CHAPTER 3
MERGERS AND ACQUISITIONS

Eleanor M. Fox+

WALTER BARTHOLD: We have a lot of material to cover, so I shall begin now with a very brief anecdote of an interview I had a year or two ago with a state court judge here in New York. As we closed the interview, we chatted about this, that and the other thing. He asked me what kind of trial work I did. I said I did a certain amount of antitrust work.

He said, "Oh good. I've always wanted to meet an antitrust practitioner. Maybe you can answer a question that has puzzled me for many, many years."

I said, "Sure. What is that?"

He said, "What ever on earth is the Herfindahl Index?"

(Laughter)

Well, our next speaker will do a far better job of telling you what the Herfindahl Index and many other things are than the job I did for that state court judge.

If I were to give our next speaker the introduction she deserves, there would be no time left for her to talk. Suffice it to say that she is a living refutation of the adage of the late George Bernard Shaw that "those who can, do, and those who cannot do, teach."

Our next speaker is a former partner in and present counsel to the firm of Simpson Thacher & Bartlett and also professor of law at the New York University Law School. She is a former Chairman of this Section, a member of President Carter's National Commission for the Review of Antitrust Laws and Procedures, a former member of the Executive Committee of the Association of the Bar of the City of New York, the author of more books and articles than most of us (including myself) have written briefs, and on top of all that a novelist.

I take pleasure, ladies and gentlemen, in introducing to you Professor Eleanor Fox, who will talk about mergers.

Eleanor M. Fox

I. Introduction

About two weeks ago you may have seen an article in the *New York Times* that was called "Frenzy and Style in the Merger Boom."[1] It reported, among other things, that in 1983 73.5 billion dollars were spent on mergers. And it was quick to go on to say that that does not include lawyers' fees.

Takeovers are very big. They are as big as ever. "Shark proofing" and "poisoned pills" are very popular, but unlike the merger boom of the late 1960's, the antitrust reporters are not filled with merger cases.

It is obvious why we have a relatively low level of merger enforcement. Bob Skitol has given you some reasons, which I will relate more specifically to the merger context.

The government's theory and philosophy of merger enforcement today has shifted into a realm that some people might call consumer welfare but I might call laissez faire. I will articulate what I believe the government's policy and philosophy to be, and as I go along I will relate this to the merger law.

First. on policy shifts. How does 1984 compare with. say. ten years ago and before?

About ten years ago and before. we had some relatively simple concepts that did not require as many economists and as large economists's bills as we pay today. Then a market was any distinct good in any distinct section of the country. That was one market. If the parties to the merger produced two different distinct goods that competed with one another. a description that included both goods was also a market.

In analyzing the substance of competition and the competitive effects of horizontal mergers. if the merger was between two significant competitors in a concentrated or concentrating market. it was probably illegal. As for vertical mergers — mergers of buyer and seller pairs — if the market at least at one level was concentrated with barriers to entry and the buyer and seller pair each had significant percentages of its markets. and if the good supplied by one partner to the other was scarce or complex. it was probably illegal. On potential competition grounds. which usally comprises potential horizontal mergers. if the market was concentrated or concentrating. if the acquiring company was one of the few entrants. and if it was acquiring a leading firm in the market. the merger was probably illegal.

The law then generally reflected Congress' desire to stem increases in concentration. The case law defined competition in terms of rivalry among a significant number of competitors. And the Supreme Court cited those economists that tended to link increasing concentration with lessened competition.

Today we have moved into a new mode. At least in terms of government enforcement. the enforcement mode is noninterventionist. The government policy is that no merger should be challenged unless the merger is inefficient — that is. unless the merger will cause society to lose scarce resources.

Inefficiency is defined in terms of output restraints. Even "output restraints" must be qualified because if the merger causes a loss of resources from output restraint but actually saves more resources from productive efficiency, the merger is not allocatively inefficicient and government enforcers might want to support the merger rather than oppose it.

Output limitation can be achieved only in one of two ways — by monopoly or a firm on its way to monopoly, the leading firm model; or by collusion. Mergers might facilitate collusion if there are few firms in the market and. given a lot of other necessary conditions. it can be predicted that the firms are likely to behave cooperatively rather than rivalrously.

The government enforcers define competition in terms of efficiency. That which is efficient is deemed procompetitive.

This does lead to minimal antitrust. If you have to make a concession to the fact that the merger law exists, how could you define antitrust to warrant the least government intervention against mergers? Well, the way to do it is to say, "We'll only attack mergers that are inefficient." That is the policy today.

That is by way of background. I want now to turn to a couple of preliminary issues — number one, environment for and opportunities for settlement; number two, a word about preliminary injunctions. And then I want to go on to substantive analysis — analysis of market definition and analysis of effect on competition given the defined market. Under effect on competition, I will deal with horizontal, potential horizontal (which includes the potential competition cases) and, briefly, vertical mergers.

II. Opportunities for Settlement and Negotiation: New Ways of Looking at the World

The environment for settlement is very good. The environment for (1) inducing the government not to sue at all, and (2) inducing the government to give its okay if the merger parties do something like a small spin-off, is very, very good.

There are many transactions that have only a small offending portion, a small offending overlap that might violate the horizontal standards. In those cases the government definitely encourages parties to get rid of offending overlaps before doing the deal and before it will okay the deal. Except — and there is one exception that has been mentioned by the Justice Department over the last year or two — where there is a hostile takeover, the acquiring company has no power to get rid of offending overlap at the outset and the government will listen hospitably to promises of getting rid of the offensive overlap after the merger is consummated. The government's agreement usually comes in the following form: the government files the complaint and the proposed consent order on the same day.

There are a number of examples. One example I will mention does not fit the "settlement beforehand" construct, but it illustrates the possibilities.

You will remember Mobil's attempted takeover of Marathon. The FTC belatedly and perhaps reluctantly sued; but in its very complaint, it gave a blueprint of how Mobil could get rid of offending overlap and validate the merger.[2] Mobil wanted Yates Field. Yates Field was rich in oil reserves. The offending overlap was in marketing. Thus, the FTC complaint showed how Mobil could avoid the strictures of the law by divesting some marketing assets.

Du Pont-Conoco is another example. And, incidentally, I would count *du Pont-Conoco* as a point along the general proximate cause chain tripped off by Mobil's pursuit of Conoco, which rushed into the arms of du Pont, then Mobil's pursuit of Marathon, which fell into the arms of U.S. Steel. When du Pont decided it wanted to take over Conoco — du Pont was the white knight and they were both happy — there was offending overlap. Du Pont and Monsanto were joint venturers to make a chemical that competed with Conoco's business. The Justice Department filed a complaint and consent order on the same day, and pursuant thereto the companies undertook to get rid of the offending overlap. One of the joint venture partners would sell out its share of the joint venture.

Another example, which I shall mention only briefly because it is not within my jurisdiction today, is the General Motors-Toyota joint venture to make a small car in the United States. *General Motors-Toyota* presented similar opportunities for settlement. The FTC and the companies reached a consent order agreement that would restrict the scope and output of the joint venture, limit its term to twelve years, limit the flow of sensitive information, and impose some reporting requirements.[3]

Of course, it is even better for the merging parties when you can convince the government not to sue at all; and this is happening very frequently with respect to deals that would probably have faced immediate challenge some years ago. An example is SCM, an important producer of titanium dioxide. It wanted to buy a couple of plants from Gulf & Western, which also produced titanium dioxide. Under traditional analysis, one would have looked at the market (there were only a few principal sellers), and one would have counted up the market shares. If you asked: What percentage of all sales made in the U.S. market is accounted for by each of the companies, you would get market percentages of about 15 percent for SCM and eight percent for Gulf & Western; and that would, under the old traditional analysis, raise questions.

Well, you may have noted in the BNA last November that the companies convinced the Federal Trade Commission not to move for an injunction.[4] They did so on two grounds. One was economic analysis showing that the parties after the merger would not gain an increment in power over price that would enable them to lessen output. They proved to the satisfaction of the FTC that this acquisition was not output-limiting. That was because, if the merged parties tried to raise price and even if the other domestic firms followed, the higher price would attract so much foreign output that the domestic firms could not profitably hold the price rise. Thus, the parties showed to the satisfaction of the FTC that the merging firms would not gain an increment in power over price because of foreign competition. Also, they presented a strong case of productive efficiencies. The FTC's receptivity indicates that the agencies may be inclined today to weigh favorably clear proof of productive efficiencies, despite the fact that there is no existing "efficiencies" defense.

As a third point on opportunities for settlement, I should mention the fact that there are and always have been special equities, such as the failing condition of a company. Special equities might induce the government not to sue.

Interestingly, since our present enforcers are interested in efficiency and not in shareholder equity or most community equity, the failing company defense might not be accepted by the enforcers in those cases where the acquisition gives the acquiring company increased market power — an increment in power to raise price and lower output. There are some cases in which a failing condition reflects that the company is about to become a non-entity; it is simply not a force in competition. There are other cases in which an acquiring company — which might be a major one in its field — may gain the rest of available capacity, and the acquistition could give the acquiring company increased power over price. The Justice Department has said in its Merger Guidelines that where the acquisition of a failing company would lead to inefficiency (increase power to raise price and lower output), it is not going to recognize the failing company defense.[5]

III. Preliminary Injunction

For the most part, the law today remains as it has been for a long time. The Justice Department, of course, has power to move under section 15 of the Clayton Act,[6] and it is entitled to a preliminary injunction if it proves reasonable likelihood of success on the merits and a balance of the equities in its favor. Irreparable harm, which is an element of the case, is proved by the government's showing a reasonable likelihood of success.

The FTC has the power to move for preliminary relief under section 13(b) of the Federal Trade Commission Act,[7] which provides that an injunction should issue if on weighing the equities and considering the likelihood of success, the relief is in the public interest. There has has been a relatively new twist in the FTC injunction law. In *FTC v. Weyerhauser Co.*,[8] decided by the D.C. Circuit in 1981, the FTC staff proved to the satisfaction of the court that the merger was probably likely to lessen competition. Nonetheless the court held that the equities of the stockholders and the communities were paramount and, in addition, it thought production would be increased in markets not subject to the antitrust challenge. The court refused to grant the injunction.

I think that case is really a straw in the wind. But it certainly does show the room for good lawyering and convincing advocacy.

Finally, as to private party injunctions, private parties can sue for a preliminary injunction against a merger under section 16 of the Clayton Act.[9] Most of these cases are takeover cases. The target is threatened and the target wants to survive and to defeat the tender offer.

For a number of years the courts looked hospitably or neutrally to targets' actions under the antitrust laws to prevent takeovers. But then came *Missouri Portland Cement Co. v. Cargill, Inc.*,[10] which was decided by the Second Circuit in 1974. Judge Friendly said, for the court, that a target company's antitrust suit is like "[d]rawing Excalibur from a scabbard where it would doubtless have remained sheathed in the face of a friendly offer."[11] He and his court looked hostilely on targets' motions for a preliminary injunction. He said, for the court, that section 7 was not meant to endow incumbent management with the power to take a free ride and prevent the free trading of securities. Rather, the private party had a heavy burden to show a clear violation of the antitrust laws in order to get preliminary relief.

Despite *Missouri Portland*, plaintiffs still have good opportunities to win preliminary injunctions. *Mobil Marathon* is an example. Marathon prevailed against Mobil, suing in the district court in Ohio where Ohio was trying to save its home industry — a very nice equity indeed.[12]

One detail that I shall no more than mention is Hart-Scott-Rodino. There are, of course, pre-merger notification and filing requirements. I thought it would be somewhat more entertaining for you to read about Hart-Scott-Rodino than for me to speak about Hart-Scott-Rodino. I have covered it in my merger book with my husband, Byron, at Chapter 20B[13] and Steve Axinn has covered it throughout his book on Hart-Scott-Rodino.[14]

IV. The Substantive Law and the 1982 Justice Department Guidelines

A. Market Definition

Let me turn now to substantive issues. I shall start with market definition and with the Guidelines' theory of markets.

The Guidelines have a very neat theory of markets which fits precisely with the government theory of challenging only inefficient mergers.

If within a defined market a single hypothetical firm could artificially raise price by (e.g.) five percent over the current level and hold that price increase in the face of whatever shifts buyers would make to alternative products and whatever shifts sellers would make to divert the same product into the relevant geographic market or to make the relevant product, then the hypothesized area is a market.[15]

Suppose, for example, that two cement producers in a Western region relatively close to one another want to merge. How do you go about defining the market?

Well, of course, you have your product dimension *and* your geographic dimension. You take your product. The product is cement. You ask, if the price of cement were to rise artificially by five percent, what would buyers do? Would there be demand substitutability? That is, would buyers substitute something else for cement, and to what extent? Would they substitute brick or wood or other alternatives? If demand would shift to a considerable extent, that would probably beat back the attempted price rise.

I would think that the anwer is probably no: that there demand substitutability is not sufficient to beat back the hypothesized rise of cement. Let's assume this to be the case.

A next question is, can firms making a related product shift quickly and easily to make cement? If so, the guidelines ask: which firms would do this within six months? That is, which firms would have the profit incentive to do so?

Any firms that would probably shift to the production of cement within six months would be counted as producing the product within the market.[16] The Guidelines would count as within the market the production that they would bring into the market within a year. This concept is production substitution.

Now, geography. We take the two cement firms that are merging and their immediate competitors. If they should artificially raise price five percent, what will more distant sellers do? Will more distant sellers divert product into the market?

If the answer is yes, the Guidelines say, you include in the market the product that those more distant sellers would, within one year, sell into the market to the customers of the firms that you started out with.[17] And that's your market definition.

After this process, you should have a market. The market should include all near price constraints, so that a hypothetical single single seller in the area would be able profitably to raise price.

If you have included all near price constraints within the market, then the percentage shares that you attribute to the incumbents in the market are meaningful in the sense that you can predict that certain very large shares will lead to probabilities of collusion. "Collusion" is used in the sense that the firms will recognize that they will profit more from cooperative behavior than from rivalrous behavior. They don't have to be sitting around the table in a smoke-filled room.

Let me talk about application of these Guidelines. I mentioned before SCM and G&W. We talked about titanium dioxide and foreign competitors. You might have said: "This is a world market. What we should do is see what SCM sells in the world." The Guidelines, as well as Landes and Posner and many other economic thinkers, are not taking that route. They are starting from a different point but are trying to capture the pressure from the foreign producers just the same. Where sales are at least on a national basis, they would hypothesize the United States as a market. The Guidelines would hypothesize a single seller, raise price hypothetically five percent, and observe what would probably happen in view of the fact that the United States now becomes the best marginal profit opportunity for geographically distant sellers.

In *SCM-G&W*, a stream of imports would come in from the foreign producers. You would include that product in the market. This will dilute the market shares of the incumbents and the market share figures might then appear much lower than they had appeared before.

The government model can, however, be somewhat difficult to apply. An enormous number of assumptions may have to be made, and they may not reflect reality.

Let us look for a moment at *United States v. Virginia National Bankshares*[18] and the government's assumption that people and firms do, and rather quickly do, take their best profit opportunities.

In *Virginia National Bankshares*, two banks in different towns in the same county wanted to merge. The government here was using the Guidelines offensively, although it is probably the case that the Guidelines most often help defendants. But here the government was saying this: there are two banks, each in a different town, but both in the same county. The county is the market. To try to establish this proposition, the government sent out a questionnaire. By the questionnaire the government sought to find out whether if Bank A and banks in its town raised price by five percent, people would flow to the banks in the other town, Big Stone Gap, and give them their business. On the basis of its investigation, the government concluded that the answer is yes, they would. Therefore, the two towns were one market.

Well, there were witnesses at the trial — banking witnesses and other people who knew the community and the people's habits. Banking witnesses testified that the people and the bankers perceived these towns as two different markets. Among other things, roads got snowy and icy during the winter and people were not about to ride from one town to another. And one bank manager testified that she offered a half point higher interest than the banks in Big Stone Gap and yet she was unable to entice the people from Big Stone Gap to come to her town.

Ater hearing what people thought, the court held that the banks were in two separate markets.

My next question is, how does the law view the economic models and the hypothetical questions that the Guidelines require?

I think that the law does not view the model too warmly and has resisted it. The law continues to perceive markets as snapshots of existing patterns of trade. As a practical matter, one thing you should do is look at the existing patterns of trade and establish market shares the way we always have: Of all sales in this area, how much does Company A account for? Asking the hypothetical question — if prices should rise five percent what would the shares be — is not enough.

I think you should do it both ways. I think you should document existing market patterns, and you should also ask: if prices were raised artificially by five percent, what would the patterns look like? By asking the second question, you are able to ascertain the extent of price pressure on your snapshot market from pressures outside of the snapshot market.

Product maket is still defined by what products are reasonably interchangeable with the merging firms at the current product price. There was a time back in the 1960's for example, when courts took greater liberties. You might remember Justice Fortas' dissenting opinion in *Grinnell* when he called the accredited central station service market a "strange red-haired, bearded, one-eyed man-with-a-limp classification."[19]

Red-haired, bearded, one-eyed man-with-limp markets are out. They are not accepted in law anymore because they exclude that which is reasonably interchangeable to buyers.

Geographically, the Supreme Court's statements — even rather recent statements — do not dovetail with the Guidelines' hypotheticals. The geographic market is, says the Court, where the merging parties sell and where their customers could easily turn.

All of this leads to what I call the snapshot market — market shares as they are, without hypothetical questions. Nonetheless, the hypothetical question is important and it has been important for a number of years. In *Philadelphia National Bank*[20] the Court talked about discounting and shading because international competition might have put pressure on bank rates in Philadelphia. There, the Court did not do very much with this pressure factor but the Court's acknowledgement of the concept may be a forerunner to discountng the snapshot shares.

B. Assessing Effects on Competition

1. Horizintal Mergers

Let us turn to assessing effects on competition, assuming a well-defined market. We will start with horizontal mergers.

Horizontal mergers is where all the action is. Apart from horizontal and potential horizontal mergers, there is almost no action at all. That is because there must be restraint on a horizontal level to lead to ouput limitation, which is now the only concern of government.

The Guidelines give us guides from the Herfindahl Index. Herfindahl, incidentally, was working on a dissertation on the steel industry at Columbia at the end of the 1940's. He set about to show that, after the initial spate of steel mergers in the very early 1900's, U.S. Steel lost market power, and that there was not increasing concentration, such as would lead to inferences of market power, in steel. He thought this was probably true of many other industries and that probably the notion on which the Celler-Kefauver Amendment was based — that there was rampantly increasingly industrial concentration — was wrong.

To measure concentration and changes in concentration over time, he devised the index which the Guidelines use. He never said that any level of concentration was bad. He simply said that at very high levels of concentration one must look further to see if the parties might have incentives to behave cooperatively.

Herfindahl used many qualifying statements cautioning that one should not rely too heavily on measures of concentration. He would not form policy on the basis of it. And he would probably be rather surprised to see 1000 and 1800 given rather precise policy meanings[21] but that is the way our Merger Guidelines have gone.

The Guidelines are based predominantly on oligopoly theory. (They are also based on single-firm market power theory, but oligopoly theory is the strongest element in the Guidelines.) This surprised a lot of people because oligopoly theory is old. It was a center for antitrust thinking in the 1940's and the 1950's and was very popular in the 1960's. Many people were surprised that the Justice Department, after deliberating for so long and after downgrading market structure as a prediction of performance, should come out with guidelines based on oligopoly theory.

Oligopoly theory is simply this: when there are very few companies in a market, especially if their costs are similar, buyers are small and numerous, there are no serious pressures from outside (like foreign competition), and barriers to entry are high, the companies are likely to profit-maximize prices and behave cooperatively rather than rivalrously. If they behave rivalrously, they will all have to drop their prices and they will all lose. If they behave cooperatively, they will all have higher profit margins and they will all win. As firms become too numerous (more than ten or twelve) or other factors change, collusion is not likely because (1) the firms will not be able to reach a consensus price, and moreover, even if they could, (2) too many colluders would successfully cheat from the cartel without detection and this would so undermine the cartel that it would self-destruct.

That is the theory. It has a lot of qualifications. It purports to be the basis of the Merger Guidelines. But I just want to plant this seed: that although oligopoly theory is said to be the basis of the Merger Guidelines, perhaps all that the government is telling us is, "Below a certain concentration level, don't worry; above a certain concentration level, look further;" just like Herfindahl said. That, however, is not the way the Guidelines read. When, then, does level of concentration flag concerns?

The Herfindahl Index is calculated by taking the market share of all firms in the market, multiplying each share by itself (you square it), and then adding the results.[22]

Suppose we have ten equal-sized firms — an easy problem. For firm A, we multiply ten times ten. That equals 100. We do this for each of the other nine firms. We add the results, and we come out with 1000.

Now that is interesting because the government's Guidelines are based on the advice below 1000, don't worry; the market is sufficiently unconcentrated so that the firms are going to have the ability to collude.[23] That is stage one — the line below which the guidelines tell us not to worry.

If you have five or six equal-sized firms, you would come out with a Herfindahl of about 1800. The index is below 1800 for six and above 1800 for five. So, what the guidelines are telling us is: when we move in the area of ten substantial firms to six, there might be concern that the firms will have an incentive to behave cooperatively.

This stage is marked by the range between 1000 to 1800 on the index. If the market concentration falls within this range, and if the merger increases concentration by 100 or more points on the index, the Guidelines say, the government is more likely than not to sue.[24]

As you will remember, I started out by saying that the government's concern is *increment* in power over price. High concentration (e.g., over 1000) may indicate possible power over price. The increase in concentration is the clue to increment in power over price. Unless the increase in concentration, in this range of concentration, is at least 100, the government supposes that any increment is insubstantial.

What produces an increment of 100? Suppose you have a five percent firm and a ten percent firm. You can figure out the increment by multiplying five times ten times two; and that is 100.

If you had a seven-plus percent firm and a seven-plus percent firm, you would get 100 also. Seven times seven times two is ninety-eight.

The Guidelines pinpoint a third stage of concentration — more than 1800. In that case you also have thresholds. At this level, the merger increases concentration by 50 to 100 on the index, the Guidelines say, the government will consider suit. It will look at all of the factors that make it more or less likely for the firms to collude, which means it will look at the factors that indicate common interests or uncommon interests, whether they are likely to be able to reach an agreement, and whether they are likely to be able to detect cheating and hold the agreement.[25]

If in the more than 1800 area the increase in concentration is 100 or more, the government says it is likely to sue.[26]

Well, what do you make of all of this? It cannot be true that these numbers capture market realities. Must we suspend disbelief to believe that we can reduce merger policy to numbers? It is possible, however, that these numbers and, more importantly the methodology behind them, are just a way to focus us on the problems, and that, above the thresholds, one must analyze all of the market facts.

The General Motors-Toyota joint venture gives one some reason to believe that the FTC — which has said that it would generaly follow the Justice Department Guidelines — is looking at the Guidelines only to what not to worry about. The majority statement in *General Motors-Toyota*[27] tells us that high concentration in the auto industry means nothing at all. The majority says: these companies have different costs. Demand is cyclical. The product is differentiated: "These and other characteristics make a collusive agreement difficult to establish and maintain."[28]

The law has many similarities, but it does not support the view of the Department of Justice or the FTC that only inefficient mergers are illegal.

Number one, if the market is fragmented, there are low barriers to entry, and the market shares of the merging partners are not very substantial, there is not likely to be an antitrust problem at all. *Von's Grocery*[29] is not the law. The claims of illegality in *Von's* are considered trivial today.

Number two, when the market is concentrated and there is a significant increase in concentration, the *Philadelphia National Bank* presumption applies. In *Philadelphia National Bank* the parties had 30 percent. The merger increased concentration by 33 percent. These factors raised a presumption of illegality.

I translated all of the Supreme Court cases into Herfindahl numbers in an article I wrote. The facts of *Philadelphia National Bank*, along with assumptions I made, indicated to me that the Herfindahl in the market was more than 1800 and that the increase in concentration was more than 600. A judgment that this merger was illegal, therefore, accords with the Guidelines analysis, if the market was correct; and it may have been correct, especially in view of banking regulations.

Marathon-Mobil[31] presents another case that might fall within the description of concentrated markets where the increase in concentration was significant. The real question there was market definition. Dr. Stigler testified that the market was a national market; that if prices went up artificially in any region, gas would pour in from another region. The court did not accept this view. Given the regional markets that the court accepted, the market was concentrated and the merger produced a significant increase in concentration.

A third situation is even more interesting. This is the case in which the market is concentrated but one cannot predict that the merger will lead to increased cooperation and lower output. In this case the government advises that it will not sue.

I do not think that is the law. The law is contrariwise. If the market is already concentrated and the merger partners are very significant forces in the same market, the merger may very well violate the law. It is not a necessary condition that plaintiff be able to prove that his merger will probably raise price and lower output. I will give you a couple of examples.

Philadelphia National Bank dictum is very clear on this point. When the market is already concentrated, it is important to keep doors open for deconcentration. There may be at present constraint on price. Maybe international banking put a constraint on price so that the merger partners could not raise price, but that constraint on price might go away tomorrow; things might change. Section 7 is a potentiality statute. It aims to preserve important competitive pressure in concentrated markets.

Second, it is a goal of the merger law to preserve alternatives for buyers. The Court states this point, also, in *Philadelphia National Bank*. Buyers are presumed better off when they have existing sellers to play against one another. The importance of this idea diminishes as we get more than a handful of suppliers. But if we have only two firms left in the market and a claim is made that they can merge because foreign competition will put pressure on price, I think the claim will — and should — fail.

There is a third reason why the law is hostile to mergers of important competitors in highly concentrated markets, even if they do not gain an increment in power over price. The law aims to promote alternative routes for innovation and to keep those alternative routes open. A case in point is *Grumman v. LTV*,[32] a 1981 takeover case in the Second Circuit. The parties produced military aircraft and commercial aircraft components. There were three markets. Two markets were highly concentrated and the parties had a substantial share. But the third market is one that interests me because, although the market was highly concentrated, each of the merging parties had almost no share at all. The court saw the merging parties as vital competitive factors. Each was out to get a major share. Each, individually, was innovating. Therefore, Judge Mishler said, in the court below, to remove one competitor from this market would undoubtedly tend to lessen competition substantially.

Rebutting the prima facie case. I have mentioned a couple of times that a merger, under certain conditions, is probably illegal. Can the defendant rebut the prima facie case after the government or other plaintiff has shown high concentration and strong statistics?

This is an evolving area. Defendants have been successful in a number of of cases. Defendants may win upon showing low barriers, very many potential competitors, frequent entry, vigorous price competition, vigorous foreign competition, declining concentration, or lack of direct overlap. Of course, if the facts allow, defendants may show under the *General Dynamics*[33] rule that the plaintiffs statistics are not trustworthy predictors of the future.[34]

There is increasing awareness that some mergers are procompetitive. And where there is no real harm to competition, it is important to preserve exit opportunities, just as it is important to preserve entry opportunities. It is the freedom of exit as well as entry — freedom to sell out after developing a successful business — that induces business people to make their investment in the first place.

Efficiencies are something to take seriously. Enforcers are sympathetic to compelling proof of clear production efficiencies. It remains to be seen whether clear production efficiencies will become an antitrust defense. I do not predict that efficiencies will save a price-raising merger.

Efficiencies can be procompetitive. By cutting costs they may enable a competitor to behave more rivalrously. Efficiencies can also be antitcompetitive. They might increase the market power of an already dominant firm. As to the former, efficiencies have always been relevant to effect on competition. As to the latter, one might be skeptical that the claimed efficiencies are real, or that the merger is necessary to realize them.

2. Potential Competition

Potential competition cases are, on the one hand, alive and well. The Merger Guidelines so indicate. The theory against certain potential horizontal mergers is the same as the theory against certain horizontal mergers. If you have very few companies in the market and you have a very strong competitive pressure from right outside the market, the elimination of the potential entrant's edge effect will facilitate collusion. It will lead to higher prices. It fits exactly into the government model.

The government model on potential competition is, very interestingly, the one aspect of the whole set of Merger Guidelines where the government approach is more pro-plaintiff than the law. That is because the government Guidelines combine edge effect and entry effect. Consider Procter and Gamble's acquisition of Clorox, the dominant producer of household liquid bleach.[35] The fact that Procter and Gamble, if it were true, would have entered the liquid bleach market and would have deconcentrated a highly concentrated market is treated as significantly as if Procter and Gamble's perceived imminent entry moderated price downwards and this edge effect was destroyed by the merger.

Otherwise, the Merger Guidelines on potential competition are quite consistent with the document as a whole. If the market is very highly concentrated, 1800 or above, if the potential competitor is one of very few firms with a clear entry advantage, and if it acquires a firm with 20 percent or more of its market, the government is likely to sue.[36]

3. Vertical Mergers

As to vertical mergers, just one or two words. The old idea that foreclosure results from a combination of buyers and sellers is no longer respected. One looks more closely today to see what the so-called foreclosed buyers or sellers can do; what their options are. They may be able to get to market just as efficiently; and new entrants may have a clear opportunity for entry. If so, "foreclosure" is an empty word.

I would refer you to the *Fruehauf* case,[37] which is the only recent vertical case. There, the percentage of all sales on the market which were accounted for by the seller and which the buyer-partner would buy from the seller was almost six percent. The court found no violation. The analysis is good and interesting and I think it represents the law today. There was no violation because the so-called foreclosed buyers had other good options and no costs were imposed on them and no barriers were raised as a result of the merger.

V. Conclusion

In conclusion, we have come a long way from *Brown Shoe*[38] and *Von's*. The courts are taking seriously competitive pressures including those imposed by foreign firms. Are they, however, applying the government's model? Are they likely to do so?

The government frames the question: is this merger inefficient? is this merger output-limiting? The case law does not. The case law asks, in a more open way, is this merger, and perhaps others like it that may follow, likely to impair competition (which is viewed as a process of rivalry among more than a couple of firms)? The case law asks, also: is this market already concentrated and is the merger likely to shut the door to opportunities for competition to break out?

The government model has not yet gained acceptance. I think it is a little too narrow, too mechanical, and too unreleated to the spirit of the merger law to be fully embraced. But there is no doubt that the government model and mode of analysis has had and will have its impact, if only to help us identify which mergers are output-limiting, which mergers are output-increasing, and perhaps to induce courts to stay their hand when the merger is itself good for consumers.

Thank you.

WALTER BARTHOLD: Eleanor, you have covered the field so well that we do not need time for questions. When you get up to speak, everything suddenly becomes as bright and clear as if the sun came out; we are very grateful to you for the time and effort that you devoted to this presentation.

When the Executive Committee was putting today's program together, a debate raged as to whether Kimba Wood's picture on the brochure would attract more participants than Walter Barthold's would scare away. I am very pleased to see that for once beauty has triumphed over the beast. We all know that the real reason for the turnout today is the caliber of the speakers that we have managed to attract, all of whom, incidentally, are volunteers and to all of whom we are grateful for the time they have put in, not just in coming here to talk but in the preparation that all of you can see went into these excellent lectures.

FOOTNOTES

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1. Williams, *Frenzy and Style in the Merger Boom*, N.Y. Times, Jan. 15, 1984, at 53, p.1, col. 2.
2. *See Congress is Critical of FTC Handling of Mobil's Bid to Acquire Marathon*, 40 Antitrust & Trade Reg. Rep. (BNA) A-19 (Dec. 17, 1981).
3. Proposed Consent Order & Commissioners' Statements, 48 Fed. Reg. 57,246 & 57,314 (1983), *reprinted in* 46 Antitrust & Trade Reg. Rep. (BNA) 42 (Dec. 28, 1983).
4. *FTC Won't Attack Acquisition in Titanium Dioxide Industry*, 45 Antitrust & Trade Reg. Rep. (BNA) 751 (Nov. 10, 1983).
5. *See* United States Dep't of Justice Merger Guidelines — 1982, §V(B), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4505.20 [hereinafter cited as 1982 Guidelines].
6. 15 U.S.C. §25 (1976).
7. 15 U.S.C. §53(b) (1976).
8. 665 F.2d 1072 (D.C. Cir. 1981).
9. 15 U.S.C. §26 (1976 & Supp. V 1981).
10. 498 F.2d 851 (2d Cir.), *cert. denied*, 419 U.S. 883 (1974).
11. *Id.* at 854.
12. Marathon Oil Co. v. Mobil Corp., 530 F.Supp. 315 (N.D. Ohio), *affd*, 669 F.2d 378 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982).
13. 2 B. Fox & E. Fox, Corporate Acquisitions & Mergers §§20B.01-09 (1983).
14. S. Axinn, B. Fogg & N. Stoll, Acquisitions Under the Hart-Scott-Rodino Antitrust Improvements Act (1979).
15. 1982 Guidelines, *supra* note 5, at §II(A), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4502.10.
16. *Id.* §II(B)(1), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4502.201.
17. *Id.* §II(C), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4502.30.
18. 1982-2 Trade Cas. (CCH) ¶ 64,871 (W.D. Va. 1982).
19. United States v. Grinnell Corp. 384 U.S. 563, 591 (1966) (Fortas J., dissenting).
20. United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963).
21. *See* Fox, *The New Merger Guidelines — A Blueprint for Microeconomic Analysis*, 27 Antitrust Bull. 519, 569-74 (1982).
22. 1982 Guidelines, *supra* note 5 at§III(A), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4503.10.
23. *Id.* §III(A)(1)(a), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4503.101(a).
24. *Id.* §III(A)(1)(b), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4503.101(b).
25. *Id.* §III(A)(1)(c), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4503.101(c).
26. *Id.*
27. Proposed Consent Order & Commissioners' Statements, *supra* note 3.
28. *Id.* at 57,316, 46 Antitrust & Trade Reg. Rep. (BNA) at 55 (statement of Chairman Miller, Comm'rs Douglas & Calvani).
29. United States v. Von's Grocery Co., 384 U.S. 270 (1966).
30. Fox, *supra* note 21.
31. Marathon Oil Co. v. Mobil Corp., 530 F. Supp. 315 (N.D. Ohio), *affd*, 669 F.2d 378 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982).
32. Grumman Corp. v. LTV Corp., 527 F. Supp. 86 (E.D.N.Y.), *affd*, 665 F.2d 10 (2d Cir. 1981).
33. United States v. General Dynamics Corp., 415 U.S. 486 (1974).
34. See Fox & Fox, *supra* note 13, §8,02[2][t].
35. *See* Procter & Gamble v. FTC, 386 U.S. 568 (1967).
36. 1982 Guidelines, *supra* note 5, at §IV(A)(3), *reprinted in 2* Trade Reg. Rep. (CCH) ¶4504.103.
37. Fruehauf Corp. v. FTC, 603 F.2d 345 (2d Cir. 1979).
38. Brown Shoe Co. v. United States, 370 U.S. 294 (1962).

CHAPTER 4
THE STATE ACTION DOCTRINE: TWO YEARS AFTER *CITY OF BOULDER*

David Klingsberg+

During the two years that have passed since the Supreme Court decided *Community Communications Co. v. City of Boulder*,[1] the lower courts have been struggling to develop a coherent and consistent interpretation of the state action doctrine in its application to municipalities, subordinate state agencies and private entities. In the not too distant past, the principal antitrust concern of states was centered around their ability to make affirmative use of the antitrust laws as evidenced by their support of parens patriae legislation. In recent years, following a number of Supreme Court decisions,[2] the states themselves have been on the receiving end of antitrust actions in cases involving state agencies such as the Port Authority of New York and New Jersey,[3] racing commissions,[4] alcoholic beverage boards,[5] and the state bar.[6] States, their subordinate administrative bodies and municipalities have been sued under the antitrust laws for such diverse activities as granting exclusive concessions,[7] controlling prices,[8] limiting entry into professions,[9] limiting entry into regulated industries,[10] zoning,[11] refusing to provide municipal services[12] and operating electric utilities[13]

I. From Parker to Boulder

The Supreme Court defined the state action doctrine in *Parker v. Brown*.[14] In *Parker* a producer and packer of raisins sued state officials to enjoin the enforcement of a statute authorizing a state commission to fix the price of raisins sold by producers to packers. Assuming that the scheme would violate the Sherman Act if engaged in by a combination of private persons, the Court explained that the Commission "derived its authority and efficacy from the legislative command of the state and was not intended to operate or become effective without that command."[15] In an oft-quoted description of what has become known as the state action doctrine, the Court said,

> We find nothing in the language of the Sherman Act or in its history which suggests that its purpose was to restrain a state or its officers or agents from activities directed by its legislature. In a dual system of government in which under the Constitution the states are soverign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress.[16]

The *Parker* Court held that state action was not intended to be subject to the antitrust laws, but it was not presented with the issue of whether Congress intended to apply the antitrust laws to municipalities or the extent to which the doctrine would shield private parties acting under state authority.

In 1975, almost thirty years after *Parker v. Brown*, the Supreme Court returned to the state action doctrine in *Goldfarb v. Virginia State Bar*.[17] At issue in *Goldfarb* was the legality of a minimum fee schedule promulgated by a local bar association and enforced by the Virginia State Bar pursuant to authority delegated by the state supreme court to enforce attorney discipline. Finding that the minimum fee schedule violated section 1 of the Sherman Act,[18] the Court explained that *Parker v. Brown* only protects "anticompetitive activities ... compelled by direction of the State acting as sovereign."[19]

The Court first addressed the liability of municipalities under the antitrust laws in *City of Lafayette v. Louisiana Power & Light Co.*[20] In *Lafayette* an investor-owned electric utility claimed that the City of Lafayette, which owned a municipal utility, had attempted to force customers of the privately-owned utility, who lived outside of the city limits, to purchase their electrical requirements from the municipal utility by conditioning the sale of water and gas on the purchase of electricity. Recognizing that the private utility's allegations "aptly illustrate the import which local governments, acting as providers of services, may have on other individuals and business enterprises with which they interrelate as purchasers, suppliers, and ... competitors,"[21] a plurality of the Court refused to accord state action immunity to municipalities.

The Court in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*[22] further refined the doctrine enunciated in *Parker v. Brown*[23] and focused on its applicability to private parties.[24] *Midcal* involved a suit by a price cutting distributor seeking to enjoin the enforcement of a California resale price maintenance scheme which authorized producers and wholesalers to set resale prices for wines sold in California. After determining that the price fixing scheme violated the Sherman Act, Justice Powell, for a unanimous Court, announced that the earlier decisions:

> establish two standards for antitrust immunity under *Parker v. Brown*. First, the challenged restraint be "one clearly articulated and affirmatively expressed as state policy;" second, the policy must be "actively supervised" by the state itself.[25]

The Supreme Court's most recent decision concerning the state action doctrine is *Community Communications Co. v. City of Boulder*,[26] where the Court upheld a preliminary injunction preventing the city from enforcing a municipal ordinance that would have had the effect of restricting the petitioner, a cable television company, from expanding its business within the city limits. After repeating the *Parker* principle derived from the supremacy clause,[27] the Court proceeded to characterize the issue as one of state exemption rather than, as the dissenters perceived it, one of federal preemption.[28] The court declined to infer an exemption from the antitrust laws for municipalities, and held that the home rule amendment to the Colorado constitution,[29] which vested the city with every power possessed by the state legislature, did not suffice as a "clearly articulated" state policy necessary to shield the municipality's allegedly anticompetitive conduct.[30]

II. The Aftermath of Boulder

As evidenced by the surfeit of lower court decisions attempting to apply the *Boulder* rule, the Court in *Community Communications Co. v. City* *of Boulder* left many questions unanswered. In considering the aftermath of *Boulder*, a convenient starting point is the decision itself where the majority, concurring, and dissenting opinions expressly recognized a number of important open issues that would have to be resolved on a case-by-case basis including whether the state action doctrine requires that states compel anticompetitive conduct and what is implied by the term "compulsion,"[31] whether one[32] or both[33] elements of the *Midcal* test of active supervision and clear articulation of state policy permitting anticompetitive conduct are applicable to subordinate governmental entities and municipalities, and the circumstances under which private entities fall under the state's aegis.[34]

A. Anticompetitive Conduct by Municipalities

1. Degree of Supervision

An important issue left open by the *Boulder* court is whether, in addition to showing a "clearly articulated" state policy (which is the first element of the *Midcal* test) a municipality also has to meet the second leg of *Midcal* by demonstrating that the state actively supervised the conduct in question.[35] Most of the appellate courts that have addressed this issue during the past year have agreed with Justice Rehnquist's dissenting opinion in *Boulder* that it would be "rather odd" to require the state actively to supervise the enforcement of a municipal ordinance, as this would in effect require that the state, rather than the municipality, enforce the municipal ordinance.[36] Thus, in *Town of Hallie v. City of Eau Claire*,[37] where a municipality refused to provide sewage treatment to adjoining towns unless they consented to annexation, the Seventh Circuit held that the refusal was protected since it involved a traditional municipal function undertaken in furtherance of a clearly articulated and affirmatively expressed state policy. The Court held that under these circumstances the municipal enforcement need not be actively supervised by the state.[38] Similarly, in *Gold Cross Ambulance & Transfer & Standby Service, Inc. v. City of Kansas City*,[39] the Eighth Circuit, confronted with a municipality's grant of an exclusive franchise to a private ambulance company, declined to apply the active supervision standard and found that the franchise award was shielded by the state action doctrine because the state had authorized the activity with an intent to displace competition.[40]

Most recently, the Ninth Circuit joined the Seventh and Eighth Circuits in rejecting an "active state supervision" requirement as a prerequisite for shielding municipal conduct under the *Parker* doctrine. In *Golden State Transit Corp. v. City of Los Angeles*,[41] a disappointed franchise sued the City of Los Angeles under section 1 of the Sherman Act for refusing to renew its franchise. The Ninth Circuit affirmed a lower court grant of summary judgment, reasoning that a state constitutional provision classifying taxicab companies as public utilities, and a state statute permitting municipalities to license and regulate taxicab companies, clearly articulated a state policy to displace competition with regulation.[42] Following both Justice Rehnquist's dissent in *Boulder*[43] and the other circuits that have passed on the question,[44] the Ninth Circuit agreed that "cities need not satisfy the second part of the *Midcal* test [active state supervision] to establish Parker immunity when they perform a traditional municipal function under a clearly established and affirmatively expressed state policy."[45]

2. Degree of Authorization

A number of courts have also considered the question of the extent to which municipalities, in order to obtain state action protection, must act pursuant to a specific authorization or direction by the state legislature permitting the anticompetive conduct in issue. Several courts have applied a broad test inquiring into whether the restraint on competition was a necessary or reasonable consequence of engaging in a generally authorized activity, rather than questioning whether the anticompetitive activity was specifically directed by the state.[46]

It is impracticable to require a specific direction by the state legislature in all cases. How, for example, would one expect the New York State legislature to deal with such diverse items as taxi franchises, garbage collection and traffic control for a small town compared with, for example, New York City and its many diverse problems. Requiring a specific direction would, in essence, impose a "compulsion" standard, which most courts have held is not applicable to state subdivisions or municipalities.[47]

3. Liability and Damages

Most reported decisions concerning the ability of cities to enjoy state action immunity are in response to motions to dismiss or for summary judgment. Accordingly, some of the more interesting issues left open by *Boulder*, such as the applicability of a rule of reason or a per se rule or the treble damage provisions of section 4 of the Clayton Act,[48] have yet to be determined. Thus, for example, Justice Stevens in his concurring opinion in *Boulder* noted that the Court had not decided that the city had violated the antitrust laws, but only that it was not exempt under *Parker v. Brown*.[49]

One unresolved question is whether in applying a rule of reason analysis to determine a city's antitrust liability, the regulatory goals of the city should be taken into account.[50] Under the rule of reason as explained in *National Society of Professional Engineers v. United States*,[51] courts should ordinarily limit their inquiry to the economic detriments and benefits of state legislation without inquiring into the traditional health, safety and public welfare concerns underlying a piece of legislation. Thus, as Justice Rehnquist observed in *Boulder*, "[a]pplying Professional Engineers to municipalities would mean that an ordinance could not be defended on the basis that its benefits to the community, in terms of traditional health, safety, and public welfare concerns, outweigh its anticompetitive effects. A local government would be disabled from displacing competition with regulation."[52] Distinguishing *National Society of Professional Engineers* in the case of governmental anticompetitive conduct may also, however, create difficulties. Without the strictures of *National Society of Professional Engineers*, federal courts would be given license to engage in a freewheeling examination of social legislation by balancing its effect on competition against its perceived social merit. This "underlying, essentially standardless inquiry into the reasonableness of local regulations"[53] would presage an undesirable return to the *Lochner*[54] era where liberty of contract and substantive due process were the predicate for a similar inquiry. Even if the particular purposes of municipal regulation were considered under the rule of reason, how, for example, would a court weigh the benefits of traffic control in awarding an airport taxi concession against the benefits of competition, or the aesthetic benefits of restrictive zoning against competition in housing? These are, essentially, legislative and political determinations.

Two other open questions are whether the courts will apply a per se rule to municipalities and state agencies where they would otherwise apply it to private parties, and whether treble damages should be awarded under section 4 of the Clayton Act.[55]

A recent district court decision addresses both of these questions. In *Unity Ventures v. County of Lake*[56] a real estate developer sued a number of parties, including a municipality, county and mayor, alleging that they had conspired to restrain trade and to monopolize by refusing to permit a sewer connection to the plaintiffs proposed land development and by engaging in "sham" challenges to the sewer interconnection in administrative proceedings. The court refused, however, to instruct the jury to apply a per se rule, explaining: "to conclude that these facts, if established, constitute a per se violation would be to fly in the face of the public entities' statutory authority to regulate. . . ."[58] Following a rule of reason, the jury returned a verdict of $9.5 million on the antitrust claims, which the court trebled.[58]

Because of the exposure of cities under the *Boulder* rule, legislation has been proposed in Congress to partially exempt municipalities from antitrust liability. The Department of Justice has given qualified endorsement to the Thurmond Bill,[59] which grants immunity to a city to the extent that its anticompetitive activity does not involve the sale of goods or services in competition with private persons.[60] The distinction between the provision of governmental services and the sale of goods in the free market is a difficult one to draw, however, and could ensnare the law of municipal liability under the antitrust laws in what Justice Frankfurter characterized in another context as the govenmental/nongovernmental quagmire[61] that has long plagued the law of governmental immunities.[62] Moreover, the pervasive competition between municipalities, even in their traditional governmental functions, and private entities might undermine the intended effect of this bill. Thus, for example, private enterprise today provides police protection, garbage collection, bus transportation, libraries, electric power and other services which are also provided by city governments exercising their traditional authority.

B. Antiticompetitive Conduct by State Subdivisions

Another question which has provoked a difference of view among the circuits is the appropriate standard under *Parker* for immunizing anticompetitive conduct by subordinate state agencies.[63] In *First American Title Co. of S.D. v. South Dakota Land Title Ass'n*,[64] a local agency for a foreign title insurer sued the State Abstracters' Board of Examiners, a quasi-state agency composed primarily of abstracters, for promulgating regulations imposing anticompetitive restraints on out-of-state abstracters. The Eighth Circuit held that the allegedly anticompetitive activities of South Dakota's Abstracting Board were shielded by *Parker* even though the challenged regulations were not compelled by the South Dakota legislature. The Court reasoned that "[t]o the extent that the challenged regulatory provisions impose an anticompetitive restraint upon [the plaintiff], such restraint is a necessary consequence of engaging in the authorized activity."[65]

Other circuits, however, have been less magnanimous in finding state authorization for anticompetitive practices by state subdivisions.[66] In *United States v. Texas State Board of Public Accountancy,* for example, the Fifth Circuit affirmed a lower court order enjoining the Texas State Board of Accountancy, which consisted of nine accountants practicing in Texas, from enforcing a competitive bidding prohibition because the prohibition was neither mandated by the state as soverign nor dictated by the state.[67]

In the recently decided case of *Hoover v. Ronwin*[68] the Supreme Court provided guidance for resolving questions concerning the necessary degree of State authorization for anticompetitive practices by state subdivisions. In *Ronwin*, an unsuccessful bar applicant sued the Arizona Supreme Court's Committee on Examinations and Admission alleging that the Committee not only limited the admission of applicants to the Arizona Bar on the basis of objective qualifications, but also attempted to limit the number of persons admitted to practice in Arizona to reduce competition among Arizona lawyers.[69] The Supreme Court, however, dismissed the applicant's complaint holding that the Committee's actions constituted state action, which was exempt from antitrust challenge under *Parker v. Brown* and its progeny.[70] The Court noted that the Arizona Constitution vested authority in the State Supreme Court to determine who should practice law in Arizona, and that although the Arizona Supreme Court Rules delegated responsibility to the Committee to "recommend" applicants for admission to the bar, the State Supreme Court reserved to itself the ultimate authority to grant or deny admission.[71] Thus, the Court found that because only the Arizona Supreme Court had authority to grant or deny admission to practice in the state, the "real party in interest" was the court and that under *Bates v. State Bar of Arizona,*[72] its legislative acts were exempt from antitrust examination.

From a policy point of view, state agencies present a lesser threat to competition than municipalities. As Justice Brennan emphasized in *City of Lafayette*[72A] municipalities may threaten competition in their pursuit of provincial policies because their local acts may have anticompetitive effects outside of their jurisdiction and conflict with the economic policies of other municipalities and the state itself. State agencies, by contrast, create rules and administer policy on a statewide level. Dissatisfaction with these rules and policies can be remedied through the statewide electoral process as well as the antitrust laws.

C. Anticompetitive Conduct by Private Parties

There also have been recent developments in the state action area which affect the liability of private or nongovernmental parties. The *Boulder* aftermath is relevant in this respect since, if a city cannot seek the protection of a state action doctrine under the newly prescribed standards, a private party acting pursuant to a city ordinance or directive similarly will not be able to shield its activities from the antitrust laws. As a consequence, the potential liability of private parties could have a chilling effect on their cooperation in the implementation of local governmental regulation. Under the *Midcal* standard, a state must both clearly articulate a policy to displace competition with regulation and actively supervise the private body. In addition to this two-part test, it remains an open question whether the additional element of state compulsion, which the Supreme Court announced in *Goldfarb v. Virginia State Bar,*[73] is still applicable.[74]

In *Goldfarb* "compel" was used in contrast to the mere promoting of the activity by the state,[75] which under the *Midcal* standard would be insufficient in any event to provide a clear articulation of an intent to displace competition with regulation. Thus, if there is compulsion in the sense apparently intended in *Goldfarb*, there is a plain articulation under *Midcal*. Compulsion, however, should not have to rise to the level of an absolute command. In *Parker*, for example, the state authorized the raisin producers to set up a proration committee to establish "orderly marketing" procedures for California raisins.[76] The Act did not, however, compel the growers to "stabilize" the prices of raisins or horizontally divide markets.

Whether private parties must establish state compulsion in order to obtain a state action exemption has proved to be a particularly troublesome issue with the Fifth Circuit requiring compulsion[77] and the Ninth Circuit relying on *Midcal's* clear articulation and active supervision standard.[78] In *United States v. Southern Motor Carriers Rate Conference,*[79] the Fifth Circuit was confronted with a rate-setting agreement among trucking companies under the aegis of private trade associations or "rate bureaus." Even though the collective ratemaking was authorized by state statutes,[80] the Fifth Circuit found that it was not compelled by the states and, therefore, failed under *Goldfarb* to constitute state action.[81]

The Ninth Circuit has rejected the compulsion test in favor of the *Midcal* standard.[82] In *Turf Paradise, Inc. v. Arizona Downs*[83] the Ninth Circuit ruled that to invoke the state action doctrine to exempt the allocation of racing days among race track operators regulated by a commission, it was sufficient that the state had evidenced the policy to limit the numbers of days of racing.[84] The court rejected the compulsion requirement based on Justice Steven's remark in *Cantor* that the inquiry "must turn on the degree to which the state or its agency has 'put its own weight on the side of [that] practice.' "[85] In other words, absolute compulsion should not be the litmus test.

In what appears to be doctrinal confusion, some courts have applied the compulsion test where it was unnecessary. In *Arzt v. Blue Cross & Blue Shield of Greater New York,*[86] for example, the court refused to dismiss a conspiracy complaint brought by a trustee in bankruptcy of a defunct hospital. In essence, the plaintiff alleged that Blue Cross, the City of New York and the State of New York had conspired to eliminate excess hospital beds in New York by manipulating medicare reimbursements and that this manipulation had caused the plaintiff's bankruptcy. Although the court dismissed the complaint as to the state by relying on *Parker v. Brown,*[87] it refused to dismiss the complaint as to Blue Cross/Blue Shield.[88] The court found that the mere participation in the scheme by the state was insufficient to immunize the alleged conspiracy because, the court concluded, the state had not compelled Blue Cross/Blue Shield's actions.[89] This case is troubling because it seems that the court resorted unnecessarily to the "compulsion" doctrine when a simple application of *Midcal* would have sufficed to prohibit the arrangement. Thus, in *Arzt*, although the state may have clearly articulated and affirmatively expressed a policy to reduce the number of hospital beds in New York, it would seem that the state did not actively supervise Blue Cross/Blue Shield's efforts to accomplish that end.

A preferable approach was adopted by the court in *North v. New York Tel. Co.*[90] In *North* a user of telephone service sued the Public Service Commission and the telephone company for setting excessive telephone rates. The court dismissed the complaint noting that phone rates are set by the Public Service Commission, that the Commission, is "actively supervised by the state, and that it acts according to a "clearly articulated and affirmative expressed" state policy.[91] One problem with this opinion, however, is that it is unclear whether both the setting of the rates by the Commission and the changing of the rates by the telephone company must meet both prongs of the *Midcal* test. It would seem that the Commission, as a subordinate state agency, need not be actively supervised by the state. Rather, it should be only acting in furtherance of a clearly articulated policy to displace competition with regulation.

III. Conclusion

In her recently published book entitled "Words and Values,"[92] Peggy Rosenthal notes that we do not lead our language where we want it to go; rather, it leads us.[93] Ms. Rosenthal writes that all disciplines tend to reify their abstractions,[94] that is, they mistake their main conceptual terms for concrete or material things.

So too, in the antitrust context abstract terms like exemption have grown into things that have created a morass which was not likely to have been the result intended by Congress when it enacted the Sherman Act. When the Courts cease to examine the scope of a statute's intended coverage or to project the consequences of extending it, but instead simply view an absence of coverage as an exemption," they may be led by their language. For there has grown up around that term the concept of presumption against exemptions which is not likely to be implied.[95] If the issue is viewed as one of federal preemption, the language may lead the courts in the opposite direction — contracting the federal arm of authority. Compulsion likewise is a term which in the view of some courts has assumed the lifelike image of a big brother issuing inexorable commands. In context, however, it should mean no more than prompted by a clearly articulated legal authority. Again, the semantic focus tends at times to alter the result without sufficient focus on the real issue of how far federal interference into local governmental activities was intended or is warranted.

Unfortunately, the difficulties created by the aftermath of *Boulder* cannot all be resolved by a proper respect for potentially misleading word images. Even under the broadest test of exemption — limited to the clear articulation leg of *Midcal's* two-pronged test — there is still a danger that municipalities will simply relinquish legitimately regulatory activity and/or refrain from providing desirable services rather than undergo the risk of treble damage liability and the expense of defending antitrust litigation. Thus, cities will become victims of the power play by a number of states which

— in the guise of waving the antitrust flag — have sought to enhance their own power and to fill the void that would be left by municipalities' attempts to avoid altogether the burden of antitrust.[96] Nor is the current proposed legislation an adequate solution in view of the impracticality of distinguishing governmental and competitive functions.

As the cities, as well as state subordinate agencies and private parties cooperating in their regulatory activities, become more battered and bruised by a plethora of litigation expenses and burdens, which thus far do not appear to be producing results that materially enhance the competitive business environment, perhaps Congress will see fit to provide a broader exemption for legitimately local — albeit sometimes competitive — governmental activities. In the meantime, the courts should use the tools that the Supreme Court has provided to preserve such legitimate local governmental activity rather than being led by terms in the applicable tests into wooden applications that produce unintended and undesirable consequences.

FOOTNOTES

+ Kaye, Scholer, Fierman, Hays & Handler, New York. The author gratefully acknowledges the contribution of John Chapman of the same firm.
1. 455 U.S. 40 (1982).
2. Community Communications Co. v. City of Boulder, 455 U.S. 40 (1982); California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); City of Lafayette v. Louisiana Power & Light Co., 435 U.S. 389 (1978) (plurality); Bates v. State Bar of Arizona, 433 U.S. 350 (1977); Cantor v. Detroit Edison Co., 428 U.S. 579 (1976); Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975).
3. Transport Limousine of Long Island, Inc. v. Port Authority of N.Y. & N.J., 571 F. Supp. 576 (E.D.N.Y. 1983).
4. *E.g.*, Euster v. Eagle Downs Racing Ass'n, 677 F.2d 992 (3d Cir.), *cert. denied*, 103 S. Ct. 388 (1982); Turf Paradise, Inc. v. Arizona Downs, 670 F.2d 813 (9th Cir.), *cert. denied*, 456 U.S. 1011 (1982); Horsemen's Benevolent & Protective Ass'n v. Pennsylvania Horse Racing Comm'n, 530 F. Supp. 1098 (E.D. Pa.), *aff'd mem.*, 688 F.2d 821 (3d Cir. 1982).
5. *E.g.*, California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); Morgan v. Division of Liquor Control, 664 F.2d 353 (2d Cir. 1981); Alcoholic Beverages Control Bd. v. Taylor Drug Stores, Inc., 635 S.W. 2d 319 (Ky. 1982).
6. *E.g.*, Bates v. State Bar of Arizona, 433 U.S. 350 (1977); Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975); Ronwin v. State Bar of Arizona, 686 F.2d 692 (9th Cir. 1982), *cert. granted sub nom.* Hoover v. Ronwin, 103 S. Ct. 2084 (1983).
7. *See, e.g.*, Central Iowa Refuse Sys., Inc. v. Des Moines Metropolitan Solid Waste Agency, 715 F.2d 419 (8th Cir. 1983); Gold Cross Ambulance & Transfer & Standby Serv. v. City of Kansas City, 705 F.2d 1005 (8th Cir. 1983); Affiliated Capital Corp. v. City of Houston, 700 F.2d 226 (5th Cir.) *reh' granted*, 714 F.2d 25 (5th Cir. 1983); Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, 562 F. Supp. 712 (D. Hawaii 1983); Deak-Perera Hawaii v. Department of Transp., 553 F. Supp. 976 (D. Hawaii 1983).
8. *E.g.*, California Retail Liquor Dealers Ass'n. v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975); Euster v. Eagle Downs Racing Ass'n, 677 F.2d 992 (3d Cir.), *cert. denied*, 103 S. Ct. 388 (1982); Knudsen Corp. v. Nevada State Dairy Comm'n, 676 F.2d 374 (9th Cir. 1982); Morgan v. Division of Liquor Control, 664 F.2d 353 (2d Cir. 1981); Kroger Co. v. Kentucky Milk Marketing & Antimonopoly Comm'n, 1982-2 Trade Cas. (CCH) ¶ 65,585 (Cir. Ct. Ky. 1983).
9. *E.g.*, Ronwin v. State Bar of Arizona, 686 F.2d 692 (9th Cir. 1982), *cert. granted sub nom.* Hoover v. Ronwin, 103 S. Ct. 2084 (1983).
10. *E.g.*, Campbell v. City of Chicago, 577 F. Supp. 1166 (N.D. Ill. 1983); Springs Ambulance Serv. v. City of Rancho Mirage, 1983-2 Trade Cas. (CCH) ¶ 65,646 (C.D. Ca. 1983); Catalina Cablevision Assocs. v. City of Tucson, 1984-1 Trade Cas. (CCH) ¶ 65,789 (D. Az. 1984).
11. *E.g.*, Westborough Mall, Inc. v. City of Cape Girardeau, 693 F.2d 733 (8th Cir. 1982), *cert. denied*, 103 S. Ct. 2122 (1983); Mason City Center Assoc. v. Mason City, 671 F.2d 1146 (8th Cir. 1982); Omni Outdoor Advertising, Inc. v. City of Columbia, 566 F. Supp. 1444 (D.S.C. 1983); Campbell v. City of Phoenix, 1983-2 Trade Cas. (CCH) ¶ 65,753 (D. Az. 1983); Scott v. Sioux City, Iowa, 1983-1 Trade Cas (CCH) ¶ 65,352 (N.D. Iowa 1983), *on reconsideration*, 1983-2 Trade Cas. (CCH) ¶ 65,589.
12. *E.g.*, City of Lafayette v. Louisiana Power & Light Co., 435 U.S. 389 (1978) (plurality); Town of Hallie v. City of Eau Claire, 700 F.2d 376 (7th Cir. 1983); Vickery Manor Serv. Corp. v. Village of Mundelein, 575 F. Supp. 996 (N.D. Ill. 1983).
13. *E.g.*, City of Lafayette v. Louisiana Power & Light Co., 435 U.S. 389 (1978); City of Kirkwood v. Union Elec. Co., 671 F.2d 1173 (8th Cir. 1982), *cert. denied*, 103 S. Ct. 814 (1983); Grason Elec. Co. v. Sacramento Mun. Util. Dist., 526 F. Supp. 276 (E.D. Ca. 1981); Winters v. Indiana & Michigan Elec. Co., 1979-2 Trade Cas. (CCH) ¶ 62,797 (N.D. Ind. 1979).
14. 317 U.S. 341 (1943).
15. *Id.* at 350.
16. *Id.* at 350-51.
17. 421 U.S. 773 (1975).
18. *Id.* at 783.
19. *Id.* at 791. *See infra* text accompanying notes 70-95.
20. 435 U.S. 389 (1978) (plurality).

21. *Id.* at 403.
22. 445 U.S. 97 (1980).
23. 317 U.S. 341 (1943).
24. The Supreme Court first considered the issue of state action immunity for a private party in Cantor v. Detroit Edison Co., 428 U.S. 579 (1976). In *Cantor* the plaintiff, a retail druggist selling light bulbs, claimed that the sole supplier of electricity in southeastern Michigan, Detroit Edison, was furnishing light bulbs to its customers without charge, which, in effect, amounted to an illegal tying arrangement with electricity as the tying product and light bulbs as the tied product. *Id.* at 581-85. The Court explained that the mere approval of the utility's rate structure by the Michigan Public Service Commission was insufficient to protect the program under *Parker v. Brown* because the defendant had done something "more than obey a state command." *Id.* at 591.
25. 445 U.S. at 105 (quoting Lafayette v. Louisiana Power & Light Co., 435 U.S. 389, 410 (1978) (plurality) (Brennan, J.)).
26. 455 U.S. 40 (1982).
27. "The Constitution and the Laws of the United States . . . shall be the supreme law of the land . . . ." U.S. Const. art. VI, cl. 2.
28. *Compare City of Boulder*, 455 U.S. at 53 ("The Parker State-Action exemption reflects Congress' intention to embody in the Sherman Act the federalism principle that States possess a significant measure of sovereignty under our Constitution.") *with id.* at 61-62 (Rehnquist, J., dissenting) ("I think it quite clear that questions involving the so-called 'state action' doctrine are more properly framed as being ones of pre-emption rather than exemption.")
29. Col. Const. art. XX, §6.
30. 455 U.S. at 55-56.
31. *See e.g.*, Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975); United States v. Southern Motor Carriers Rate Conference, 702 F.2d 532 (5th Cir. 1983) (en banc); Sound, Inc. v. A.T.&T., 631 F.2d 1324 (8th Cir. 1980); Artz v. Blue Cross & Blue Shield of Greater New York, 76 Civ. 5723 (S.D.N.Y. 1982) (available February 1, 1984 on LEXIS, Genfed library, Dist. file).
32. *See, e.g.*, Golden State Transit Corp. v. City of Los Angeles, 726 F.2d 1430 (9th Cir. 1984); City of North Olmstead, Ohio v. Greater Cleveland Regional Transit Auth., 722 F.2d 1384 (6th Cir. 1983); Parks v. Watson, 716 F.2d 646, 663 (9th Cir. 1983); Gold Cross Ambulance & Transfer & Standby Serv., Inc. v. City of Kansas City, 705 F.2d 1005 (7th Cir. 1984); Town of Hallie v. City of Eau Claire, 700 F.2d 376 (7th Cir. 1983); Pueblo Aircraft Servs., Inc. v. City of Pueblo, 679 F.2d 805 (10th Cir. 1982), *cert. denied*, 103 S. Ct. 762 (1983)
33. *See, e.g.*, California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); Ronwin v. State Bar of Arizona, 686 F.2d 692 (9th Cir. 1982), *cert. granted sub nom.* Hoover v. Ronwin, 103 S. Ct. 2084 (1983); Euster v. Eagle Downs Racing Ass'n, 677 F.2d 992 (3d Cir.); *cert. denied*, 103 S. Ct. 388 (1982); Knudsen Corp. v. Nevada State Dairy Comm'n, 676 F.2d 374 (9th Cir. 1982); Morgan v. Division of Liquor Control, 664 F.2d 353 (2d Cir. 1981); Corey v. Look, 641 F.2d 32 (1st Cir. 1981); Jetro Cash & Carry Enters. v. Food Distrib. Center, 569 F. Supp. 1404 (E.D. Pa. 1983); Ajax Aluminum, Inc. v. Goodwill Indus. of Muskegon County, 564 F. Supp. 628 (W.D. Mich. 1983); Trident Neuro-Imaging Laboratory v. Blue Cross & Blue Shield of S.C., 1983-2 Trade Cas. (CCH) ¶ 65,674 (D.S.C. 1982); Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, 562 F. Supp. 712 (D. Hawaii 1983).
34. *See, e.g.*, California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980); Cantor v. Detroit Edison Co., 428 U.S. 579 (1976); First American Title Co. of South Dakota v. South Dakota Land Title Ass'n, 714 F.2d 1439 (8th Cir. 1983), *cert. denied*, 104 S. Ct. 709 (1984); United States v. Southern Motor Carriers Rate Conference, 702 F.2d 532 (5th Cir. 1983) (en banc); United States v. Title Ins. Rating Bureau of Arizona, Inc., 700 F.2d 1247 (9th Cir. 1983); Turf Paradise, Inc. v. Arizona Downs, 670 F.2d 813 (9th Cir.), *cert.* denied, 456 U.S. 1011 (1982).
35. *See supra* text accompanying notes 23-26.
36. 455 U.S. at 71, n.6 (Rehnquist, J., dissenting).
37. 700 F.2d 376 (7th Cir. 1983).
38. *Id.* at 384-85.
39. 705 F.2d 1005 (8th Cir. 1983).
40. *Id.* at 1011; *see also* Central Iowa Refuse Sys., Inc. v. Des Moines Metropolitan Solid Waste Agency, 715 F.2d 419 (8th Cir. 1983).
41. 726 F.2d 1430 (9th Cir. 1984).

42. *Id.* at 1433-34.
43. 455 U.S. at 71, n.6 (Rehnquist, J., dissenting).
44. *See* Central Iowa Refuse Sys., Inc. v. Des Moines Metropolitan Solid Waste Agency, 715 F.2d 419, 425 (8th Cir. 1983); Gold Cross Ambulance & Transfer v. City of Kansas City, 705 F.2d 1005, 1014-15 (8th Cir. 1983); Town of Hallie v. City of Eau Claire, 700 F.2d 376 (7th Cir. 1983).
45. *Golden State Transit Corp.*, 726 F.2d at 1434.
46. *See, e.g.*, Golden State Transit Corp. v. City of Los Angeles, 726 F.2d 1430 (9th Cir. 1984); City of North Olmstead, Ohio v. Greater Cleveland Regional Transit Auth., 722 F.2d 1434 (6th Cir. 1983); Parks v. Watson, 716 F.2d 646, 663 (9th Cir. 1983); Central Iowa Refuse Sys., Inc. v. Des Moines Solid Waste Agency, 715 F.2d 419 (8th Cir.); Gold Cross Ambulance & Transfer & Standby Servs. v. City of Kansas City, 705 F.2d 1005 (8th Cir. 1983); Town of Hallie v. City of Eau Claire, 700 F.2d 376 (7th Cir. 1983); Pueblo Aircraft Serv., Inc. v. City of Pueblo, 679 F.2d 805 (10th Cir. 1982).
47. *See, e.g.*, Golden State Transit Corp. v. City of Los Angeles, 726 F.2d 1430 (9th Cir. 1984); Gold Cross Ambulance & Transfer & Standby Serv., v. City of Kansas City, 705 F.2d 1005 (8th Cir. 1983); Town of Hallie v. City of Eau Claire, 700 F.2d 376 (7th Cir. 1983); Scott v. Sioux City, 1983-1 Trade Cas. (CCH) ¶ 65,352, *on reconsideration*, 1983-2 Trade Cas. (CCH) ¶ 65,589 (N.D. Iowa 1983); Hybud Equip. Corp. v. City of Akron, 1983-1 Trade Cas. (CCH) ¶ 65,356 (N.D. Ohio 1983).

    Underlying the decision insisting on a greater degree of state authorization for municipal anticompetitive conduct may be the fact that the more heinous or hardcore the antitrust offense and the more anticompetitive the challenged activity, the less likely it is that the state legislature or supreme court clearly authorized the activity or contemplated the result.
48. In *City of Boulder*, Justice Brennan writing for the Court suggested that the treble damage remedy might be inappropriate in suits against municipalities. 455 U.S. 40 at 57 n. 20. Representative Fish has introduced a bill into Congress which would codify this suggestion and limit recovery against a municipality to actual damages plus attorney's fees. H.R. 3361, 98th Cong., 1st Sess. (1983). So far, however, no court has suggested that a municipality might be liable for anything less than treble damages and, in light of the language of section 4, it would seem that such a limitation would have to come from Congress, not the courts.
49. 455 U.S. at 58-60 (Stevens, J., concurring).
50. *Compare, e.g., id.* at 56 n.20 ("As we said in City of Lafayette, 'it may be that certain activities which might appear anticompetitive when engaged in by a private party, taken in a different complexion when adopted by a local government.' ") *with id.* at 65-68 (Rehnquist, J., dissenting).
51. 435 U.S. 679 (1978).
52. 455 U.S. at 71 (Rehnquist, J., dissenting).
53. *Id.* at 67.
54. Lochner v. New York, 198 U.S. 45 (1905).
55. 15 U.S.C. §15 (1982). In Affiliated Capital Corp. v. City of Houston, 700 F.2d 226 (5th Cir. 1983), *reh. granted*, 714 F.2d 25 (5th Cir. 1983), a Fifth Circuit panel reinstated a treble damage verdict against the Mayor of Houston after applying a per se rule to a territorial market division in a suit by an unsuccessful applicant for a cable television franchise. Query whether if the city remained in the case the court would have treated it differently on the per se issue or on the question of treble damage liability.
56. 1984-1 Trade Cas. (CCH) ¶ 65,883 (N.D. Ill. 1983); *see also* 46 Antitrust & Trade Reg. Rep. (BNA) 595 (N.D. Ill. 1984).
57. *Id.* at 65,718.
58. *Id.* at 596.
59. S. 1578, 98th Cong., 1st Sess. (1983).
60. The Thurmond Bill states, in part:

    > The Federal antitrust laws shall not apply to any law or other action of, or official action directed by a city . . . in the general exercise of its regulatory powers . . . but excluding any activity involving the sale of goods or services . . . in competition with private persons. . . .
61. Indian Towing Co. v. United States, 350 U.S. 61 (1955) (Federal Tort Claims Act).
62. *See, e.g.*, Fry v. United States, 421 U.S. 542 (1975); New York v. United States, 326 U.S. 572 (1946).

63. *Compare, e.g.*, United States v. Texas State Bd. of Public Accountancy, 592 F.2d 919 (5th Cir.), *cert. denied*, 444 U.S. 925 (1979) (compulsion standard) *with, e.g.*, First American Title Co. of S.D. v. South Dakota Land Title Ass'n., 714 F.2d 1439 (8th Cir. 1983) (clear articulation), *cert. denied*, 104 S. Ct. 709 (1984).
64. 714 F.2d 1439 (8th Cir. 1983), *cert. denied*, 104 S. Ct. 709 (1984).
65. *Id.* at 1454 (quoting *Gold Cross Ambulance*, 705 F.2d at 1013).
66. *See, e.g.*, Ronwin v. State Bar of Arizona, 686 F.2d 692 (9th Cir. 1981), *cert. granted sub nom.* Hoover v. Ronwin, 103 S. Ct. 2084 (1983); United States v. Texas State Bd. of Public Accountancy, 464 F. Supp. 400 (1978), *affd*, 592 F.2d 919 (5th Cir.), *cert. denied*, 444 U.S. 925 (1979).
67. *Id.* at 404.
68. 52 U.S.L.W. 4535 (U.S. May 15, 1984).
69. *Id.* at 4537.
70. *Id.* at 4538.
71. Rule 28(a) of the Arizona Supreme Court Rule (1973), provided that the Committee "shall examine applicants" on the subjects mentioned in the Rules and "recommend to th[e] Court for admission to practice." 52 U.S.L.W. 4535, 4536 (U.S. May 15, 1984).
72. 433 U.S. 350 (1977).
72A. 435 U.S. 389, 406-08 (1978).
73. 421 U.S. 773 (1975). *See supra* text accompanying notes 18-20.
74. *See* United States v. Title Ins. Rating Bd. of Arizona, 700 F.2d 1247, 1252-53 (9th Cir. 1983) (clear articulation standard); Sound Inc. v. AT&T, 631 F.2d 1324 (8th Cir. 1980) (applying both compulsion and clear articulation standards).
75. 421 U.S. at 791-92.
76. *See supra* text accompanying notes 15-17.
77. United States v. Southern Motor Carriers Rate Conference, 702 F.2d 532 (5th Cir. 1983) (en banc).
78. Turf Paradise, Inc. v. Arizona Downs, 670 F.2d 813 (9th Cir.), *cert. denied*, 456 U.S. 1011 (1982).
79. 702 F.2d 532 (5th Cir. 1983) (en banc).
80. *See id.* at 538 n.11.
81. *Id.* at 538.
82. *See supra* text accompanying notes 23-26.
83. 670 F.2d 813 (9th Cir.), *cert. denied*, 456 U.S. 1011 (1982).
84. *Id.* at 817-18.
85. *Id.* at 823 n.8 (quoting Cantor v. Detroit Edison Co., 428 U.S. 579, 594 (1976)).
86. 78 Civ. 5723 (S.D.N.Y. 1982) (available February 1, 1984, on LEXIS, Genfed library, Dist. file).
87. *Id.* at 12-15.
88. *Id.* at 14.
89. *Id.* at 12.
90. 1980-81 Trade Cas. (CCH) ¶ 63,675 (S.D.N.Y. 1980).
91. *Id.* at 77,627-28.
92. P. Rosenthal, Words & Values (1984).
93. *Id.* at vii.
94. *Id.* at ix.
95. *See, e.g.*, Gordon v. New York Stock Exch., 422 U.S. 659, 682 (1975) (quoting United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 350-51 (1963)).
96. Interestingly, despite the apparent increase in the exposure of state agencies to antitrust liability under the state action doctrine, twenty-three states including the State of Colorado supported the petitioner in *Community Communications Co. v. City of Boulder*, and urged the applicability of the antitrust laws to the City. Apparently the interest of the states in *City of Boulder* was, at least in part, a political attempt to recapture power over municipal affairs, rather than an interest in the enforcement of the antitrust laws. *See generally* 644 Trade Reg. Rep. (CCH) 5 (April 10, 1984).

CHAPTER 5
INTERNATIONAL ANTITRUST

Sanford Litvack+

Walter Barthold: We are going to start the afternoon program with an area that has attracted considerable interest in recent years, raising such weighty questions as why a tiny country like Switzerland cannot give full faith and credit to the Federal Rules of Civil Procedure, and other very knotty questions. Anyone here who has been practicing antitrust law and has not encountered the name of our next speaker should seriously consider going back and starting over. Our speaker is a Fellow of the American College of Trial Lawyers and a partner in the firm of Donovan, Leisure, Newton & Irvine. Under President Carter he served as Assistant Attorney General in charge of the Antitrust Division of the Department of Justice. In case your memory is short, you unanimously elected him Vice Chairman of this Section for the term beginning on June 1. He, as I say, will lecture on antitrust in international trade.

Ladies and gentlemen, it is my privilege and pleasure to present my good friend, Sandy Litvack.

SANFORD M. LITVACK

International trade and the problems associated with it have in fact been over the last several years probably one of the most important areas of antitrust and one of the greastest areas of concern. In recent years we have seen rising concern in American business and in Congress over America's weakening international market position. In truth, our trade deficit is larger today than at any time in this country's history. Some of us might not think that antitrust had an important part in that, but that is not the perception which is widely held by Congress and by the business community.

As a result, for some period of time the Congress has considered and the executive branch has had to deal with a series of proposals designed to deal with what they called the perception of the interference of antitrust with our international trade position. It is really interesting because this trend, this concern, has led to a variety of different proposals before Congress, which finally in 1982 enacted a law signed by President Reagan entitled the Export Trading Company Act of 1982.[1]

The law, which I shall be talking about as I go on, is an interesting development of something which had been going on both administratively and internally within the Department of Justice prior to that. As the congressional swell grew and as the business community made itself felt — and I can digress and tell you that in every administration, the business community through the Department of Commerce always sees a host of problems which could be solved if you could simply curb antitrust or something like that — in 1977 in an effort to respond to part of those concerns, the Department of Justice published its "International Guidelines."[2]

What led to that was very simple. On the one hand the Department of Commerce and others were contending that antitrust had been an inhibitor of the United States' position in international markets. On the other hand you had people in antitrust, in law enforcement, asking for or demanding to see evidence that would substantiate that claim. When none was forthcoming — and there never has been any — the fallback of Commerce and others was always, "Well, whether antitrust does or does not inhibit trade, the perception is that it does and that is enough; and we should deal with that."

In response to that, the Justice Department for years pointed to its business review letter procedure as the answer. The Department would always say, "Just ask us for a business review letter, and that will solve the problem." And business would always say, "That's inadequate."

So in 1977, trying to take a different tack, the Antitrust Division of the Department published the International Guide. The Guide was a working statement of the Division's approach to international enforcement in the antitrust area. It tried to reassure U.S. export firms that they could reasonably cooperate and reasonably act in U.S. commerce without the risk of violating antitrust laws. The Guide and the Divison also implemented special procedures under the Business Review Act to try to deal with these problems.

But the fact is that the number of business reviews did not increase and the perception of concern did not decrease, and the move for further legislation continued.

In 1982, as I said, the Export Trading Company Act was enacted; it has four titles, two of which are most relevant to us. The first title basically just sets forth the act's purposes and its definitions, which apply only to that title, and calls upon the Commerce Department to promote export trade associations and companies.[3]

Title 2, which if you look back at the legislative history really was a very controversial one but not for antitrust reasons, amends the Bank Holding Company Act of 1956 so as to permit bank holding companies, bankers, banks, and BHC Act corporations to move directly into the export business by acquiring or forming export trading companies.[4] There was a great deal of controversy over that, largely within banking circles.

Title 3 was what was at the heart of the act to start with.[5] Title 3 provides a new procedure for approval of joint export activities through the mechanism of a Commerce Department certificate of review. These certificates, when issued, would give a qualified exemption from federal antitrust laws for conduct specified in and complying with the certificate's terms. The Antitrust Division is an important factor in that procedure because its approval is required. The applicant, in order to receive the certificate, must demonstrate that its export trading activities will not result in a substantial lessening of competition in the U.S. or restrain domestic competitors' export trade, and that they would not constitute unfair methods of competition or include any act that reasonably may be expected to result in a sale for consumption or resale in the U.S. of the goods in question.

I shall come back and go into that in more detail — but in short there is a certificate procedure whereby if the applicant meets the standards so that a certificate is granted with the Department's approval, the applicant will have a qualified immunity under the antitrust laws.

Title 4 is really totally different and was always a different issue and a different act.[6] But it is not surprising that when Congress went into conference on these bills, title 4, which was a separate statute, found itself lumped with title 3.

Title 4 is strictly jurisdictional. It applies a jurisdictional rule of reason test to cases under the Sherman Act and the FTC Act. It does that by amending the laws so as to provide that in order for activity to be within the jurisdiction of our laws, it must have a direct, substantial, and reasonably foreseeable effect on domestic commerce or other American exporters.

In analyzing any of these statutes from the point of view of an export trade problem, assessing the applicability of title 4 is probably the key because it applies automatically and universally to any non-import trade with foreign nations, whereas title 3 applies only to American individuals and firms who seek the Commerce Department clearance for their export activities. Title 4 is jurisdictional and goes to the heart of the antitrust laws.

Interestingly, title 4 — the direct, substantial, and reasonably foreseeable test — is in reality copied from the International Guide published by the Antitrust Division in 1977. It represents a codification of Justice Department policy dating back to 1977.

Title 3 really is kind of a strange animal because certification is useful only when you find in the first instance that you are subject to either the Sherman Act or FTC Act under title 4. If you have conduct or an activity that is not going to have a direct, substantial, and reasonably foreseeable effect, you are not subject to the law at all. The Sherman and Federal Trade Commission Acts would not apply. If you do, then you may — *may* — come under title 3.

You may also want to use title 3 if the conduct falls under antitrust laws other than the Sherman and FTC Acts, for instance the Clayton Act.

And finally, probably the most important use of title 3, when all is said and done and the one that if you look at what has happened to date is the reality of it, is when, for some reason that no one can ever describe, you would like the government stamp of approval even though it may not do anything for you. And that is probably the greatest use to which title 3 is ultimately going to be put.

Title 3 leaves the Webb-Pomerene Act, which has been on the books for so long and has fallen in so much disfavor, intact as it is. The Webb Act exempts from the antitrust laws, as you know, all acts of Webb associations, whereas title 3 gives antitrust immunity for specific conduct set forth in the appliction.

Those people who are eligible under title 3 are basically American individuals, partnerships, corporations, state and local government entities. The groups that have applied so far have included such important basic industries as catfish farmers, commercial truck sellers, etc. We have had about eight applications so far.

One thing that you must show in getting a certificate is that the conduct in question is — and I am not quoting but paraphrasing — not reasonably likely to adversely affect U.S. commerce. Of course, you will recall that if it is not reasonably likely to affect U.S. commerce, it is probably not subject to the Act in the first place. That inconsistency has not seemed to bother anyone to date except the Department of Justice, which, I think, has been left querulous at why they receive these applications.

One unresolved area that anyone must face when going for a title 3 certificate is the duration of the certificate itself — how long is it going to be? Is it forever? Is it for a fixed period of time? Should it be renewable under some schedule? Well, no one really knows for sure. To date, the Department of Justice has approached it with some skepticism, recognizing that while it might be safe to try to predict what will happen over the next five years or so in any given certificate, it is a different issue if you are giving a blanket approval to a particular kind of conduct.

I ought to digress and say you also have another interesting balancing question. On the one hand, you would like the certificate and the conduct to be covered to be as broad as possible. On the other hand, it seems reasonably clear that a lack of specificity yields two problems.

First, the Justice Department has said a lack of specificity will or may lead to a refusal to grant the certificate.

Second, a lack of specificity may mean at a later time when challenged before a court that the court is going to be troubled by exactly what conduct was immunized, because all that is immunized is conduct.

So there is a balancing that has to be done and has to be worked out, and neither the rules nor the statute are very helpful in doing that except in generalities to say, as you would guess they would say, you should be as specific as you have to be to enable us to make a judgment, which does not tell you very much about how specific you have to be. But it is a real concern.

Assuming for a moment you are specific, and assuming for a moment a certificate is going to issue, the time problem I alluded to becomes crucial. To date the Departments have been requiring periodic reports and giving themselves the right, much as they would have for instance under a consent decree, to come in and look at data that might be relevant as time goes on.

I would suggest that another thing that you will probably see before long is actual time limits put within the certificates themselves, much akin to what is done in consent decrees where a ten-year time period is now commonplace. You will probably also see continued provisions for right of access and you may have an expansion of the reporting requirements.

One who is not enamored with the Act, as I am obviously not, must digress and say isn't it interesting that business, which wanted the certificate procedure and was concerned about paper work, now must have an ongoing reporting requirement. Someone told me that Secretary Baldridge had said when the Act was passed that it would create 300,000 new jobs. I thought they would all be in the Commerce Department.

Title 3, as a qualified exemption, does provide judicial review and judicial challenge in the federal district courts. First, of course any person may sue in a district court to challenge either the issuance, the denial, the revocation or the modification of a certificate.[8] When I say any person, I mean any aggrieved person. I shall come back and put further qualifications on that too.

Because a person is defined as a U.S. resident, a U.S. business, or state and local government,[9] it would appear that foreigners probably cannot challenge the issuance of certificates, which is not out of line with what you would expect if the Act was designed to encourage U.S. businesses to band together and to be able to be more effective abroad. Challenges to certificates would logically and likely be limited, as they are, to U.S. citizens. In addition, the government itself, while not able to prosecute criminally, may, in extreme circumstances where the public interest so requires, challenge or seek to set aside a certificate which has been issued.[10]

In terms of individuals or persons, if you will, as defined, they may, as I said, sue either to have an issued certificate set aside, revoked, or modified, or in the case of the failure to grant one, to have it granted. So, too, a person may sue challenging conduct as being ultra vires, i.e. outside the scope of whatever the particular certificate required. And finally, I suppose as part of that trilogy, a person could sue and seek damages for injury sustained as the result of a wrongful issuance of a certificate.

Now Congress was clearly of a mind to discourage that kind of suit and encourage maximum security, if you will, or at least the perception of security to a business receiving a certificate. Indeed, one of the constant complaints about the prior procedure was not so much that the government would sue if you went ahead with a joint venture — whether you used or did not use the business review procedure - but rather that under our treble damage statutes some private litigant would come along and sue. The exposure and the risk of that, it was argued, was inhibiting. That is one of the things that title 3 was designed to deal with, and it dealt with it in a very particular way

One of the ways it dealt with it was to provide that if a private person sued to challenge conduct within the scope of certificated activity, arguing that certificate should not have issued and claiming damages, the plaintiff will (1) only be able to receive single, not treble, damages;[11] and (2) run the risk that the plaintiff will be assessed attorneys' fees if it should lose.[12] This is the first introduction, if you will, of the reverse concept of attorneys' fees — generally speaking, only plaintiffs receive attorneys' fees in a successful case. Now you would have a situation where the defendant would receive attorneys' fees were the plaintiff unsuccessful — a clear disincentive for the bringing of such cases and recognized as such.

Treble damages and the usual kinds of remedies are all still available if the act is ultra vires in terms of the certificate or if the allegation is, for instance, that the defendant did not reveal to the government the true facts. To use a bad analogy — fraud on the Patent Office — where you have not told the facts which were relevant to the issuance of the certificate, the defendant would not only be subject to the possibility of treble damages and the revocation of the certificate but probably your friendly government would come back into it if that could be established.

Private treble damage cases and the private suits generally have not yet arisen. Indeed, to date there have only been a handful of applications under title 3. That could well be because the certainty offered by the certification may well turn out to be more procedural than substantive.

While, to be sure, the applicant can make his case before the enforement authority, Justice and Commerce, the fact is that at the end of the day a court challenge may still await. While it is true that there are certain disincentives, as I said, to private suits, those disincentives are not perhaps sufficient to assure that no litigation will result. Indeed, as I pointed out, in many cases the certificate will be of little use whatsoever for a variety of reasons.

On the other hand, there are times when certification may be useful. For instance if the conduct is under the Clayton Act, including section 7, certification may well be beneficial because then title 4 doesn't come into play at all. Under title 4, which we talked about earlier, the direct/substantial test is of some comfort in jurisdiction in the first place.

One uncertainty which ought to be mentioned, particularly in the area of title 3, which creates a problem is the fact that the Department of Justice has been concerned all along — and has tried to call this to Congress' attention when passing the law — with the so-called spillover effects of this export activity. Let me take a step back.

Generally speaking, most of the kind of conduct that is either going to be covered under title 3 or that anyone is talking about has always been perceived by the government enforcers and probably by most people who have looked at it not to be within the ambit of the Sherman Act and not itself sufficient to cause a problem. The concern has always been the so-called spillover. When you have people banding together, whether through a common agent or otherwise, to engage in permissible export trade, one must necessarily be concerned about the spillover effects of that combination back in the United States. And the statute and the certificate procedure really does not deal with that issue because to the extent that there is still this spillover and a case can be made out, liability or potential liability still exists.

One final thing ought to be mentioned. If one goes through the title 3 procedure, as you would have guessed and as I did not mention, there is publication in the Federal Register.[13] If you have conduct which is in a gray area or which might raise concern, one thing you must recognize is that by this publication you are waving a red flag at others who might seek to challenge. Now you might say, "Yeah, but if you get the certificate, aren't you protected?" Well, you are qualifiedly protected here in the U.S., but as I shall mention in a second, the world does not end there.

You are not protected from the EEC, for instance. And if you are publishing or about to embark upon an activity which raises questions under their law, the publication in the U.S. will signal that.

So, too, you are not protected by this legislation, as you cannot be, under other countries' laws. And again, this may well serve as a red flag to a variety of other interests that may then come into play.

Finally, of course, no matter what they say, there is the regulatory lag problem. By putting it in the Commerce Department, the procedure has not speeded up any. And the complaints that existed and that do exist concerning the need for red tape and filing and the delay in reacting quickly to international problems exist just as much now and perhaps more so now under the certificate procedure as they ever did.

Thus, when one is considering whether or not a certificate is useful or appropriate, one of the things that must go into the mix is the business give-ups that are necessarily going to result from that procedure.

Let me talk a little bit more, if I may, about title 4 because, as I said at the outset, that certainly in Sherman and FTC Act terms, is in fact the heart of the matter. I mean it really is a Catch-22. If you have conduct that is not covered by title 4, you don't worry about title 3. And if it is covered by title 4, I bet you are not going to get a certificate under title 3. So title 4 really becomes the focal point of what anyone ought to be looking at. Is the conduct in question subject to the Sherman Act?

As I told you earlier, title 4 represents a codification of the Department's enforcement position — that in order for there to be jurisdiction (and we are talking about subject matter jurisdiction at this juncture), there must be a direct, substantial, and reasonably foreseeable impact on U.S. commerce or U.S. importers.

We start in this whole area with the *Alcoa*[14] test and Judge Hand and we move through a variety of cases over the years, through *Timberlane*[15] and *Mannington Mills*[16] and a host of them which tended to add confusion to the jurisdictional test that would be applied. These cases, it was said, tended to confuse American businessmen in their efforts to compete abroad, due to their concern that activity which only had a peripheral or tangential effect here would nonetheless subject someone to treble damage liability — not an insubstantial or unfair concern. While the Justice Department had adopted a rule similar to the statute in 1977, the fact is that that, of course, was not binding on the courts. And, if one looks at the court decisions, one finds a number of decisions that purported to or did assert jurisdiction in situations where the direct, substantial, and foreseeable test could not be or was not in fact met. In this case, title 4 gives some meaning, as it is a universally applied statute.

While in fact title 4 offers no assurance that there would not be proceedings, for instance, under the Clayton Act, section 7, or under some other statute, the fact is that the enactment of that statute probably signals to the courts a congressional intent to hold back, if you will, on our jurisdictional reach as we try to make ourselves more attractive in international markets. And that leads me to point out that there are, of course, two sides to the coin.

On the one side, we are trying to make ourselves better competitors in the world market which many people believe means, in some cases, aggregating, and combining skills, talents and attributes of various companies and businesses in export trading companies. The standard in this area has always been the Japanese. You can't have a discussion about this without someone pointing to Japan and saying, "Look how the Japanese do it." So as we look to the world market on the one hand, we want to position ourselves and give immunity under our laws.

The flip side of that has been the reaction of other countries to the imposition of our laws upon activities, people and things which in their view at best, tangentially or remotely, affect United States foreign commerce. Here, too, it is important to deal with perception as well as fact. Title 4 in part does that, dealing with part of the perception.

Nonetheless, it comes too late perhaps. And certainly with respect to private suits — the government policy was not totally relevant — it comes too late to have avoided a number of statutes, administrative rulings, and laws passed in other countries designed to block or meet our antitrust intrusion as seen by the foreign countries.

I am talking particularly about the various blocking statutes and so-called claw-back statutes which have created — certainly the blocking statutes have — enormous problems not just for private litigants in the spate of their litigation but for the judicial system as well. And probably there has been no better example of this quagmire in which we find ourselves than the recent *Laker* controversy.

As you know, in that case there was initially a criminal investigation by the Department of Justice and a related civil suit seeking almost two billion dollars in damages brought in Washington, D.C. by the liquidators of Laker. The essence of the charge, both in the complaint and the subject of the investigation, is an alleged predatory pricing conspiracy to drive Freddie Laker out of the business. Also in the same alleged conspiracy group was at least one airplane manufacturer which allegedly entered into the conspiracy to prevent Laker from completing a refinancing deal.

What happened there is almost a casebook illustration of how everything can go wrong.

The case in D.C. was assigned to Judge Greene. Since there are three Judge Greens in D.C., it is the Judge Greene of *AT&T*[18] fame. Early on in the case two of the British defendants brought suit in the U.K. high court for declaration of non-liability in the *Laker* U.S. antitrust case, and they sought a permanent injunction preventing Laker from going forward with the U.S. case and an injunction preventing Laker from interfering with the British court proceedings.

Well, those of you who know Judge Greene or know the case also know that he reacted very prompty to that and he issued his own injunction preventing the other defendants from taking any action in the foreign forum to try to interfere with the jurisdiction of his court. Meanwhile, Laker's liquidators appealed in the U.K. and were successful in convincing the Queen's Bench that the U.S. federal court did have jurisdiction and there was no basis for British judicial interference with those proceedings. However, they left out British administrative interference.

True to form, an administrative order was issued by the British government which said in essence that no one could comply with orders to furnish commercial information related to the U.S. civil case or the criminal proceeding. They entered another order in the U.K. saying that anyone who carries on business there cannot comply with any requirement or prohibition imposed pursuant to the U.S. antitrust laws which would contravene the previous general orders.

The British court then said, "Okay, we agree that the U.S. federal district court has jurisdiction and perhaps that is even the better forum, but the administrative rulings by the British government made it impossible for the defendant to carry on a defense in the U.S. proceedings." So when asked to resolve these conflicting directives, the British court did the only thing it could think of. It enjoined Laker from continuing with the U.S. prosecution against the British defendants.

Now Laker has filed an appeal, and that is going to proceed. Meanwhile, here we are back with Judge Greene who finds himself in a situation where parties are operating now under orders which prohibit them from disclosing information and prohibit the plaintiff from proceeding with the lawsuit.

Judge Greene, has now appointed an *amicus curiae* to suggest ways out of the deadlock. And he has been critical of the British tribunal, calling its actions premature and improper even on its own terms. He pointed out that the documents may never be needed, and he stated that the crux of the problem is that as a consequence of the actions of the British officials, the adversary process before his court has broken down. He listed a variety of options that he might take including appointing a trustee for the liquidator to proceed with the case.

It is obvious as this exchange of legal volleys goes on, airplanes may become obsolete while the courts try to figure out how they are going to proceed.

But the strength in the will and the outrage of the British is, I assure you, very real. Without commenting on its validity or invalidity, it is real. The blocking statute involved there — the blocking action involved there — is not, as you well know, unique. It grows out of a situation which, from the standpoint of the British, has existed since at least the first instance of extraterritorial application of U.S. antitrust laws. And the British will be quick to point out, as I have heard them do, that it is the United States that has opened that box, not the British. That is a problem which is not going to be readily resolved. And as I say, it is not limited to the British; but the *Laker* situation is probably as confusing and as complex an illustration of it as one can see.

When you combine those blocking statutes with the so-called claw-back statutes, you have an interesting combination. Claw-back, as you know, is basically the British way, in this case, of dealing with our treble damage laws. What they did in essence was say that if you are sued in the U.S. and have to pay treble damages, you can turn around and sue that plaintiff, assuming they have assets in the U.K., and recover back two-thirds of what you paid out, thereby effectively reducing treble damages to single damages, which is something a lot of people have been trying to do in this country for years. It is just a complicated way of accomplishing the same thing.

It is not uninteresting to note that while the United States and the Department of Justice have reacted with outrage to the notion that the British statutes could do this and the British courts would attempt to do this, the fact is that this does go hand in hand, at least time-wise, with a general debate or movement in this country to detreble in the first place. Certainly, as you will hear later, there are statutory proposals to detreble in some areas. There are conversations and proposals generally to detreble in all areas. And what you have here is a foreign counterpart with those countries seeking to be certain that treble damages cannot be collected abroad.

Probably the impetus for all of this was the *Uranium Cartel*[19] litigation which spawned so many of the blocking statutes and claw-back statutes and generally played havoc, I must say, with relations with those countries that were involved.

Not too long ago when talking about the claw-back status of Britain and France, one U.S. observer stated that it provided the defendant with a virtually automatic judgment in the home country courts against the American plaintiff for the penal two-thirds. The British have stated that as far as they are concerned, the provision came into being as a defensive measure and would only apply to a British company's British assets. Sir Haver, the Attorney General of England, said, "We do not for a moment seek to tell this country how to handle antitrust cases. But in our country we believe that civil matters should never get triple damages." With that in mind, it would seem unlikely that one is going to have a great deal of success in reversing the British on that issue.

One additional note ought to be mentioned in moving out of the British area and talking about the reaction abroad generally. Walter mentioned why a country like Switzerland gives us so much trouble when it comes to getting documents. And you could add Australia and Britain and our good friends in the north. Canada, who also do not like to part with their documents, and a host of other countries. But in some ways the Japanese have really been the most interesting. They are the most interesting because the dialogue always goes on and there is never a confrontation. Theie is just never progress either.

(Laughter)

The Japanese have a view of our antitrust laws that is not inconsistent with or very different from that of most of the European countries. The treble damage provisions disturb them. And most of all, of course, they have been terribly concerned about what they perceive to be as our extraterritorial jurisdiction.

This is an ongoing problem, although relations in an antitrust sense with the Japanese have always been close and cordial. Agreement after agreement, understanding after understanding is generally reached providing for a wide exchange of information and dialogue between the enforcement agencies in both countries. The fact is, however, that really very little gets done in that regard and the Japanese, above and beyond all, are terribly protective of their industries and their companies and their markets.

The Japanese, of course, have their own antitrust laws and one should not be too surprised if in the not too distant future one of our export trading companies with all our antitrust immunity should find that somehow the Fair Trade Commission of Japan thinks, shockingly enough, that they have violated Japanese antitrust laws. It will be interesting to see the arguments being made in the office of the counterpart of the assistant attorney general of Japan by our companies.

I ought to digress finally and talk about the EEC because that is the last element of this equation. One thing that ought to be said and people frequently ask is: what are the relations or what is the liaison between our antitrust department and the EEC? How do exchanges of information work? Is there a high degree of exchange of information?

The truth is that there is in fact no formal mechanism for exchanges or participation by the two agencies. Both agencies recognize that they are of the same spirit generally in that they are enforcement agencies enforcing a concept of antitrust and competition. On the other hand, both agencies recognize that they work for different sovereigns under different statutes and under different political and economic conditions. Hence, the exchange and interchange of information is really more personal and informal than mechanical and regular.

So when one talks about movements in the EEC, one is often talking about something very different and apart from whatever the mood may be in the U.S. Certainly, at its inception, the EEC looked heavily to the U.S., the U.S. antitrust laws and the U.S. Department of Justice as kind of the fountain of all knowledge in this area. As time has gone on, that fountain has dried up, I think, in their minds, and they tend more to strike off on their own. And indeed there are some who would tell you that there is more vigorous enforcement today in the EEC than there is in the Department of Justice or the Federal Trade Commission.

Without commenting on whether that is so or not so, the fact is that they do take very different courses for all the reasons I mentioned — political, economic and historical. Some things, however, ought to be mentioned because they directly impact on our business-doing ability abroad. And while I half jokingly hypothesized the Japanese Fair Trade Commission coming after one or more of our companies, it is much easier and much more serious to hypothesize the EEC taking a very different view of our immunity and our approach.

It is fine for us to say, "As long as it doesn't substantially hurt the U.S., it's got our blessing." One may say that if it is effective, it is going to substantially hurt somebody else and maybe that somebody else is going to care — and that might be the EEC.

The EEC has been active in a variety of areas. Probably the one that is most interesting and most lively is in the intellectual property area, whether copyrights or patents. One ought just generally mention the kind of trend that has been going on there because it is not terribly different from ours, it just develops differently.

Initially in the EEC, patent licensing was thought to be and was basically approached as being per se lawful with a variety of restraints. But as time went on and as the Commission became more active in the 1960's and 1970's, it started to take an approach very similar to our courts — banning a variety of practices as what we would call per se illegal. And as the mood here changed, so too the mood there changed. In 1979 the Commission talked about establishing a block exemption for patent licensing. And that block exemption, which is still sort of hanging out there, has been put in limbo because of the *Maize Seed* judgment.[20]

In the *Maize Seed* case the court took an approach which injected into the patent area the rule of reason test. Remember the progression. First the restraints were basically per se unlawful. And you get a Commission reaction which says let us put in a block exemption that would make the restraints totally lawful. Now *Maize Seed* comes along with a rule of reason approach, putting the block exemption on the back burner for a while.

Thus what you have in the EEC is basically a rule of reason test on patent restraints. The main issue which arises in all these cases is whether there is a restraint upon competition under patent licenses between and among member countries. The approach taken is that an exclusive license, referred to as an open license (i.e. where all you have is an exclusive) will generally be acceptable, and all right. What they call a closed license, which would generally mean where there is an effort to preclude parallel importers from other countries who are also licensed from shipping into the country, is more suspect and probably is not all right. Not an unusual development given the developments that are occurring in our own laws.

One development which has occurred there, however, which ought to be mentioned because it is inconsistent with ours and potentially significant to most of us, is the approach that they have taken to the law of attorney/client privilege which does pose a very different kind of problem.

I remember, as a personal aside, in 1980 when I was in Brussels and the issue of the attorney/client question had not yet finally been decided. There was a discussion or a debate about what the rule should be. I know I was struck — coming from the U.S. and from a private law firm background — and knowing how zealously we guard the attorney/client privilege and how many documents have at least the potential of privilege questions in them — at the vigor with which the Commission staff approached the problem in terms of the absolute inapplicability of and the frustration of the attorney/client privilege. It was their absolute conviction as a matter of approach that privilege was really something that ought to be basically read out in its entirety. They have not done that, but they have not gone too far from that either.

The privilege is a very limited privilege. And the privilege, as you know, really applies only a) to independent attorneys, not in-house, and b) only to attorneys who are admitted in the member states, not Americans. This poses all kinds of problems in terms of counseling clients, in terms of compliance programs both here and abroad, and in terms of developing and maintaining records of conduct and reasons for conduct.

Suffice it to say the one conclusion it leads you to is that when developing a compliance program or when developing a retention program, one must have in mind not merely the U.S. laws but one must have in mind very practically the foreign statutes, whether in other foreign countries or the EEC, which may come into play and which may end up being an invasion upon documents, an invasion upon legal advice, and an intrusion into process that we never envisioned. If we forget about that very important element of the law enforcement, we can do severe damage.

Thank you.

MR. BARTHOLD: Thank you very much, Sandy, not only for the time you spent with us today but for the very substantial amount of time and effort that your talk showed went into its preparation.

FOOTNOTES

* Donovan, Leisure, Newton & Irvine, New York City.

1. Pub. L. No. 97-290, 96 Stat. 1233 (1982) (codified in scattered sections of 12 & 15 U.S.C.A. (West Supp. 1984)).
2. Antitrust Div., U.S. Dept. of Justice, Antitrust Guide For International Operations (1977).
3. 15 U.S.C.A. §§ 4001-4003 (West Supp. 1984).
4. Bank Export Services Act, Pub. L. 97-290, 96 Stat. 1233, 1235-40, §§201-07 (1982)(codified in scattered sections of 12 U.S.C.A. (West Supp. 1984)).
5. 15 U.S.C.A. §§4011-4021 (West Supp. 1984).
6. Foreign Trade Antitrust Improvements Act of 1982, Pub. L. 97-290, §§ 401-403, 96 Stat. 1233, 1246-47 (codified at 15 U.S.C.A. §§6a, 4.5(a) (West Supp. 1984)).
7. 15 U.S.C. §§#61-65 (1982).
8. 15 U.S.C.A. §4015 (West Supp. 1984).
9. *Id.* § 4021(5).
10. *Id.* § 4016(5).
11. *Id.* § 4016(b)(1).
12. *Id.* § 4016(b)(4).
13. *Id.* § 4012(b)(1).
14. United States v. Aluminum Co. of America, 148 F.2d 416, 443-44 (2d Cir. 1945).
15. Timberlane Lumber Co. v. Bank of America, N.T.&S.A., 549 F.2d 597, 608-15 (9th Cir. 1976).
16. Mannington Mills v. Congoleum Indus., 595 F.2d 1287, 1291-92 (3d Cir. 1979).
17. See Laker Airways Ltd. v. Sabena, 1984-1 Trade Cas. (CCH) ¶65,885(D.C. Cir. 1984).
18. United States v. American Tel. & Tel. Co., 552 F. Supp. 131 (D.D.C. 1982), *affd mem. sub nom.* Maryland v. United States, 103 S. Ct. 1240 (1983).
19. Nungesser v. Commission, 1981-83 Comm. Mkt. Rep. (CCH) ¶8805 (June 8, 1982).

CHAPTER 6

VERTICAL RESTRAINTS — RECENT DEVELOPMENTS

William T. Lifland+

There have been a number of recent developments with respect to the antitrust treatment of restrictions on dealers, usually called vertical restraints. This paper considers two such restraints: resale price maintenance and restrictions on dealer territories.

I. Resale Price Maintenance

Since 1911 agreements between suppliers and dealers to maintain resale prices have been held unenforceable.[1] Efforts to implement such agreements by termination or other coercive action have been held illegal.[2] Action taken pursuant to agreement has been distinguished from action taken unilaterally, with unilateral action being upheld. This is the so-called *Colgate* doctrine, which the Supreme Court has stated as follows:

> A simple refusal to sell to customers who will not resell at prices suggested by the seller is permissible under the Sherman Act.[3]

As a strictly unilateral act cannot constitute a "contract," "combination" or "conspiracy" within the meaning of the Sherman Act,[4] this proposition seems self-evident. Nonetheless, as a practical matter, lawyers are rarely in a position to advise their clients to rely on it. In most cases, there will be additional facts or so-called "plus factors" going beyond the mere refusal to sell to a dealer. Enlisting additional participation in the program, or reinstating terminated dealers on assurance of future compliance, may be found "plus factors" sufficient to bring the conduct within the Sherman Act[5] and thus per se unlawful. Frequently, a complaint of a terminated dealer will allege that his termination was the result of his failure to adhere to such an assurance, or was the result of the supplier's agreement with other dealers who insisted on his termination in return for their continued observance of the manufacturer's suggested prices.

It is only in circumstances where no such conspiracy can be alleged or proved that the so-called "*Colgate* doctrine" — that strictly unilateral action is permissible — has relevance. Yet it has always presented some conceptual problems. To some, the seller's unilateral statement of policy, coupled with the customer's compliance, constitutes a tacit agreement no different in principle from an express agreement. Particularly when the statement of policy is supplemented by threats of termination for violators, the distinction between lawful unilateral and unlawful bilateral conduct has seemed difficult to draw.

A. *Russell Stover*

Accordingly, despite the relatively narrow scope for application of the unilateral conduct rule, the FTC set out in 1980 on a course of litigation which was designed to secure judicial reconsideration of the *Colgate* doctrine. The FTC brought an administrative complaint against Russell Stover Co., a chocolate manufacturer, which sold its products through thousands of retail dealers.[6] The facts were contained in a 24-paragraph stipulation which seemed contrived to pose the legal issues starkly, without the myriad opportunities for findings of conspiracy typical of records of actual commercial dealings. The stipulation stated that it was the manufacturer's policy to designate resale prices, and that the manufacturer announced to prospective retailers that it would refuse to sell to a retailer which it reasonably believed would undercut its designated prices. The manufacturer did not request or accept express assurances from prospective or existing retailers with respect to compliance with the designated prices. It simply refused to deal with retailers it thought would do so and stopped selling to retailers because they had done so. The stipulation also indicated that about 94% of the manufacturer's products were sold at retail at or above the designated prices, and that a substantial number of retailers desired to discount the products, but did not do so in order to avoid termination.[7] The manufacturer claimed that its policy was within *Colgate*, there being no pricing agreement with retailers.

Analyzing the *Colgate* rule in light of later court decisions, the FTC concluded that the manufacturer's conduct was a violation of the Sherman Act.[8] It noted that a number of decisions implied that repeated threats of termination went beyond "a simple refusal to sell."[9] But it also noted that these cases could be distinguished from the case before it and it therefore based its conclusion on the broader ground that the logic of later decisions made the "plus factor" required to convert unilateral conduct into a Sherman Act conspiracy superfluous when unwilling compliance resulted from threatened termination. It stated that the plus-factor requirement had "evolved to serve as a device for the courts to infer the presence of coercion, a concept that the court has utilized to connote bilateral behavior." It concluded that the manufacturer's threats of termination, followed by unwilling compliance, followed in turn by continued dealing, was the "antithesis of unilateral behavior", and thus constituted a conspiracy to maintain resale prices, which was per se illegal.[10] The FTC made an exception for the manufacturer's initial selection of dealers, and stated that the manufacturer was free to exercise unilateral discretion to distribute only through non-discounters. The basis for regarding this action as unilateral was that initial customer selection, standing alone, did not raise an inference of unwilling compliance on the part of the distributor.[11] Similarly a manufacturer's dissemination of suggested retail prices, when freely complied with, was not regarded as bilateral conduct, because of the absence of coercion.[12]

Although the FTC's reassessment of the *Colgate* doctrine was the most significant part of its decision, it also considered another theory upon which its staff alleged that the stipulated conduct constituted bilateral action within the meaning of the Sherman Act. Relying on the Supreme Court's 1939 *Interstate Circuit* case,[13] the staff alleged that each dealer had in effect been invited to participate in a scheme to charge particular prices, and had accepted by participating in the scheme. The "invitation and acceptance" theory was rejected by the FTC with the observation that the issue in *Interstate Circuit* was whether a horizontal combination among distributors could be inferred from the express vertical agreements which were admitted to exist.[14] In the absence of evidence that the dealers played a role in initiating the plan, or that the manufacturer wished to avoid horizontal competition, the FTC stated that the evidence did not warrant a finding of vertical-horizontal combination as in *Interstate Circuit*. It also noted that such a finding would call into question the legality of many vertical agreements between suppliers and dealers by raising an inference of a horizontal inter-dealer combination.[15]

The *Russell Stover* decision was, as expected, appealed. The Eighth Circuit reversed the FTC's order, noting that the more recent cases might indeed, as the FTC had indicated, foreshadow the eventual overruling of *Colgate*, but stating that if *Colgate* was to be overruled or modified, it was "for the Supreme Court, not this court, to so declare."[16]

This appellate ruling could not have been entirely unanticipated. One might have thus expected that a petition for certiorari would be promptly made to the Supreme Court. No such petition, however, was filed. Between the FTC's decision on the merits, in July 1982, and its decision with respect to seeking certiorari, in December 1983, two new commissioners had joined the Commission. They voted with the Chairman, who had dissented from the original decision, in deciding not to carry the matter further.[17] Interestingly enough, the Chairman's dissenting statement, which seems to have ultimately carried the day, was not based on whether an antitrust combination or conspiracy could be established on the basis of the stipulated record. The Chairman did not disagree with the majority on that point. Instead, he parted company with the majority's condemnation of the conspiracy, once found, as per se illegal.[18] The Chairman expressed the view that the Supreme Court had implicitly recognized that the rule of per se illegality for resale price maintenance sweeps too broadly, and had devised a "safety valve" in the form of the *Colgate* doctrine. While this doctrine was "far from satisfying," it nonetheless seemed to the Chairman to avoid some of the "mischief that results from application of the per se rule." In his view it would have been better to address the inappropriateness of the per se rule itself.[19] The Chairman also criticized the majority's "coercion equals conspiracy" theory, noting that the stipulated record indicated that the respondent competed with at least seven other manufacturers, who presumably stood ready to supply terminated dealers, and that it could therefore be inferred that the dealers were not "coerced" to accept the respondent's terms but merely found them preferable to those of its competitors.[20] The use of the concept of "coercion" as the test of the existence of a conspiracy was also criticized, and a preference expressed for adopting a single definition of "conspiracy" for both vertical and horizontal arrangements, and basing the resulting antitrust conclusions on analysis of their competitive effects.[21]

B. Monsanto

Somewhat similar issues were involved in the second major development in the area of resale price maintenance, the Supreme Court's decision in *Monsanto Co. v. Spray Rite Service Corp.*, on March 20, 1984.[22]

Monsanto was a more conventional dealer termination case, brought by the terminated dealer to collect treble damages. The dealer claimed that he had been terminated as a result of a conspiracy between Monsanto and other dealers to maintain retail prices and that it was the complaints of the other dealers about his price-cutting which provoked Monsanto's action. Monsanto claimed that the termination was for other business reasons, generally relating to the adequacy of representation provided by the dealer. The case was tried to a jury and there were many contested issues of fact. The jury found in favor of the terminated dealer, and a judgment in its favor was upheld on appeal[23] The Supreme Court granted certiorari to resolve a difference among the circuits as to what evidence was needed to sustain a verdict for a terminated dealer in such circumstances.

The difference among the circuits related to the importance to be attached to complaints from other dealers that the terminated dealer was price-cutting. The Seventh Circuit had stated that if there was evidence of such complaints followed by a termination, it was permissible for the jury to infer the existence of a conspiracy.[24] Other circuits required evidence that the termination was actually in response to the complaints.[25] The Supreme Court ruled there must be evidence that "tends to exclude the possibility that the manufacturer and non-terminated distributors were acting independently."[26] More affirmatively, the court stated that the plaintiff should present evidence that reasonably tends to prove that the manufacturer and others had a "conscious commitment to a common scheme designed to achieve an unlawful objective."[27] The reason given for this evidentiary requirement was that it would be wrong to infer an agreement merely from existence of complaints or from termination "in response to complaints," since this would inhibit the manufacturer in the exercise of his right, under *Colgate*, to act independently. Complaints from distributors about price-cutters were recognized to be natural and unavoidable reactions of distributors to the activities of their competitors. It was to be expected that these reactions would be communicated to manufacturers in the normal course of operations. Thus to permit concerted action to be inferred from termination after complaints would inhibit management's "exercise of independent business judgment."[28]

Applying its evidentiary requirement to the facts before it, the Supreme Court found sufficient evidence to enable the jury to conclude that Monsanto and some of its distributors were parties to an agreement to maintain resale prices and terminate price-cutters. The Court cited evidence of an agreement between Monsanto and another distributor to charge Monsanto's suggested price despite the distributor's initial objection. It also referred to a distributor newsletter which it said could be reasonably interpreted to indicate such an understanding. As evidence that plaintiffs termination was pursuant to the understanding, it relied on evidence that Monsanto had informed the plaintiff of other distributors' requests that prices be maintained and had later explicitly threatened to terminate the distributor unless it raised prices.[29]

The *Monsanto* decision is significant on two counts. It reaffirms the manufacturer's right to unilaterally terminate a price-cutting distributor, a result which suggests that the FTC's *Russell Stover* initiative, if pursued to the Supreme Court, would not have been successful. The Court appears both to recognize and approve the existence of the unilateral right of termination. The Court stated:

> It is precisely in cases in which the manufacturer attempts to further a particular marketing strategy by means of agreements on often costly non-price restrictions that it will have the most interest in the distributor's resale prices. The manufacturer often

> will want to insure that its distributors earn sufficient profit to pay for programs such as hiring and training additional salesmen, or demonstrating the technical features of the product and will want to see that "free riders" do not interfere .... Thus the manufacturer's strongly felt concern about resale prices does not necessarily mean that it has done more than the Colgate doctrine allows.[30]

The second important feature of the decision is the Court's insistence that the plaintiff must do more than adduce "highly ambiguous" evidence to justify inferring an unlawful agreement between supplier and competing distributors leading to plaintiff's termination. This point is sure to lead to more litigation. In most situations one would expect evidence consistent with both unilateral and concerted action. If the Court is requiring evidence consistent only with concerted action, that would place a heavy burden on plaintiff.[31] If on the other hand, as is suggested in footnote 8 to the Court's opinion,[32] the plaintiff's burden is only to introduce "additional" evidence beyond complaints, the plaintiff's burden will be much lighter. The Court's opinion does not clearly address the nature of the additional proof required, and other courts will undoubtedly look in the first instance for evidence similar to that the Court ruled sufficient in *Monsanto*.

If only these issues had been involved in the *Monsanto* case, it would have attracted great attention from the bar. It became the subject of still more interest because of other issues which it did not resolve.

The Reagan administration's first head of the Antitrust Division, William F. Baxter, had been, like Chairman Miller, critical of the established doctrine that resale price maintenance is illegal per se. He had publicly suggested that the Supreme Court reconsider the issue.[33] It was not appropriate, in his opinion, for the Antitrust Division to attempt to provoke such reconsideration by attempting to enforce the doctrine where the Division did not consider that it would advance consumer welfare, so as to give the defendant an opportunity to ask for reconsideration. Such an approach was considered unsound. An alternative approach was to urge, as amicus curiae in a case involving private litigants, that the court overrule earlier precedents. *Monsanto* appeared to offer an opportunity to follow this course. In an amicus brief filed in the Supreme Court, the Division urged that the per se rule be replaced by a rule of reason, like that employed in the case of non-price restrictions. The Division argued that vertical price restraints do not differ in principle from other vertical restraints and that the manufacturer's imposition of such restraints may often advance consumer welfare by increasing interbrand competition sufficiently to warrant a sacrifice in intrabrand competition.[34]

The Supreme Court declined to reach this issue, observing that neither party had argued below that the rule of reason should apply to a vertical price fixing conspiracy.[35] However, the effort to raise the point provoked considerable controversy. A rider was attached to an appropriation bill prohibiting the Department from spending any funds for overturning the established law with respect to the illegality of vertical price fixing.[36] In compliance with this directive Mr. Baxter did not press the point in his oral argument before the Supreme Court.[37] This highly unusual legislative action is one indication of the depth of the differences in views as to the appropriate rule of law. Another is the fact that 46 state attorneys general joined as amici to urge the continuation of the per se rule against vertical price fixing.[38] Subsequent to the *Monsanto* decision, supporters and opponents of the Division's position in the per se controversy claimed to find some indirect support for their views in the Court's language.[39] It appears clear, however, that a definitive statement will have to come in another case. For the time being, the per se rule is likely to be applied by courts, and the various state attorneys general are likely to bring enforcement proceedings against resale price maintenance if the federal authorities do not.

II. Territorial Restraints

It will be recalled that the Supreme Court's 1977 *Sylvania* decision[40] ruled that non-price vertical restraints, such as limitations on the territory to be served by a dealer, were to be governed by the rule of reason rather than a per se rule. In *Monsanto* the Supreme Court commented that the need to insure the viability of *Sylvania* was an important consideration in its decision.[41] A natural question is whether the application of the rule of reason is likely to lead to declarations of legality. It is worthwhile, therefore, to review briefly the trend of decisions applying the rule of reason to non-price restraints.

Two older appellate court decisions upheld territorial restrictions on dealers in circumstances in which the suppliers had very modest market shares (below 5%) and there was evidence that exclusive territories were the only way to assure the supplier that the sales territories would be worked adequately, and in one of the cases, worked at all.[42] The preservation of exclusive territories, by definition, required the imposition of territorial restrictions. Where similar facts can be shown, there is good reason to expect that a restraint will be upheld.

Also likely to be upheld are various types of arrangements which may significantly promote interbrand competition while imposing little or no restriction on intrabrand competition. The best example is an "area of primary responsibility" clause, under which a dealer is made responsible for covering a particular territory and subject to termination for failing to cover it adequately, but is not prohibited from sales elsewhere. This type of arrangement does not restrict a dealer appreciably and thus should raise no antitrust problem whatever unless, of course, sales personnel misinterpret it as a restriction and apply it as such.[43] Similarly, a location clause, under which the location of a dealer's place of business is designated in the dealer agreement, but the dealer is not barred from selling by mail or telephone to customers in distant areas, will often restrict the dealer's freedom only minimally. It was this type of arrangement which was in issue in the *Sylvania* case. It was upheld on remand with the court commenting that a location clause was one of the "less restrictive methods" the manufacturer might have used, that it was likely to promote interbrand competition, and that the purpose was not to protect "dealers from price-cutters."[44]

Also arguably in the category of minimal restraints are so-called profit pass-overs, under which a distributor is permitted to sell in another's territory but is obliged to pay the other an amount reflecting its estimated cost of advertising or post-sale service. Assuming that the amount realistically reflects the costs involved, and is not intended as a penalty to make such sales impractical, it may be regarded as a salutary practice to avoid discouraging advertising and service on the part of dealers subject to incursions from others. There are, however, decisions both ways with respect to this practice.[45]

A more generalized test for applying the rule of reason to vertical non-price restraints has been suggested by Judge Posner, writing for the Seventh Circuit in *Valley Liquors, Inc. v. Renfield Importers, Ltd.*[46] Judge Posner reasons that if the supplier does not have sufficient market share to connote market power, no restraint it imposes on distributors will be contrary to consumer welfare. In *Sylvania*, for example, Judge Posner's reasoning would have resulted in automatic upholding of the restraints in issue, because Sylvania's market share was only about 5%. This approach, if adopted by other courts, would substitute for the economic analysis of individual situations a rule of law based upon the economic proposition that a supplier's interest in maximizing its own profits will normally cause it to make its distribution organization as efficient as it can, to the consumer's ultimate benefit. This approach in effect withdraws from antitrust scrutiny the relationship between supplier and distributor on the ground that the division of responsibilities and decision-making powers between them is of no concern to the ultimate consumer.

The opinion in *Valley Liquors* indicated that its approach was employed by the Fifth and Ninth Circuits,[47] which have indeed attached significance to the market power of the supplier, but have also considered other factors as well.[48] Thus the *Valley Liquors* approach cannot be treated as a generally recognized rule, but only as a provocative suggestion. It is likely that the *Valley Liquors* approach will be reflected to some extent in guides for assessing the legality of vertical restrictions that the Antitrust Division plans to issue in late 1984,[49] and will also become the subject of considerable discussion in other cases. An important issue, if the *Valley Liquors* approach is adopted by other courts, will be the degree of market share which is deemed to give rise to market power as well as the other factors which may bear on this determination.

A recent decision which may illustrate the application of the *Valley Liquors* approach where market power is found involves a firm with a 70% national market share.[50] Its termination of a distributor which operated outside its assigned territory was held to have been unlawful, with the court indicating that the absence of substantial interbrand competition made an adverse effect on intrabrand competition more significant to consumer welfare. It laid down a pattern for the prosecution and defense of a rule of reason case. It stated that plaintiff must prove, first, defendant's market power; second, the existence of intrabrand competition affecting price; and third, a restraint with effects substantially adverse to competition. Once plaintiff had proved these elements, defendant could in rebuttal attempt to prove that the restraint was reasonably necessary to achieve procompetitive purposes.[51]

In evaluating territorial restraints, it is well to recall that an arrangement which may appear on the surface to be vertical, and governed by the rule of reason, may in fact be horizontal, and subject to a per se rule. This issue has arisen in a number of cases where the supplier has operated to some extent as a distributor, and the restraints it imposes are challenged as horizontal restrictions. In general, courts have treated these arrangements as vertical where their primary effects are vertical.[52] Of much greater concern is the allocation of distributor territories, ostensibly vertical, but in fact adopted at the behest of distributors. An inter-distributor territorial allocation may be challenged as per se illegal if distributors originate the proposal and the manufacturer grants his endorsement to the plan.[53] An arrangement with exactly the same economic effect may be lawful, if unilaterally decided upon by the supplier and put into place by him. Like the distinction between price restrictions — which continue to be per se illegal — and non-price restrictions — which in many circumstances will be upheld — this distinction may appear overly technical and to make very serious consequences hinge on matters of minor importance. As in other areas of the law, however, small differences may have great importance. There thus continues to be abundant reason to review proposed distribution programs with counsel well in advance of placing them into effect.

FOOTNOTES

+ Cahill, Gordon & Reindel, New York City.
1. Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).
2. United States v. Parke, Davis & Co., 362 U.S. 29 (1960).
3. *Id.*, at 43, referring to United States v. Colgate & Co., 250 U.S. 300 (1919).
4. 15 U.S.C. §1 (1980). The statutory words "contract," "combination" and "conspiracy" are hereafter collectively referred to as "conspiracy."
5. United States v. Parke, Davis & Co., 362 U.S. 29 (1960).
6. The FTC's opinion and order in *Russell Stover Candies, Inc.*, Dkt. 9140, are found in CCH Transfer Binder, FTC Complaints and Orders — 1979-1983 at ¶ 21,933 (hereafter "RSC").
7. RSC at p. 22,354.
8. RSC at p. 22,370.
9. RSC at p. 22,363.
10. RSC at pp. 22,363, 22,370.
11. RSC at p. 22,369.
12. RSC at p. 22,366.
13. Interstate Circuit, Inc. v. United States, 306 U.S. 208 (1939).
14. RSC at p. 22,365.
15. *Id.*
16. Russell Stover Candies, Inc. v. FTC, 718 F.2d 256 (8th Cir. 1983).
17. 45 Antitrust & Trade Reg. Rep. (BNA) 1041 (December 22, 1983).
18. RSC at p. 22,372.
19. RSC at pp. 22,372-73.
20. RSC at p. 22,373.
21. *Id.*
22. 104 S.Ct. 1464 (1984) (hereafter "Monsanto").
23. 684 F.2d 1226 (7th Cir. 1982).
24. 684 F.2d at 1228.
25. See cases collected in *Monsanto*, 104 S.Ct. 1468 n.5.
26. *Id.* at 1471.
27. *Id.*
28. *Id.*
29. *Id.* at 1471-72.
30. *Id.* at 1470.
31. *Id.* at 1471.
32. *Id.*
33. 51 Antitrust L.J. 31-32 (1982).
34. Brief for the United States as Amicus Curiae, at 19-29.
35. *Monsanto*, 104 S.Ct. 1469 n.7.
36. See 45 Antitrust & Trade Reg. Rep. (BNA) 723 (November 3, 1983).
37. 45 Antitrust & Trade Reg. Rep. (BNA) 965, 967 (December 15, 1983).
38. *Monsanto*, Brief for 46 States as Amicus Curiae, Dkt. 82-914.
39. Colloquy between Frank Easterbrook, Esq. and Hon. John Seiberling at ABA Antitrust Section Meeting, March 1984.
40. Continental T.V., Inc. v. GTE Sylvania Inc., 433 UY.S. 36 (1977).
41. *Monsanto*, 104 S.Ct. at 1469 n.6.
42. Snap-On Tools v. FTC, 321 F.2d 825 (7th Cir. 1963); Sandura Co. v. FTC, 339 F.2d 847 (6th Cir. 1964).
43. This type of clause was even permitted by the final judgment in United States v. Arnold, Schwinn & Co., holding resale restrictions illegal per se, and later overruled by *Sylvania, supra.* 1968 Trade Cas. (CCH) ¶ 72,480 (N.D. Ill. 1968) (Sec. VI).
44. Continental T.V., Inc. v. GTE Sylvania Inc., 694 F.2d 1132 (9th Cir. 1982).
45. *Compare* Superior Bedding Co. v. Serta Associates, 353 F.Supp. 1143 (N.D. Ill. 1973); Ohio-Sealey Mattress Co. v. Sealey, Inc., 585 F.2d 821 (7th Cir. 1978), with Eiberger v. Sony Corp., 622 F.2d 1068 (1980).
46. 678 F.2d 742 (7th Cir. 1982).
47. *Id.* at 745.
48. *See* Muenster Butane, Inc. v. Stewart Co., 651 F.2d 292 (5th Cir. 1981); Cowley v. Braden

Industries, Inc., 613 F.2d 751 (9th Cir. 1980); Continental T.V., Inc. v. GTE Sylvania, Inc., 694 F.2d 1132 (9th Cir. 1982).

49. Address by Assistant Attorney General J. Paul McGrath, Association of the Bar of the City of New York, May 7, 1983.
50. Graphic Products Distributors, Inc. v. Itek Corp., 1983-2 Trade Cas (CCH) ¶65,670 (11th Cir. 1983).
51. *Id.* at 69,425.
52. *See* Donald B. Rice Tire Co. v. Michelin Tire Corp., 638 F.2d 15 (4th Cir. 1981); Abadir & Co. v. First Mississippi Corp., 651 F.2d 422 (5th Cir. 1981); Krehl v. Baskin-Robbins Ice Cream Co., 664 F.2d 1348 (9th Cir. 1982).
53. *See* Davis-Watkins Co. v. Service Manufacturing Co. 686 F.2d 1190 (6th Cir. 1982); Service Merchandise Co. v. Boyd Corp., 1984-1 Trade Cas. (CCH) ¶ 65,759 (1st Cir. 1983).
54. *See* Service Merchandise Co. v. Boyd Corp., *id.* at 67,106.

CHAPTER 7

JOINT VENTURES IN RESEARCH AND DEVELOPMENT AND ELSEWHERE

Taylor R. Briggs+

WALTER BARTHOLD: The theme of today's program, I have said before, is "A New Era in Antitrust." And once again, we have a perfect manifestation of that theme in our next topic; and we have a very fine speaker to deal with it.

Our next speaker is a fellow of the American College of Trial Lawyers, a partner in the firm Leboeuf, Lamb, Leiby & MacRae. He has been active in committee work for the Antitrust Law Section of the American Bar Association. He has lectured for many groups, including the Practicing Law Institute. He will talk to us on joint ventures in research and development and elsewhere.

Taylor Briggs

I. Introduction

There is a great flurry today, in Congress and in the press, about joint ventures for research and development. This paper reviews the basic antitrust standards applicable to joint ventures generally and the antitrust risks that joint ventures may pose, or that they are often believed to pose, because the R&D joint venture ought to be looked at as a part of that bigger picture. This review includes a consideration of recent actions in the joint ventures area by the Antitrust Division and the Federal Trade Commission. The paper then explores whether, in fact, the antitrust laws, and the risks of antitrust prosecution or private civil litigation, do significantly deter the formation and use of joint ventures; deter them to an extent that impairs the growth of the American economy or affects the ability of Americans to compete in international markets and against the influx of foreign traders. Finally, the current legislative proposals designed to alleviate the perceived antitrust burden on joint venture activities are reviewed and the questions posed whether they are necessary. Do the legislative proposals attack real problems, and do they provide sensible solutions?

This paper concludes that those who see the antitrust laws as imposing any significant bar to legitimate joint venture formation and activities are substituting mythology for history.

II. Defining the Joint Venture and its Role in the American Economy

First, it is necessary to define the "joint venture" that has become such a hot topic. In today's world almost any economic arrangement reasonably could be styled a "joint venture." After all, a merger results in a "joint venture" between previously unaffiliated concerns and their shareholders, but that is a more permanent and all-encompassing venture than is typically evoked by the term. At the other extreme, virtually all commercial contracts commit the parties to a joint undertaking for a limited purpose, requiring mutual cooperation and dedication of resources and a sharing of risks, just as a joint venture does.[1]

This is obviously too expansive an approach, but these two extreme examples do help to define the joint venture for antitrust analysis. A merger is not a "joint venture" because it entails the blending of two entities into one. In contrast, a joint venture involves propagation: the creation of a new entity by two or more persons or corporations — call them the parents — that will exist apart from its parents.

Like a commercial contract, a joint venture requires a substantial contribution from each participant, whether it be money, skills, facilities or other resources. But a joint venture entails more than that. It includes a sharing of control over the enterprise by the parents, which may not be present in a contract. And it creates some new commercial property or capability, such as a new product or new technology, which rarely will be involved in a simple contract.

To point to a current example: Rolls-Royce, Pratt & Whitney, Fiat Aviazione, Japanese Aero Engine Corp. and three other companies have agreed to create an entity this year, to be called International Aero Engines. The parents will contribute to the new entity technology and an initial financing of $1 billion, in order to create by 1988 a gas turbine jet engine. The proposed engine promises to be superior to what any one of the participants could have produced by itself. More specifically, they hope it will be superior to the comparable engine to be offered by General Electric, particularly as to fuel efficiency. International Aero Engines will have a life of 30 years. (Incidentally, it is also assumed that some other entity will be willing to build a plane to take this engine.)[2]

Thus we have the joint venture: a new entity created for the purpose of carrying on a distinct enterprise by two or more co-existing parents through their mutual contribution of assets or resources and subject to their joint control.[3]

This focused definition is useful because it immediately explains the decisions in a number of cases in which the defendants' reliance on joint venture arguments to justify their conduct fell on deaf judicial ears.[4] Those defendants actually were not engaged in joint venture activities, but in traditional cartel behavior — such as fixing prices or dividing markets — which they attempted to disguise as a joint venture.

In the best known of these cases, *Timken Roller Bearing Co. v. United States*,[5] an American, a British and a French manufacturer of antifriction roller bearings entered into a series of agreements, which they styled a "joint venture," to regulate their manufacture and sale of antifriction bearings and to provide for the use of the "Timken" trademark. In fact, these companies were allocating among themselves the world markets for antifriction bearings and fixing the prices on the products of each of them sold in the territories of the others. The Supreme Court rejected their appeal that "joint venture" nomenclature should save them.[6]

That conclusion was clearly correct. These roller bearing companies were not creating a new entity to carry on a distinct enterprise. They were not contributing any substantial assets or resources to their common undertaking. In short, they were not engaged in a true joint venture.

The historical and continuing significance in the American economy of the joint venture may be readily appreciated from the following brief summary of ways in which joint ventures have been, and are being, used. Major, costly undertakings have often been pursued through the joint venture vehicle. Historically, railroad development and oil and gas exploration, particularly in the Middle East, often took the joint venture form. More recently, the joint venture has been utilized for projects of similar magnitude such as oil or gas pipelines, and communications satellites, where two giants — AT&T and IBM — are now engaged in a joint venture.

Market creation or development also has often occurred through joint ventures. In recent years, this has included the use of so-called bid depositories in the construction trades and multiple listing services by real estate brokers.

Similarly, trade associations, a form of joint venture, have undertaken and continue to undertake numerous market development activities such as data collection and dissemination, and standards setting.

Finally, joint ventures continue often to be used in the exploitation of new products or markets. Today, the cable television industry is replete with joint ventures (which frequently are not financial successes) offering a variety of specialized general distribution services or channels, pay TV channels offering specialized programming such as movies or sports and limited duration pay-per-view ventures. The banking industry, too, is awash with joint ventures, particularly for the purpose of supplying credit card services and automatic teller facilities and services regionally and nationwide. Thus, there are now an estimated 175 to 200 networks of multi-bank automatic teller or cash machine systems, six of which are nationwide ventures.[7]

In short, it is fair to conclude that the joint venture has long played a significant part in the development of the American industrial and post-industrial society, and continues to make important contributions today.

Notwithstanding this influential role for joint ventures in the American economy, the complaint is regularly heard that the antitrust laws unduly inhibit the formation of joint ventures and, particularly, that this inhibiting effect may prevent the United States from realizing its full economic potential despite the native ingenuity of its people and its great resources. A recent analysis in *Legal Times* pulled no punches: "Congress is no doubt correct in believing that this uncertainty [on the legal status of joint ventures], coupled with the possibility of trebled damages and high litigation costs, has imposed a burden on the research efforts of U.S. firms."[8]

What is not often seen is evidence that the antitrust laws have actually been applied to enjoin or undo particular joint undertakings that hold the promise of providing some significant economic or social benefit. The dearth of examples of this sort is not surprising: in truth, antitrust standards have had only a limited impact on joint venture activities.

III. The Antitrust Standards

The antitrust standards applicable to joint ventures are not exotic. They look to three principal factors to determine the propriety of any given joint venture: structure or market power, objectives of the venture, and collateral agreements.[9]

A. Structure or Market Power

Investigation of structure asks: "What competitive relationships are affected by a particular joint venture, and how are they affected?" Are the parent entities direct horizontal competitors, producers (or consumers) of the same product or service in a discrete market? Are they potential or nascent horizontal competitors who might be expected to lock horns in the market place in the reasonably near future but for their affiliation through the joint venture? Are the participants vertically related, a supplier of some significant input in the production process, one to the other, or a purchaser of an output produced by another participant in the venture (or one of its competitors)?

These questions should also be asked about the competitive relationship between the parents and the joint venture itself. Will the venture compete in markets of any of the parents, or in markets which a parent logically might enter (but for the joint ventures)? Will it be a supplier of goods or services to one or more of its parents, or a purchaser from a parent?

Once the competitive relationships among the parent entities and their joint venture are recognized, the significance of these relationships must be evaluated by investigating the nature of the affected markets. Principally, as in merger analysis, this inquiry entails an assessment of the concentration levels in the pertinent markets, or what is commonly called "market shares," and how these levels are likely to be affected by the combination of the parents through their joint venture.

At least for prospective analysis, this inquiry reasonably assumes that the parents and the joint venture will avoid head-on competitive confrontations — such as attempting to sell the same of readily substitutable products to the same buyers.[10] An apparent contradiction to this assumption is presented by the joint venture between General Motors Corp. and Toyota Motor Corp. to produce jointly a new subcompact car (for marketing in the United States by General Motors Corp.), which recently was approved by the Federal Trade Commission. The parties apparently attempted to limit the scope of their venture in order to permit continued competition between them notwithstanding their common interest in the joint venture.[11]

The inquiry then becomes the extent to which on the horizontal level competition or potential competition is eliminated by the parents' affiliation through their joint venture, or the extent to which on the vertical level competitors are foreclosed from significant markets by the venture's presence, or both. Without reciting the traditional antitrust merger guidelines set out in terms of market share statistics,[12] or the current Administration's provocative reformulation of these guidelines utilizing the Herfindahl-Hirschman Index,[13] it is obvious that the competitive impact of an affiliation like a joint venture generally will increase as the number of alternatives — that is, independent competing firms — decreases. It may well be the number of strong auto manufacturers which justifies the GM-Toyota arrangements. Furthermore, the auto industry may well become a market characterized by joint ventures, for both research and development and for other purposes.[14]

The various Antitrust Division guidelines, as well as numerous judicial decisions, establish fairly clear standards of when a merger will be deemed to cause an excessive diminution in competition in the absence of other factors having an ameliorating or exacerbating effect. Generally speaking, however, market structure will not have the decisive impact on the legality of a joint venture that it typically has in the merger context. Rather, it is merely the starting point in the analysis. Primarily, this is because a joint venture, unlike a merger, does not ordinarily or necessarily *eliminate* any competitors, but, instead, creates a new, additional market participant.[15]

An extreme situation could test this general rule, where a joint venture whose parents include one or more dominant firms in a highly concentrated market — roughly, four or fewer major participants — is formed to carry on an activity formerly performed by the parents or which is closely related to the principal business activities of the parents. For example, should two direct competitors in a highly concentrated market, one of which is one of the largest firms in the industry, form a joint venture to act as their sales agent, disapproval would be likely.[16]

Note, however, that a joint venture between these firms to pursue some other, less sensitive goal — such as development of a *new* product or penetration of a market not presently served by the parents — would not necessarily be condemned as anticompetitive. On that basis, indeed, the Justice Department recently cleared the International Aero Engines plan to develop jointly a gas turbine jet engine.[17]

Only when the joint venture supplants the previously competing conduct of its parents in a highly concentrated market will the venture likely be condemned out of hand. And, in truth, such a joint venture would treat suspiciously close to being a cover for a merger or to fix prices.[18]

While this discussion has focused on market share analysis, other structural considerations also will often be significant, principally because of their impact on the reliability of the market share data. In particular, barriers to entry may significantly alter the antitrust conclusions.[19] Obviously, a joint sales agency by two of the four participants in an industry will be of substantially less concern if the industry is the production of, say, fly swatters rather than the production of complex chemicals such as DDT.

Similarly, the dynamics of the industry may temper the antitrust assessments. For example, a limited joint venture between participants in a declining industry may be the only way short of merger to permit their continued survival. That conclusion, no doubt, underlies the Newspaper Preservation Act[20] which exempts from the antitrust laws joint newspaper operating arrangements where one of the two venturers otherwise would not likely remain financially sound, in order to preserve two independent reportorial and editorial voices.

B. Objectives of the Joint Venture

The second principal factor in the antitrust calculus investigates the objectives of the joint venture. Leaving aside patently improper objectives such as price fixing or market division, the pertinent inquiries include the purpose, the scope and the duration of the joint venture.[21]

1. Purpose

Joint ventures exist to serve a wealth of purposes, including research, production, marketing, purchasing, advertising or promotion, exploitation of natural resources, data collection and dissemination, market creation, and standards setting. Each has differing antitrust implications. For example, a joint venture by tobacco growers to establish a tobacco auction house could have a positive effect on the competitive process, while their amalgamation to market their tobacco crops could be decidedly anticompetitive. (And here a sense of history is instructive: the legislative proposals which seek to pro tect an imperiled segment of the economy — high technology enterprises unable to withstand the onslaughts of foreign competition — may be seen to parallel an analogous fear in the 1920's — that application of then-existing antitrust laws threatened another fragile part of the American economy — the American farmer. The result then was the Capper-Volstead Act,[22] which exempted from the reach of the antitrust laws cooperative agricultural processing, handling and marketing activities.)

2. Scope

Analysis of the scope of a joint venture asks how much of the parents' businesses will the venture undertake. For example, is the enterprise simply a research venture, or will it also pursue promotion, marketing or other activities? And even within an activity such as research, a joint venture may have a limited or an expansive scope: single subject research, general basic research, practical applications of scientific or technical findings, translation of findings or applications into efficient productive processes, and so on. In short, the probable competitive impact of the participants' joint undertaking may well turn on the preciseness of its description.

3. Duration

Similarly, the intended duration of a joint venture may significantly affect the concerns of our antitrust guardians. Obviously, the shorter the period of time during which the venture will exist, the less one needs to worry about its anticompetitive potential. Recent examples, however, suggest that the duration of a joint venture is no longer a significant factor. The GM-Toyota deal is for 12 years.[23] The $1 billion jet engine venture was approved with a 30-year lifespan, because 30 years was assumed to be the commercial life span of successful jet engines.[24] What if the subject were water pipes? Or cathedrals?

All these analytical factors intertwine. An emphasis on only one aspect, say market structure, may lead to paradoxical results. For example, a joint venture having substantial market power, or whose parents have substantial market power, may be taboo, while a venture which includes nearly everyone in the industry, and thus may have absolute market power, may be permissible. The distinction depends on the objectives pursued by the joint venturers and the need for access to the venture in order to compete.

To play upon the facts of the best-known case of this sort, *Associated Press v. United States*,[25] suppose 20% of the nation's newspapers spread evenly across the country formed a joint venture, which they named the Associated Press, to pool their newsgathering efforts so that a paper in Albany would have access to the information about California politics collected by a paper in Sacramento, and vice versa, and so on. Presumbly, since 20% of the newspapers were capable of forming a functioning joint venture, other groups of papers could do the same, and no necessary anticompetitive results would flow from the formation of the first venture, the Associated Press, and limitations on participatory rights to its original group of founders.

Now, however, assume that the Associated Press were comprised of 70% of the nation's newspapers, or 20% of the papers having 70% of the assets, reporters or readers in the industry, and that this was the reasonable minimum level of participation necessary to permit the venture to function effectively and efficiently. Whereas, in the prior example, a rule limiting participation in the venture may have been procompetitive by preventing the organization from growing to a size that would raise antitrust problems, now the same rule has an anticompetitive effect: it precludes outsiders from enjoying the benefits of the venture in a situation in which they are realistically unable to duplicate the venture on their own. Under these circumstances, the Associated Press must be converted into a quasi-utility joint venture: available on relatively equal terms to everyone in the industry.[26]

C. Collateral Restraints

Taken together, structure and objectives tell the whole story of the antitrust laws and joint ventures proper. However, joint venturers have had a demonstrable historical predilection to saddle their common enterprise with a variety of collateral agreements or restraints. It is these collateral attachments, or in the slightly erotic phraseology of the Carter administration — these "facilitating devices" — that are the antitrust rocks upon which many joint ventures founder.[27]

For example, Getty Oil Company and four major motion picture producer-distributors recently formed a joint venture, called Premiere, to package and offer movies for local cable television systems, primarily in competition with Home Box Office. Whether or not the participation of these four producer-distributors — who controlled one-third of all films shown on pay television and received about 50% of the total pay television film rentals — would have, alone, condemned the venture (and the Justice Department's recent actions on the Showtime-The Movie Channel joint venture merger suggest it would have[28]), the participants included a so-called "nine-month window" to their joint venture agreement. Under this "nine-month window," the parents made their films available only to their joint venture during the nine months following a film's release. Given the realities of the film industry, nine months is a lifetime for a new film. In part because of this nine-month exclusive marketing agreement, the court granted the Justice Department's request to enjoin the joint venture from commencing operations.[29]

That the parents chose to abandon their venture, rather than to excise its offensive provisions and concentrate on competing with HBO, suggests that they were more interested in accumulating substantial market power, as the nine-month window surely would have accomplished, than in introducting a new entity to compete on the merits for pay TV customers.

This eagerness to include overreaching ancillary restraints in certain joint ventures has led, not surprisingly, to their condemnation.[30] And it is this condemnation of attempts to limit competition or to increase market power through collateral agreements to a joint venture that has given the antitrust laws the reputation of preventing useful cooperative activity. The reputation is undeserved.

The Justice Department, in its Guide Concerning Research Joint Ventures, states that collateral agreements are permissible to the extent they "(1) are reasonably ancillary to a lawful main purpose of the [joint venture], (2) have a scope or duration no greater than necessary to achieve that purpose, and (3) are not part of an overall pattern of restrictive agreements that has unwarranted anticompetitive effects."[32] Whatever those generalities may mean in practical terms, a collateral restriction that legitimately promotes the primary mission of an otherwise proper joint venture is unlikely to be found to violate antitrust strictures.[32] For example, the parents' cross-licensing of pertinent patents and exchange of relevant technical information is undoubtedly permissible in the context of their research joint venture.[33]

IV. Antitrust Division and FTC Actions

The preceding discussion has already touched upon a few of the Justice Department's more significant actions over the years involving joint ventures, such as *Timken Roller Bearing Co.*[34] and *Associated Press.*[35] To these must be added the Department's challenge of a joint venture between Pennsalt Chemicals Corporation and Olin Mathieson Chemical Corporation, called Penn-Olin Chemical Corporation to produce and sell sodium chlorate in the southeastern United States.[36] Pennsalt was a manufacturer of chemicals throughout the United States. It produced sodium chlorate at its plant in Portland, Oregon. Olin Mathieson also manufactured chemicals, but was not a producer of sodium chlorate. It was, however, a purchaser of sodium chlorate and acted as Pennsalt's sales agent in the Southeast.

Pennsalt and Olin Mathieson formed Penn-Olin as an equally owned joint venture to build a sodium chlorate plant at Calvert City, Kentucky and to produce and sell the resulting sodium chlorate. Pennsalt operated Penn-Olin's plant, and Olin Mathieson handled the sales of the sodium chlorate.

The Justice Department argued that the joint venture was anticompetitive because Pennsalt and Olin Mathieson *could* have competed with each other since each had sufficient individual financial ability and technical competence.[37] The district court rejected this contention, stating that the proper inquiry was not whether Pennsalt and Olin Mathieson *could* have competed with each other, but whether they *would* have done so absent the joint venture. The court concluded that it was not reasonably probable that *both* Pennsalt and Olin Mathieson would have built sodium chlorate plants in the southeast if Penn-Olin had not been created and, thus, that the joint venture did not result in any diminution of actual or probable competition.[38]

The Justice Department appealed. The Supreme Court accepted neither the government's nor the district court's position. Instead, it declared the appropriate minimum standard to be whether there was a "reasonable probability that either one of the corporations would have entered the market by building a plant, while the other would have remained a significant potential competitor."[39] This standard at least required a showing that the joint venture caused some reduction in competition or potential competition before condemning it under the antitrust laws.

The *Penn-Oil* decision was typical of the prevalent attitudes at the Justice Department and on the Supreme Court during the Warren years. It represents one of the major underlying causes for concern that the antitrust laws may excessively impede joint venture formations. Ironically, on remand the district court found that neither Pennsalt nor Olin Mathieson was an independent potential entrant into the market and upheld the joint venture.[40] (The Supreme Court affirmed this decision *per curiam* by an equally divided Court.[41])

How have the Antitrust Division of the Justice Department and the Federal Trade Commission treated joint ventures over the last few years? Quite favorably.

Official actions and pronouncements *critical* of specific joint ventures generally have focused on ventures between competitors in highly concentrated markets and on the inclusion of collateral restraints. In 1979 the Federal Trade Commission successfully opposed a joint venture between Brunswick Corporation and Yamaha Motor Company, two leading producers of marine outboard motors, to manufacture and sell in the United States a line of outboard motors.[42] Its analysis followed the course outlined in the preceding discussion. Brunswick already was a major force in the highly concentrated U.S. market, with the top four firms accounting for 94.9% of units sold and 98.6% of dollar volume, and the top two firms, one of which was Brunswick, holding 72.9% of units sold and 85% of dollar volume. Yamaha manufactured and sold outboard motors everywhere except in the United States and had substantial marketing experience and brand name recognition in the U.S. from its substantial motorcycle sales. In addition, Yamaha had the financial resources and technical skills necessary for entry, and had twice previously made attempts to enter the U.S. market unilaterally. Yamaha was to contribute existing production facilities to the joint venture, while a Brunswick subsidiary would sell the outboard motors in the United States under its own label.

On the basis of these facts, the FTC concluded that Yamaha was a leading potential competitor[43] and that the elimination of its potential presence as a result of the joint venture would have greater anticompetitive effects than any procompetitive benefits to be derived from the venture. It is hard to quarrel with the FTC's conclusion. The concentrated market structure in outboard motors, and Yamaha's transfer of its production facilities to the venture, probably assured that Yamaha thereafter would never enter the U.S. market alone.[44]

Moreover, as so often is the case, Brunswick and Yamaha were not content merely to establish their joint venture, but used this undertaking to agree to a number of competition-limiting collateral restrictions. Yamaha was to be prohibited from producing or purchasing for resale outboard motors not the product of the joint venture. Brunswick and Yamaha agreed not to pursue each other's dealers in non-exclusive markets throughout the world, such as Europe and South America. And, in connection with a probably reasonably ancillary technical assistance agreement providing for the exchange of reciprocal licenses to use technical information, Brunswick agreed not to produce any product that would be competitive with *any* Yamaha product, except for snowmobiles. Not surprisingly, these collateral restrictions also failed to pass antitrust muster.

Similarly, the Justice Department has successfully challenged exclusionary ancillary restrictions on participation in real estate multi-list ventures.[45] These cooperative operations permit realtors to gain mutual access to the listings of other realtors in the area, thereby permitting each realtor to offer substantially improved and broader market information to both buyers and sellers, to the benefit of these consumers. Much like *Associated Press*,[46] access to the multi-listing service quickly became a virtual necessity to compete in the real estate broker business, and establishment of a competing multi-list operation would have been ineffective and not practically feasible. In fact, in the leading case, *United States v. Realty Multi-List, Inc.*,[47] the vast majority of realtors in the area were members and the service handled most of the properties offered for sale. Again, it is not surprising that a number of membership restrictions (such as a requirement that a broker have an office open during all customary business hours) were struck down.

As already mentioned, the Justice Department successfully opposed the Premiere pay cable TV joint venture among Getty Oil Company and four major motion picture producer-distributors because of the venturers' inclusion of an exclusively collateral agreement that was likely to have a significant anticompetitive impact on the ability of other pay cable television firms to obtain desirable movies.[48]

The Justice Department also repeatedly opposed the proposed merger of The Movie Channel and Showtime into a single joint venture so long as two major motion picture distributors — Paramount Pictures Corp. and Universal Studios, Inc. — were participants. Once Paramount and Universal Studios withdrew, the Antitrust Division cleared the joint venture among Viacom International, Inc., American Express and Warner Communications, Inc.[49]

In 1982, the Justice Department convinced the Interior Department's Bureau of Land Management that a joint bid by three public electric utilities to lease coal lands on the Camp Swift Military Reservation in Bastrop County, Texas would be anticompetitive.[50] The Justice Department had argued that the joint bidding would undermine the competitive bidding process and preclude a fair market price for the leases.[51]

Finally, last summer the Justice Department declined to furnish antitrust clearance to a proposal of the National Small Shipments Traffic Conference for the formation of a "shippers' council" that would collectively negotiate freight rates on less-than-truckload shipments with motor and rail carriers.[52] The Department noted that shippers' councils were not inherently anticompetitive and would be challenged only if the council was likely to result in the exercise of undue market power over freight rates in a relevant market. As a guideline, the Department explained that such monopsony power was *not* likely to exist if (1) the members in the council do not account for significantly more than 15% of the pertinent shipments, (2) no restrictions are placed on the volume members can ship, and (3) members remain free to negotiate individually with carriers.

The Justice Department refused to state its enforcement intentions not because the proposed shippers' council breached these guidelines — it didn't — but because insufficient information was provided to assess whether council members were direct competitors accounting for a large percentage of sales in particular markets and whether the freight rates were an important component of the price of the shipped products in those situations.

In summary, the FTC and the Justice Department can be expected to challenge joint ventures when they include significant anticompetitive collateral agreements, as in the *Yamaha-Brunswick* venture and in the real estate multi-listing case, or when the joint venture is an arrangement among principal members of a concentrated industry and will either directly reduce competition or potential competition, as in *Yamaha-Brunswick*, or will significantly foreclose others from access to an important product, as in the pay cable television ventures. This approach hardly can be considered either particularly inhibitive of beneficial joint venture formation, or so vague as to cause any substantial uncertainty.

In contrast to this sampling of government challenges to particular joint ventures stands a voluminous collection of Justice Department and FTC actions and statements affording a broad and permissive scope to joint venture undertakings. Approval has been given to numerous joint ventures, including joint approaches to negotiation, research and development, dissemination of data on costs and revenues and pricing, and actual manufacture and sale.

In the early 1970's, the Justice Department cleared joint oil company bargaining and other cooperation to counteract the OPEC cartel.[53] The then principal Antitrust Division officers made it clear that the concerted use of such countervailing force would not be considered violative of the antitrust laws.[54]

Such joint ventures, formed for conducting joint negotiations, have become more common. Recall the guidelines offered to the National Small Shipments Traffic Conference in connection with its disapproved proposal to form a shippers' council to collectively negotiate freight rates with motor and rail carriers on less-than-truckload shipments.[55]

In contrast to that proposal, the Justice Department in March 1983 approved a plan by Gross Common Carriers, a Wisconsin intrastate motor carrier, to negotiate a variety of joint-line arrangements, including joint-line rates, with small carriers serving areas not serviced by Gross Common Carriers. This would permit Gross to offer shipping services to all locations in Wisconsin with point-to-point rates.[56] The plan really constituted a series of joint ventures among participants in the same industry, who undoubtedly compete in some places and not in others, to offer combined services in those areas where they do not directly compete and to negotiate the rates to be charged for those services. The Department particularly noted that the larger number of authorized carriers in Wisconsin, and the ease with which new entrants can obtain operating authority due to the state's deregulation of the industry, made it unlikely that the joint-line arrangement will facilitate collusive behavior or otherwise cause a significant reduction in competition.

In contrast to the Justice Department's opposition to the joint bid by three public utilities for coal leases at Camp Swift, the Department has approved a number of cooperative purchasing programs over the past year. These include the participation by eight gasoline service station dealer associations, with memberships principally in separate geographic areas of New York State, in a cooperative purchasing program established by Mechanics Choice Automotive Products, Inc. Under the program, Mechanics Choice will purchase batteries, motor oil and other automotive products for resale to the participating organizations (who, in turn, will resell the products to service station dealers for ultimate sale to the public).[57]

A similar group purchasing proposal by the Ohio Hospital Purchasing Consortium, composed of eight Ohio hospital purchasing groups representing 160 of the 204 non-profit hospitals in the state, was also approved.[58]

And a proposal by the Greater Detroit Theatre Operators Purchasing Corp., representing up to 36 motion picture exhibitors in the Detroit area, to make volume purchases of theatre goods and services, other than film rentals, such as advertising, promotional and merchandising services, paper goods, and theatre equipment was cleared by the Department.[59]

The Justice Department and the FTC have also approved in the past year a number of ventures to collect and disseminate (in aggregated form) cost information and similar data for firms in the particular industry. These have included a proposal by the National Tank Truck Carriers, Inc. ("NTTC") to engage Ernest & Whinney to prepare a "Guide to Bulk Motor Carrier Costing" and a "Bulk Carrier Cost Index."[60] The Guide will set out procedures and methodology by which NTTC members can compute their costs and allocate them to individual shipments. And the Index will collect and aggregate cost information from NTTC members, which will permit the carriers to compare their individual costs and evaluate their operating results against the standards reflected in the Index.

The Department has also approved plans by the National Association of Broadcasters to publish aggregated data on the revenues and expenses of commercial television stations.[61]

Similarly, the FTC has given its go-ahead to a natural gas company's program to collect natural gas price data and to use this information in redetermining contract prices for natural gas sales.[62]

Moving to actual production joint ventures, New York's Metropolitan Taxicab Board of Trade, an association of the city's fleet taxicab owners, has received Justice Department clearance for a plan to offer data processing services to New York City taxicab operators.[63] These services would include salary and benefit administration and periodic management reports on costs, revenues and other similar information. The services will be made available to all taxi owners at the same cost whether or not they are members of the Metropolitan Taxicab Board of Trade. Of particular note, the Department declined to state any enforcement intention for the Board of Trade's additional plan to generate aggregate industry data, apparently because the data would be in a form that would permit company identification.

The Justice Department also cleared a travel agent cooperative formed by ASTA Marketing Services, Inc. to provide informational and promotional services to suppliers of travel services.[64] The Department noted that "travel agent cooperatives, by integrating functions that would otherwise be performed by agents individually, can achieve important marketing efficiencies" and that the Department would not challenge the formation of a joint venture unless it "was likely to facilitate the exercise of market power in any geographical market."[65]

A clear contrast to the FTC's *Brunswick-Yamaha* decision in 1979 is provided by its recent approval of the General Motors-Toyota joint venture[66] and by the Justice Department's approval of two separate engine production joint ventures. Last February, the Department cleared a proposed joint venture between Briggs & Stratton Corp. and Lombardini, F.I.M. S.P.A., an Italian corporation, for the manufacturer of small diesel engines in the United States.[67] The companies both manufacture small diesel engines in Europe and import them to the United States. Their combined imports in 1981 represented less than 3% of total United States sales, a figure exceeded by at least eight other companies in the U.S. Thus, no substantial increase in concentration would result from the combination of these two firms' productive efforts in a joint venture.

Finally, there is the Justice Department's antitrust clearance to the International Aero Engines plan.[68]

What about research and development joint ventures, specifically? The Justice Department in fact has cleared numerous research ventures. Most notably, in December 1982 the Department approved a venture proposed by Control Data Corp., to be called Microelectronics and Computer Technology Corp. ("MCTC"), which would sponsor and oversee research projects in the computer and microelectronics industries.[69] At least 13 computer companies have joined the venture, and, as of July 1983, MCTC is pursuing research in four basic areas: semiconductor packaging and interconnect technology, software engineering, computer-aided design and manufacturing, and computer architecture.[70] In short, MCTC is essentially an industry-wide research joint venture in one of the areas said by critics of antitrust enforcement to be critical to America's ability to compete against foreign manufacturers.[71]

In September 1983, the Justice Department, the FTC and the Small Business Administration cleared a joint venture among eight firms in New England, called the Small Business Technology Group ("SBTG"), to bid on high technology research and development contracts, particularly those offered by the Defense Department.[72] SBTG and its participants received antitrust immunity under section 9 of the Small Business Act,[73] which authorizes the SBA Administrator to except from the scope of the antitrust laws, after consultation with the Justice Department and the FTC and approval by the Attorney General, joint programs for research and development which the Administrator finds "will maintain and strengthen the free enterprise system and the economy of the nation." Significantly, the participants in this joint venture did not restrict their several rights to bid independently on any R&D contracts, and thus avoided a collateral agreements problem.

Looking at all the cases, the joint venture vehicle is available, consistently with the antitrust laws, to pursue a wide range of activities, from pure research to market surveying to cooperative buying and, finally, to combined manufacture and sale. If structured with an eye toward the concerns of antitrust enforcers — principally the avoidance of unnecessary ancillary restrictions — the joint venturers and their counsel may comfortably undertake concerted activities that promote innovation, efficiency, rational business conduct, and profits. As all of these examples illuminate, antitrust uncertainty has not and need not deter the formation of useful joint ventures.

Even in those cases where the government successfully challenged a particular venture, the antitrust laws cannot be said to have prevented the attainment of a beneficial goal that was not otherwise reachable. Thus, the Movie Channel-Showtime combination was permitted to proceed once the troubling participation by major motion picture distributors was eliminated. And production and marketing consortiums have been approved when, in contrast to the *Brunswick-Yamaha* proposal, they were not interlaced with collateral restrictive agreements.

Nor can the antitrust laws honestly be said to introduce unacceptably severe uncertainty risks to joint venture planning and formation. The Justice Department has issued Guides, detailing the standards it follows and containing numerous concrete examples applying those standards to realistic sets of facts.[74] Indeed, the commercial jet engine development and production project described in the preceding discussion closely tracks a specific hypothetical case in the Department's Antitrust Guide Concerning Research Joint Ventures.[75] And a review and clearance procedure is available to venturers that affords a ready mechanism for ascertaining the Justice Department's and the FTC's attitude toward the legality of particular undertakings. While Administrations change, and, thus, the Government's antitrust philosophy and policies are dynamic and not static, there is no evidence that subsequent Administrations do not respect the statements of enforcement intentions of their predecessors which private parties have obtained and relied upon.

In short, antitrust enforcement in the joint venture realm is both reasonably predictable and attuned to commercial realities. No remarkable prescience is required to ascertain the permissibility of particular undertakings. And there is little basis to fear that beneficial ventures will be precluded from pursuing important goals by an irrational or uninformed application of antitrust principles. Certainly, the present research consortium of 13 significant computer companies demonstrates the compatibility of antitrust to economic advancement through joint activities.

V. Current Legislative Proposals

That brings us, finally, to the current legislative proposals to ameliorate the impact of the antitrust laws on R&D joint ventures. At least five bills[76] are presently before one or the other of the Houses of Congress, which propose to modify the antitrust rules applicable to research joint conduct. Legislation is said to be necessary in order that American industry may better compete in our brave new world of internationally populated markets — compete against the threat supposedly presented by government-assisted foreign firms and foreign research, development and marketing consortiums which do not suffer the impediments of antitrust proscriptions. The common thread to all of these proposals is the thesis that quaint antitrust notions of a free and private economy, made up of independent actors, have become incompatible with the dominant economic and competitive realities of centralized planning and operations. The picture is presented of earnest, but outmatched, American industrial Davids succumbing to the foreign consortium Goliaths.

Most prominent among these legislative proposals is the Justice Department's offering, entitled the National Productivity and Innovation Act of 1983.[77] That bill proposes to temper the antitrust constraints that supposedly inhibit R&D joint venture formation in two ways. First, the per se rule of illegality is affirmatively declared to be inapplicable to joint research and development programs.[78] Second, the bill would limit a plaintiff injured by anticompetitive conduct of a research and development program to recovering its actual damages, rather than the standard treble damages, so long as the Justice Department and the ETC have been notified in advance of the details of the program.[79]

This notification procedure — and the bill incorporates mere notification, not antitrust clearance[80] — requires a person participating in a joint research and development program to specify the identify of the parties participating in the program, the nature, scope and duration of the program, and any agreements or understandings ancillary to the program.[81] The Commission is to publish in the Federal Register a notice of any notification received containing a general description of the participants, the program, and its objectives so that the public and competitors may be apprised of the program's existence and intended activities.[82] The bill also includes procedures for requesting confidential treatment of information or materials submitted with the notification and for withdrawing a notification prior to the publication of notice in the Federal Register.[83] Of course, the protection of the single damages limitation would be lost if a notification is withdrawn.

Finally, the bill defines a "joint research and development program" as jointly conducted "theoretical analysis, exploration, or experimentation, or . . . the extension of investigative findings and theories of a scientific or technical nature into practical application, including the experimental production and testing of models, devices, equipment, materials, and processes. . . ."[84]

Other bills resurrect other gimmicks. For example, the bill sponsored by Representative Fish of New York[85] would authorize judges to grant attorneys' fees to harassed, but prevailing, defendants in suits challenging R&D joint ventures.

Is legislation of this sort necessary, or likely to contribute significantly to remedying the perceived imbalance between domestic and foreign innovation, productivity and competitiveness? One can liken it to the discovery by medical researchers of a remedy for which there is no disease.

First, as the analysis herein suggests, there simply is no evidence that the *antitrust* laws — rather than, say, our tax laws[86] — have inhibited American research and development efforts. As the Justice Department, itself, has stated: "A pure research joint venture without ancillary restraints has *never* been challenged by the Antitrust Division. Even cases challenging restrictive conditions in such ventures have been rare."[87] One is hard pressed to understand why we need to pass special legislation to address a problem which there is no reasonable basis to believe exists.

But, proponents argue, private parties are not constrained by the good sense of the Justice Department and the FTC and may independently enforce the antitrust laws against procompetitive R&D joint ventures. There is, of course, a fatal non sequitur in this contention: such procompetitive joint conduct does not violate the antitrust laws. The federal courts have dealt with antitrust claims and the intricacies of economic analysis for nearly 90 years and, on balance, have displayed an ability to appreciate business realities and to apply antitrust standards with sensitivity to those realities. Diligent research has not found a single instance of a successful private antitrust challenge to a pure research and development joint venture.[89] Second, if R&D really suffers under the burdens of antitrust compliance, there is no reason to conclude that joint ventures are necessarily the most efficient vehicles for re-establishing American innovative and technological supremacy. Mergers, contracts, and other methods for pooling knowledge, knowhow and effort may provide equally efficacious, or more efficacious, means of attaining the purported goal of improving domestic industrial productivity and competitiveness, particularly since R&D cannot be viewed in isolation from the other elements of industrial activity. The Administration's proposal seems to favor the joint venture over other forms of affiliation without strong empirical evidence that joint ventures are the best way to get the R&D job done.

Third, there is little evidence that enterprise size is positively related to R&D achievements. The proposed legislation assumes that bigger is better in the research and development arena. No substantial studies, however, demonstrate that large-scale economies beyond quite low thresholds are a factor in innovation. Thus, these legislative reforms may be encouraging conduct that is unrelated, or only poorly related, to solving the perceived problem.

Finally, it is difficult to accept the assumption that any shortcomings in American productivity and competitiveness are the result of deficient research and development efforts. The industries being battered by foreign competition — such as steel and automobiles — are not losing out because of an inability to pursue R&D projects. Their problems seem to be due to a combination of high labor costs and poor managerial judgment, factors that are addressed by the proposed legislation only indirectly in the first instance, and not at all in the second.

Certainly, other of our high-technology industries, such as electronics and genetic manipulation, have not yet displayed an inability to compete with the innovativeness of foreign concerns. Yet the Administration's proposal skews corporate decision-making in favor of research rather than other equally significant aspects of economic activity such as production, marketing and service. Substantially better evidence that inadequate R&D is at the heart of America's supposed industrial woes ought to be presented before we elevate joint research and development programs to preferred status in our antitrust cathedral.

WALTER BARTHOLD: Taylor, you very generously accepted a cruel assignment — winding up a program of the caliber we have been fortunate enough to present today. Good for us for selecting someone who is up to the job. And we all thank you for the extensive, exhaustive thought and work that went into the preparation of your superb talk today.

Ladies and gentlemen, that concludes the daytime program.

FOOTNOTES

+ LeBoeuf, Lamb, Leiby & MacRae, New York City. The author gratefully acknowledges the collaboration in the writing of this article of Frederick R. Dettmer of the same firm.
1. *See* Brodley, *Joint Ventures and Antitrust Policy*, 95 Harv. L. Rev. 1523, 1524-25 (1982)
2. *See Antitrust Division Clears Joint Venture to Build Advanced Technology Jet Engines*, 45 Antitrust & Trade Reg. Rep. (BNA) 726 (Nov. 3, 1983).
3. For other similar definitions of joint ventures, *see, e.g.*, P. Areeda, Antitrust Analysis ¶360 (3d ed. 1981); Brodley, *supra* note 1 at 1526.
4. *E.g.*, *Timken Roller Bearing Co. v. United States*, 341 U.S. 593 (1951); *North Am. Soccer League v. National Football League*, 670 F.2d 1249, 1256-58 (2d Cir.), *cert. denied*, 103 S. Ct. 499 (1982); United States v. American Smelting and Ref. Co., 182 F. Supp. 834 (S.D.N.Y. 1960); United States v. National Lead Co., 63 F. Supp. 513 (S.D.N.Y. 1945), affd, 332 U.S. 319 (1947).
5. 341 U.S. 593 (1951).
6. "Nor do we find any support in reason or authority for the proposition that agreements between legally separate persons and companies to suppress competition among themselves and others can be justified by labeling the project a 'joint venture.' Perhaps every agreement and combination to restrain trade could be so labeled." *Id.* at 598.
7. Hertzberg, *Banks Linking Cash Machines Across the U.S.*, Wall St. J., Nov. 16, 1983, at 33, col. 3.
8. Brunsvold and Moy, *R&D Joint Venture Bills Address Antitrust Concerns*, Legal Times, Nov. 28, 1983, at 11, col. 1.
9. *See, e.g.*, Antitrust Div., U.S. Dep't of Justice, Antitrust Guide Concerning Research Joint Ventures (1980) [hereinafter cited as Joint Venture Guidelines], Brodley, *supra* note 1.
10. *See, e.g.*, 3 P. Areeda & D. Turner, Antitrust Law ¶703c (1978).
11. The FTC's proposed consent order is published at 48 Fed. Reg. 57,246 (1983) and is also reproduced in full at 46 Antitrust & Trade Reg. Rep. (BNA) 42 Dec. 28, 1983. A Commissioner's Statement further explaining the FTC's decision is published at 48 Fed. Reg. 57.314 (1983). *See also* Moore, *FTC Likes 'Minimalist' GM-Toyota Joint Venture*, Legal Times, Jan. 16, 1984, at 2, col. 1.
12. United States Dep't of Justice Merger Guidelines - 1968, reprinted in 2 Trade Reg. Rep. (CCH) ¶4510.
13. United States Dep't of Justice Merger Guidelines - 1982, reprinted at 2 Trade Reg. Rep. (CCH) ¶¶4501-4505 [herein after cited as 1982 Merger Guidelines]; *see generally* 4 Areeda & Turner, *supra* note 10, ¶913 (1980).
14. "In the past five years alone, auto makers have started more than 30 new joint projects, forming links that are rapidly changing the structure of the world auto industry." Koten and Ingrassia, *British Car Maker's Tie To Honda Shows Why Auto Linkups Increase*, Wall St. J., Dec. 12, 1983, at 1, col. 6.
15. *See, e.g.*, Unitged States v. Penn-Olin Chem. Co., 378 U.S. 158, 170 (1964).
16. *Cf.* United States v. American Smelting and Ref., Co., 182 F. Supp. 834 (S.D.N.Y. 1960).
17. *See supra* note 2 and accompanying text.
18. *E.g.*, Timken Roller Bearing Co. v. United States, 341 U.S. 593 (1951); Lee Line Steamers, Inc. v. Memphis, Helena & Rosedale Packet Co. 277 F.5 (6th Cir. 1922); United States v. American Smelting and Ref. Co., 182 F. Supp. 834 (S.D.N.Y. 1960).
19. *See* 1982 Merger Guidelines, *supra* note 13, at §§III(B), IV(A)(3)(b), IV(B)(1), *reprinted in* 2 Trade Reg. Rep. (CCH) ¶¶4503.20, 4504.103(b), 4504.201; Joint Venture Guidelines, *supra* note 9 at §1(a).
20. 15 U.S.C. §§1801-04 (1970).
21. *See* Joint Venture Guidelines, *supra* note 9, at §1(A).
22. 7 U.S.C. §§291-92 (1976).
23. *See supra* note 11 and accompanying text.
24. *See supra* note 2 and accompanying text.
25. 326 U.S. 1 (1945).
26. *See* United States v. Terminal R.R. Ass'n, 224 U.S. 383 (1912); Gamco, Inc.,v. Providence Fruit & Produce Bldg., Inc., 194 F.2d 484 (1st Cir.), *cert. denied*, 344 U.S. 817 (1952); Joint Venture Guidelines, *supra* note 9 at §l(c); *see also L. Sullivan, Handbook of the Law of Antitrust* §48, §105, at 300 (1977); Brodley, *supra* note 1, at 1532-34, 1551-52 (1982).
27. *See* United States v. Topco Assocs., 405 U.S. 596 (1972); United States v. Sealy, Inc., 388

U.S. 350 (1967); Yamaha Motor Co. v. FTC, 657 F.2d 971 (8th Cir. 1981), *cert. denied*, 456 U.S. 915 (1982); United States v. Realty Multi-List, Inc., 629 F.2d 1351 (5th Cir. 1980); Engine Specialities, Inc. v. Bombardier Ltd., 605 F.2d 1 (1st Cir. 1979), *cert. denied*, 446 U.S. 983 (1980) & 449 U.S. 890 (1980); United States v. Columbia Pictures Indus., 507 F. Supp. 412 (S.D.N.Y. 1980), *aff'd* mem. No. 81-6003 (2d Cir. Apr. 7, 1981); Joint Venture Guidelines, *supra* note 9, at §1(B); *see also* Brodley, *supra* note 1, at 1543-44.

28. The Justice Department opposed a proposed merger of The Movie Channel and Showtime so long as it included participation by two major motion picture distributors.*See infra* note 49 and accompanying text.
29. United States v. Columbia Pictures Indus., 507 F. Supp. 412 (S.D.N.Y. 1980), *aff'd mem.*, No. 81-6003 (2d Cir. Apr. 7, 1981).
30. *See* cases cited *supra* note 27.
31. Joint Venture Guidelines, *supra* note 9, at §I(B) (footnotes omitted).
32. *See generally*, United States v. Addyston Pipe & Steel Co. 85 F. 271, 282 (6th Cir. 1898), *aff'd*. 175 U.S. 211 (1899); L. Sullivan, *supra* note 26, §64 at 171, §89 at 253-56; *see also* United States v. Realty Multi-List, Inc., 629 F.2d 1351 (5th Cir. 1980) United States v. Columbia Pictures Indus., 507 F. Supp. 412, 428 (S.D.N.Y. 1980), *aff'd mem.* No. 81-6003 (2d Cir. Apr. 7, 1981).
33. *See* Joint Venture Guidelines, *supra* note 9, at §I(B)(2).
34. Timken Roller Bearing Co. v. United States, 341 U.S. 593 (1951). *See supra* text accompanying notes 5-6.
35. Associated Press v. United States, 326 U.S. 1 (1945). *See supra* text accompanying notes 25-26.
36. *See* United States v. Penn-Olin Chem. Co., 378 U.S. 158 (1964).
37. The Justice Department's position in Penn-Olin stands in stark contrast to the FTC's recent approval of a joint venture between the world's first and third largest auto manufacturers, neither of which lacks financial ability or technical knowhow. *See supra* text accompanying note 11.
38. United States v. Penn-Olin Chem. Co., 217 F. Supp. 110, 130 (D. Del. 1963), *rev'd*, 378 U.S. 158 (1964).
39. United States v. Penn-Olin Chem. Co., 378 U.S. 158, 175-76 (1964).
40. United States v. Penn-Olin Chem. Co., 246 F. Supp. 917 (D. Del. 1965), *aff'd per curiam by an equally divided Court*, 389 U.S. 308 (1967).
41. United States v. Penn-Olin Chem. Co., 389 U.S. 308 (1967).
42. Brunswick Co., 94 F.T.C. 1174 (1979), *aff'd and modified sub nom.* Yamaha Motor Co. v. FTC, 657 F.2d 971 (8th Cir. 1981), *cert. denied*, 456 U.S. 915 (1982).
43. Ironically, on November 14, 1983, Outboard Marine Corp. filed suit against Yamaha Motor Co. to prevent Yamaha from importing outboard motors into the United States.
44. The joint venture between General Motors Corp. and Toyota Motor Corp. also entailed the transfer of a production facility to the joint venture (by General Motors). In contrast to the Brunswick-Yamaha venture, however, General Motors transferred only a single facility and one that had been previously closed down. The transfer of this single facility could hardly be considered to reduce the ability of either General Motors or Toyota to produce and market automobiles in the United States, particularly in light of the parties' efforts to limit the scope of their venture, which may permit continued competition between them.*See supra* text accompanying note 11.
45. *E.g.*, United States v. Realty Multi-List, Inc., 629 F.2d 1351 (5th Cir. 1980); United States v. First Multiple Listing Serv., Inc., 5 Trade Reg. Rep (CCH) ¶50,836 (N.D. Ga. Nov. 16, 1983 (proposed consent decree).
46. Associated Press v. United States, 326 U.S. 1 (1945).
47. 629 F.2d 1351 (5th Cir. 1980).
48. United States v. Columbia Pictures Indus., 507 F. Supp. 412 (S.D.N.Y. 1980), *aff'd mem.*, No. 81-6003 (2d Cir. Apr. 7, 1981). *See supra* text accompanying notes 28-29.
49. *See Antitrust Division Finally Clears Revamped Showtime/Movie Channel Venture*, 45 Antitrust & Trade Reg. Rep. (BNA) 275 (Aug. 18, 1983); *Pay Television Programming Merger*, 610 Trade Reg. Rep. (CCH) 3 (Aug. 22, 1983).
50. *See Interior Dep't Agrees With Justice, Cancels Lease Bids For South Texas Lignite*, 43 Antitrust & Trade Reg. Rep. (BNA) 403 (Sept. 2, 1982).
51. *See Justice Opposes Joint Bidding in Lease Offering for Texas Lignite*, 41 Antitrust & Trade Reg. Rep. (BNA) No. 1040, at A-17 (Nov. 19, 1981).

52. *See Shippers' Councils*, 606 Trade Reg. Rep. (CCH) 7 (July 27, 1983).
53. *See* Davidow, *Antitrust, Foreign Policy, and International Buying Cooperation*, 84 Yale L.J. 268, 278-79 (1974).
54. Thus, then Deputy Assistant Attorney General for Antitrust Donald I. Baker explained: "In fact, the Justice Department has authorized — and the Sherman Act permits — necessary cooperation among American firms to deal with a foreign government buying or selling cartel, provided that cooperation does not spill over into the domestic market." Address by Donald I. Baker at UCLA Merchantilism and Monopoly — The Alternative To A Competitive America, at 16-17, Nov. 16, 1973, *quoted in* Davidow, *supra* note 53, at 278.
55. *See supra* text accompanying note 50.
56. *See Justice Has No Antitrust Objections to Joint-Line Shipping Arrangement*, 44 Antitrust & Trade Reg. Rep. (BNA) 699 (March 31, 1983); *Intrastate Trucking*, 590 Trade Reg. Rep. (CCH) 7 (Apr. 4, 1983).
57. *See Justice Does Not Object to Co-op Purchasing by Auto Service Dealers*, 44 Antitrust & Trade Reg. Rep. (BNA) 1045 (May 26, 1983); *Cooperative Purchasing Program*, 597 Trade Reg. Rep. (CCH) 13 (May 24, 1983).
58. *See Antitrust Division Won't Attack Hospital Group Purchasing Program*, 42 Antitrust & Trade Reg. Rep. (BNA) 1321 (June 24, 1982).
59. *See Justice Clears Buying Cooperative of Movie Theatres*, 44 Antitrust & Trade Reg. Rep. (BNA) 1213 (June 23, 1983); *Cooperative Purchasing Program*, 601 Trade Reg. Rep. (CCH) 5 (June 21, 1983).
60. *See Cost Information Sharing*, 582 Trade Reg. Rep. (CCH) 7 (Feb. 14, 1983).
61. *See Antitrust Division Declines To Attack Broadcasters' Plan to Publish TV Data*, 45 Antitrust & Trade Reg. Rep. (BNA) 250 (Aug. 11, 1983); *Television Revenue and Cost Data*, 609 Trade Reg. Rep. (CCH) 7 (Aug. 15, 1983).
62. FTC Advisory Opinion to Santa Fe Energy Co., *reprinted* in 3 Trade Reg. Rep. (CCH) ¶22,018 (April 18, 1983); FTC Advisory Opinion to Resource Analysis & Management Group, *reprinted* in 3 Trade Reg. Rep. (CCH) ¶22,019 (April 18, 1983).
63. *See Justice Won't Attack Taxi Board's Plan to Provide Data Processing Services*, 43 Antitrust & Trade Reg. Rep. (BNA) 61 (July 8, 1982).
64. *See Justice Will Not Challenge Formation of Travel Agent Cooperative*, 43 Antitrust & Trade Reg. Rep. (BNA) 298 (Aug. 5, 1982).
65. *Id.*
66. *See supra* notes 11 and 44.
67. *See Antitrust Division Raises No Objection to Joint Venture by Diesel Engine Makers*, 44 Antitrust & Trade Reg. Rep. (BNA) 390 (Feb. 24, 1983); *Joint Venture — Small Diesel Engines*, 583 Trade Reg. Rep. (CCH) 11 (Feb. 21, 1983).
68. *See supra* note 2 and accompanying text.
69. *See Justice Won't Challenge Formation of Computer Research Joint Venture*, 44 Antitrust & Trade Reg. Rep. (BNA) 18 (Jan. 6, 1983); *Joint Research*, 575 Trade Reg. Rep. (CCH) 5 (Jan. 3, 1983).
70. *See Antitrust Division Investigates MCTC's Plans for Future Joint Research Projects*, 45 Antitrust & Trade Reg. Rep. (BNA) 15 (July 7, 1983).
71. As it indicated it would in clearing the venture, the Justice Department is currently investigating MCTC's specific research plans and projects to assure that MCTC serves to promote innovation rather than controlling the rate of research and competition in the computer industry. *See id.*
72. *See* Letter from United States Attorney General William French Smith to Small Business Administration Administrator James C. Sanders, *reprinted in* 5 Trade Reg. Rep. (CCH) ¶50,453; *see also Antitrust Division Approves Creation of Immunized Small Business Joint Venture*, 45 Antitrust & Trade Reg. Rep. (BNA) 425 (Sept. 22, 1983).
73. 15 U.S.C.A. §638 (West 1976 & Supp. 1984).
74. *See* Joint Venture Guidelines, *supra* note 9; Antitrust Div., U.S. Dep't of Justice, Antitrust Guide for International Operations (1977); *see also* 1982 Merger Guidelines *supra* note 13.
75. Joint Venture Guidelines, *supra* note 9, at §II, Case B.
76. H.R. 108, 98th Cong., 1st Sess. (1983); H.R. 1952, 98th Cong., 1st Sess. (1983); H.R. 3878, 98th Cong., 1st Sess. (1983); H.R. 3975, 98th Cong., 1st Sess. (1983); H.R. 4043, 98th Cong., 1st Sess. (1983); S. 568, 98th Cong., 1st Sess. (1983); S. 737, 98th Cong., 1st Sess. (1983); S. 1383, 98th Cong., 1st Sess. (1983); S. 1561, 98th Cong., 1st Sess. (1983); S. 1841, 98th Cong., 1st Sess. (1983).

77. H.R. 3878, 98th Cong., 1st Sess. (1983); S. 1841, 98th Cong., 1st Sess. (1983).
78. H.R. 3878, 98th Cong., 1st Sess §202 (1983); S. 1841, 98th Cong., 1st Sess. §202 (1983).
79. H.R. 3878, 98th Cong., 1st Sess., §203 (1983); S. 1841, 98th Cong., 1st Sess., §202 (1983).
80. In contrast, the Export Trading Company Act of 1982, 15 U.S.C.A. §§4001-4021, (West Supp. 1984) utilizes a system of application and approval (by the Secretary of Commerce) in extending antitrust immunity and damage limitation benefits to export trading companies. *Id.* §§4012, 4013, 4016.
81. H.R. 3878, 98th Cong., 1st Sess., §204(a) (1983); S. 1841, 98th Cong., 1st Sess. §204(a) (1983).
82. H.R. 3878, 98th Cong., 1st Sess. §204(b) (1983), S. 1841, 98th Cong., 1st Sess. §204(b) (1983).
83. H.R. 3878, 98th Cong., 1st Sess. §204(c), (d) (1983); S. 1841, 98th Cong., 1st Sess. §204(c), (d) (1983).
84. H.R. 3878, 98th Cong., 1st Sess. §201 (1983), S. 1841, 98th Cong., 1st Sess. §201 (1983).
85. H.R. 3878, 98th Cong., 1st Sess. (1983).
86. The potentially inhibitory effect of the tax laws on research and development efforts was addressed in section 221 of the Economic Recovery Tax Act of 1981, 26 U.S.C.A. §44F (West Supp. 1983), by allowing a 25% tax credit for increases in research activities over prior years. This credit is scheduled to expire on December 31, 1985; the Treasury Department has proposed to extend the credit through December 31, 1988, while limiting qualifying expenditures to those associated with the development of new products or processes or significant improvements to existing products or processes.
87. Joint Venture Guidelines, *supra* note 9.
88. In my own firm's experience, we have never had to discourage proposed joint ventures from their venture; perhaps half a dozen such ventures are now actively operating.

CHAPTER 8
ANNUAL DINNER AND ADDRESS

J. Paul McGrath +

CHAIRMAN KIMBA M. WOOD: Good evening, ladies and gentlemen. I am Kimba Wood, Chairman of the Antitrust Law Section of the New York State Bar Association. On behalf of the Section, I welcome all of you to our Annual Dinner.

We had a full day's program today with six distinguished speakers exploring new directions in antitrust. These participants are here on the dais, and I am going to introduce them to you in a moment. The Section thanks all of the participants for the considerable time and effort that went into the very good presentations. Outlines of the presentations are contained in the handbook that was handed out during the course of the program. I understand that copies are still available should any of you wish to take a look at these excellent outlines.

At this time, I would like to begin the introduction of each of our dais guests. I will ask you to hold your applause until we come to the end of the introductions.

At my far left is Barry Hawk, Professor of Antitrust Law at Fordham Law School. Barry was elected to the Section's Executive Committee this morning, and we welcome him to that position.

Next to Barry Hawk is Barry Brett who has served ably this year as Secretary of the Section and who was this morning reelected to that position. Barry is a partner in the firm of Parker, Chapin, Flattau & Klimpl.

To Barry Brett's right is Bill Lifland of Cahill, Gordon & Reindel who serves as our Section Delegate to the House of Delegates and who made an excellent presentation on today's program on the subject of vertical conspiracy.

Next to Bill is Eleanor Fox, former Chairman of this Section and now a member of the Executive Committee. Eleanor is counsel to Simpson Thacher & Bartlett and teaches at New York University Law School. Eleanor made a lively and scholarly presentation this morning on the subject of mergers and acquisitions.

Next to Eleanor is Jim Halverson of Shearman & Sterling, also a former Chairman of this Section and a member of the Executive Committee.

To Jim's right is Sandy Litvack of Donovan, Leisure, a former Assistant Attorney General in charge of the Antitrust Division. Sandy was this morning elected to the position of Vice Chairman of this Section. He made an excellent presentation today on the subject of international antitrust law.

To Sandy's right is Bob Skitol of Wald, Harkrader & Ross in Washington, D.C. Bob graciously agreed to substitute on today's program for Steve Axinn who, as many of you know, is in the midst of some litigation right now. Bob gave a fascinating talk today on recent antitrust decisions of the Supreme Court.

Next to Bob is Walter Barthold of Barthold & Eikenbery. Walter is chairman-elect of this Section and organized today's excellent program. I'd like to express my special thanks to Walter for all the help he has given me this year.

To my far right is David Klingsberg of Kaye. Scholer, Fierman, Hays & Handler, whose presentation in today's program on state action and other exemptions encapsulated very skillfully the confusing trends in that area of the law.

Next to David is John O'Brien, Actiong Regional Director of the Federal Trade Commission in New York, whom we are delighted to have tonight as our guest.

Next to John is Irving Scher of Weil, Gotshal & Manges, a former Chairman of this Section and a member of the Executive Committee.

To Irv's left is Ralph Giordano who is the Director of the New York office of the Department of Justice Antitrust Division, and who is our Section's liaison to the Antitrust Division.

Next to Ralph is Henry King of Davis, Polk & Wardwell, a former Chairman of the Section and a member of the Executive Committee.

To Henry's left is Taylor Briggs of LeBoeuf, Lamb, Leiby & MacRae, whose presentation today on joint ventures was both enlightening and engrossing.

To Taylor's left is Terry Calvani, formerly a law professor at Vanderbilt Law School and newly appointed Commissioner of the Federal Trade Commission, whom we welcome tonight as our honored guest.

Next to Terry is Paul McGrath, newly appointed Assistant Attorney General in charge of the Antitrust Division, formerly in charge of the Civil Division, and prior to that a partner at Dewey, Ballantine, Bushby, Palmer & Wood. We are delighted to have Paul with us tonight as our featured speaker.

Now your applause for our dais guests is in order.

(Applause)

Thank you.

We are especially honored to be the audience for one of Paul McGrath's first speeches as head of the Antitrust Division. This is undoubtedly a coincidence, but it is altogether fitting and proper that New York should be the setting for one of his first speeches. After all, it was here in New York City that the very first price fixing prosecution was brought.

(Laughter)

The year was 1679 . . .

(Laughter)

....305 years ago. On December 17 of that year, 21 coopers, who made barrels and casks, signed a little agreement. Without a lot of legal jargon, these 21 coopers agreed among themselves that each half barrel they manufactured would be sold to the public for the sum of one shilling, sixpence.

No sooner had the coopers conspired than they were roundly condemned. Mere condemnation was not the end of it. Justice moved a little more swiftly then, and within three weeks they were hauled before the Council Chamber in lower Manhattan. On January 8 of the next year, the coopers' contract was declared void. The verdict read as follows: "They are adjudged guilty, all who have signed the contract, and are to pay each 50 shillings."

There was another point at which custom then didn't quite conform to custom now. Those 50 shilling fines were not paid to the government, and they were not paid to a class of purchasers harmed by the agreement.

Remember, this was 1680. Our Constitution had not been adopted. Separation of church and state was an unknown concept then. So the 50 shilling fine was to be paid either to the church itself or to some other organization that would use the money for "pious purposes."

(Laughter)

There is something else that Mr. McGrath might like to keep in mind during a year in which his boss is seeking reelection to the Presidency. And that is New York's prominent role in the Antimonopoly Party, a party that I suspect we could resurrect in this very room tonight.

(Laughter)

The Antimonopoly Party was born exactly 100 years ago. Its platform was simple. Labor and capital, it said, should be allies, and corporations, the creations of law, should be controlled by law. Luckily for the Antimonopolists, their party found a household name to be their standard-bearer for president. Who among us does not remember General Benjamin Franklin Butler?

(Laughter)

Not to mention his running mate, Gereral Absolom Madden West.

(Laughter)

Well, it was a while ago.

The Antimonopolists did not do too well in the election of 1884. Grover Cleveland won that year, with over 5 million votes. All told, the Antimonopolists garnered 175,000 votes, which was still 25,000 more than the Prohibitionists won that year.

(Laughter and applause)

The Antimonopolists may not have done too well nationwide, but New York gave them 17,000 votes, a full ten percent of all the votes they got.

Both minor parties that year eventually came into their own. The Prohibitionists — well, you know what happened to them. The Antimonopolists, however, really started something. What they started hasn't ended, and the fact that we are here tonight is testimony to the fact that we are all still dealing with questions raised in their platform.

I thought it might be good for Paul to have something to look to for inspiration, should he have moments of prosecutorial uncertainty. On behalf of all of us in the Antitrust Law Section, I'd like to present Paul with a small bust.

(Laughter and applause)

This is a very small bust of the 1884 Antimonopoly Party candidate for President, General Benjamin Franklin Butler.

(Laughter and applause)

J. Paul McGrath

Some Americans — hopefully few in this room — harbor rather extreme views on antitrust enforcement. There are those who believe that the main function of the Antitrust Division is simply to bring a lot of lawsuits — any kind of lawsuits — to keep businessmen in a state of constant concern that one false move and they will go to jail or pay a huge fine or see their companies dismantled. Others argue that in this era of dramatic economic change businessmen already have too many problems without having to worry about the antitrust laws and that there ought to be some kind of a recess from antitrust enforcement — at least for troubled industries. Each of these views misconceives the proper role of antitrust.

The last 94 years prove conclusively that when we have concentrated on rules that foster competition and on unleashing the incredibly diverse talents of our economy to produce new and better products at lower costs — in short when we have concentrated on consumer welfare — antitrust enforcement has been good. But when we have followed policies with no sound basis in economics or tried to use antitrust as a kind of populist scheme, then the enforcement of these laws has been terrible.

It should come as no suprise that the Antitrust Division today views as fundamental the goal of promoting competition. We seek to promote the competitive process — the process which drives our economy by fostering efficiency and spurring innovation, thereby creating opportunities for economic growth. Preservation and enhancement of our free market economy are critical today as we consolidate the gains of the current economic recovery.

The Antitrust Division works toward this goal in two basic ways, one obvious and one not so broadly appreciated. First, and obviously, we enforce the antitrust laws to ensure that the competitive process is permitted to flourish. We seek to condemn and deter practices that artificially inflate costs and unreasonably exclude competition from concentrated markets. At the same time we try not to interfere with business arrangements that do not create or misuse market power but rather foster efficiency.

In addition to our role as prosecutor — as case-bringer, if you will — there is a second role that I regard as of equal importance, perhaps because of my background as a private antitrust lawyer. That is our "educational" role, in which we bring to the bench and the private bar and to business people the fruits of the best legal and economic analysis we can muster on questions of antitrust policy.

This kind of analysis is routinely done in the exercise of prosecutorial discretion. Our enforcement resources are not unlimited, and they should be targeted to address the competitive problems that most seriously threaten consumer welfare. Historically, however, the Antitrust Divison has gone beyond merely using its analysis to decide which cases to bring and how to prosecute those cases. For many years it also has quite properly assumed an educational function. In speeches, in articles and in guidelines the Division has spelled out its enforcement policies to the public, for the guidance of businessmen and the bar. In carrying out this function, the Antitrust Division has played a particulary strong role in helping to develop antitrust doctrine where the law may be relatively unsettled or even unsound. It is, of course, not our function to settle or make the law, but we do have an important role to play in helping to bring the law into line with our best legal and economic thinking. Over the years, the Antitrust Division has had an enormous impact on the law, for two main reasons. First, our lawyers and economists are an enormous collection of legal and economic talent. And it is also widely recognized that the Antitrust Division is institutionally unbiased — neither pro-big business nor pro-small business; neither pro-manufacturer nor pro-distributor.

The reason I am focusing on this tonight is that this is a particularly critical time for guidance and for settling of the law. There have been fundamental changes in antitrust law during the last few years, not just new rules but new approaches, particularly in the willingness of courts and scholars to consider the best, up-to-date economic thinking. Of course, in the landmark *Standard Oil* case, Chief Justice White observed that antitrust law would change as economic understanding progressed.[1] As Judge Bork puts it, this means that

> [t]here is no particular reason why courts have to keep doing harm, rather than good, once they understand economic reality.

And since there has been more solid economic work done in the antitrust field during the last decade and a half than in the prior 70 years, this means that the courts approach to antitrust has been — and should be — different today from 20 years ago. But in turn this leads to uncertainty at a time of rapid technological change and difficult international business competition.

With that background, let me focus on one area as an example of both evolution and the uncertainty that often accompanies that evolution — that of vertical restraints or vertical practices.

In order to understand how this area came to be a problem, we need to look back at two parallel historical developments in the period from roughly 1940 to 1970. During those years courts were making it more and more difficult for manufacturers to choose the manner in which their products were distributed by creating new per se prohibitions and lessening the amount of evidence needed to establish the "combination" or "conspiracy" necessary to hold the manufacturer in violation of section 1 of the Sherman Act. At the same time, economists were learning a great deal about how markets work. They concluded that restricting a manufacturer's freedom to choose among distribution methods often prevents the manufacturer from choosing the most efficient one. Economists found that rigid restrictions on the distribution of products was hardly a prescription for either economic growth or greater competition, for that matter.

The rules being devised by the courts were plainly at odds with the results of this economic analysis. The earliest Supreme Court decision to acknowledge this was *Standard Stations* in 1949, where that Court appeared to take the position that economic efficiencies could flow from exclusive dealing[2] but refused to give any weight to those efficiencies on the ground that courts were ill-suited to the task.[3]

The gap between law and economics widened in the 1960's. In 1967 in the *Schwinn* case[4] the Court overruled the four-year-old *White Motor* decision[5] and abruptly changed course and held customer and territorial restrictions illegal per se even though there was neither legal precedent, nor historic experience, nor generally accepted economic theory to support that step. At the time *Schwinn* seemed almost a definitive rejection of an economic approach to vertical restraints. Yet, it was soon apparent that an economic view of vertical restraints was in fact gaining ground rather than losing it. Ultimately, of course, economic analysis won out in *GTE Sylvania*,[6] where *Schwinn* was overruled and customer and territorial restraints were held subject to the rule of reason. The *GTE Sylvania* decision is a virtual economic treatise, in which the Court quite conclusively proves that courts are very well-suited to analyze the economic efficiencies inherent in business arrangements.

While *GTE Sylvania* solved some of the problems relating to vertical restraints, it also created a number of new complications for in that case the Court simply decided that a rule of reason analysis would apply and not what distribution systems were lawful and which ones unlawful.

The result has been confusion. I will cite only two especially striking example: in *Dos Santos*[7] the Seventh Circuit treated an exclusive arrangment between a hospital and a group of anesthesiologists as an exclusive dealing contract subject to the rule of reason; in *Hyde*[8] a similar contract was held by the Fifth Circuit to be a per se illegal tie-in. Similarly, on a single day in 1982, two different panels of the Eighth Circuit reached precisely opposite conclusions as to whether complaints to a manufacturer by dealers that another dealer was engaged in price-cutting, followed by termination of the price-cutter, were enough to imply a conspiracy in violation of section 1.[9] Last year the cases were reheard en banc and the result in both cases was a 4-4 tie.[10] Plainly manufacturers engaged in national distribution of their products can derive little comfort from the fact that their distribution arrangements are lawful in some places and of doubtful legality in others or from the fact that half the judges in a particular circuit would rule in their favor, while the other half would not.

In order to deal with the problems created in the wake of *GTE Sylvania*, the Antitrust Division is engaged in both a short-range strategy to help patch up existing law, and long-range strategy to bring about application of a sound economic approach to vertical practices generally and to simplify the litigation of vertical cases

For example, in the *Hyde* case that I mentioned earlier, which has been argued and is awaiting decision by the Supreme Court, we filed an amicus brief that combined both strrategies. We urged the Court to clarify the status of exclusive arrangements such as the one in that case so that businesses could know which side of the rule of reason per se line they fell on. In addition, we asked the Court more generally to restate the law of trying so that that law is more clearly in line with the economic approach.

We are planning to continue these efforts. Where appropriate, we will file *amicus* briefs with the courts explaining our position on current problems, such as the characterization of the distribution schemes and the method of proving conspiracy. I expect also to give another speech this year that will spell out our views on both current and long-range questions of vertical enforcement policy. And in the tradition of the guidelines I mentioned earlier, we are working hard on an antitrust guide to vertical practices. We expect that our vertical guide will explain the economics of vertical practices, and show how current Division policy follows from those economics. It is contemplated that the guide will set out a method for simplifying the adjudication of vertical practice cases, so that firms wishing to engage in beneficial vertical practices are not discouraged by the prospect of lengthy pretrial and trial proceedings, and so that firms desiring to impose anticompetitive vertical practices are not encouraged by the prospect of wearing down plaintiffs through protracted rule of reason trials.

As you are no doubt aware, in recent years the Division has not brought many cases concerning vertical practices. One reason for this is that there are plenty of private plaintiffs who have demonstrated the willingness and the ability to detect and challenge vertical arrangements which may have caused them antitrust injury. In contrast, our investigative and prosecutorial resources have in large part been devoted to identifying and challenging collusive behavior which may not be so readily detected by aggrieved private parties. It would be a serious mistake, however, to infer from recent history that the Division will not challenge vertical conduct. When vertical practices increase the risk of collusion or throw unnecessary obstacles in the path of competition, they produce horizontal effects of great concern and will be challenged vigorously.

A serious likelihood of collusion might exist, for example, where exclusive dealing arrangements are broadly employed in a market characterized by high concentration at the distribution level or where industry-wide adoption of certain vertical practices may facilitate collusion by helping cartel members to monitor secret discounting. Vertical arrangements will also be questioned where companies with strong market positions engage in practices designed to exclude their competitors. An example of such a misuse of market power is discussed in our filing with the Civil Aeronautics Board concerning airline computer reservations sytems. In short, the mere fact that anticompetitive practices such as these are nominally vertical in form will by no means immunize them from Division action.

The subject of vertical restraints merits a great deal of our attention, because so many businesses, so much commerce and so much consumer welfare is involved. There are other areas that merit equal attention.

Consider, for instance, merger policy — an area of intense interest to the business community as a whole. The law increasingly (and, in my view, properly) recognizes that mergers can have significant economic benefits. In keeping with this trend, the Department's 1982 Merger Guidelines[11] were intended to assist enforcement agencies and the courts in narrowing the focus of legal attack to those mergers which appear most likely to facilitate the exercise of market power. Nearly two years have passed since the Guidelines were issued, however, and we are already actively considering a revision of these Guidelines to reflect the experience of the past two years. Although I believe the Guidelines reflect a sensible enforcement policy and work rather well, it is important that we keep them continually up-to-date and not simply allow them to become obsolete, as happened to the 1968 Guidelines.[12]

A related topic of concern is the impact of current antitrust law on the formation of joint ventures for research and development. If fear of antitrust liability may deter the formation of desirable R&D joint ventures, the antitrust laws may actually have anticompetitive effects. Such effects are the natural, albeit unfortunate, consquence of prudent antitrust counseling in the face of legal uncertainty. To reduce that uncertainty and thereby remove impediments to joint ventures that may well be procompetitive, President Reagan has proposed legislation that would require courts to judge joint ventures under a rule of reason standard.

Of equal concern are developments related to the licensing of technology — another area where current law often has anticompetitive effects. Again, certain older court decisions cast doubt on the legality of arrangements which, in most business settings, would be perfectly reasonable, indeed pro-competitive. In addition to seeking legislation that would mandate rule of reason treatment for technology licensing arrangements, we plan to spell out in speeches — and perhaps guidelines — a more realistic enforcement approach to this important subject.

It is probably fair to say that each of the topics I have mentioned so far is in some measure controversial, in part because of gaps between what lawyers think the law may be and what economists say the law should be. Battle lines tend to form over the dimensions of those gaps, the pace with which they are being narrowed by Congress and the courts, and indeed whether they should be narrowed at all. It is not our intention to politicize the antitrust debate, but rather to focus it — a function that is a traditional and proper role for the Antitrust Division.

There also remains for discussion one topic which I consider wholly uncontroversial but nonetheless critical: our continued vigilance in enforcing the nation's laws against collusive conduct among horizontal competitors. Price fixing does more than impose excessive costs on consumers; it runs counter to the economic underpinnings of our society, and the Division has no higher priority than its efforts to detect and prosecute such conduct wherever it may exist in our economy. In that regard I should note that we currently have 109 active grand juries throughout the nation, of which 55 are investigating activity unrelated to construction industries. Although I believe the Division's performance in prosecuting price fixing has been splendid, we would like to make it even better. To that end, I have set up a task force of Antitrust and Criminal Division personnel to look into ways of sharpening our investigative techniques. I think both Divisions are likely to benefit from such an effort and if I am correct, the real winners will be the American people, whose tax dollars will produce even greater enforcement results.

The role of educator may sound like an odd one for someone charged with enforcing the antitrust laws to adopt. It is not. Economists have been breaking new frontiers in antitrust theory, and the simple truth is that neither the lawyers nor the courts have been able to keep up.

If I were concerned solely with my responsibility for antitrust enforcement, perhaps I could ignore those facts, and say that informing the bar and focusing the debate were the responsibilities of academics, or as we sometimes call them, the professors.

I do not agree with that. We have 50 economists in our Office of Economic Policy, and I believe them to be not only highly capable, but the very backbone of intelligent and responsible antitrust enforcement. We could save them for prosecuting cases, knowing that many, if not all defendants, could muster to the defense expensive economists of their own.

I do not think that is our job. To prosecute, yes. To use the resources at our command solely to prosecute, no.

I believe that we have a positive obligation to use that impressive pool of experienced and capable economic talent, as well as the 350 skilled lawyers in the Antitrust Division, to make every possible effort to see that potential defendants are given a fighting chance to avoid being defendants. Don't tell me how difficult that can be. I know. Why is that? The answer is simple.

You do not have to be a genius to advise a client how to avoid being nailed for extortion, or stock fraud, or bribery.

What is so different about antitrust law? Is it any harder to counsel a client to avoid a felony indictment for price fixing or rigging? No, not very much.

Where the ambiguity comes in is in the civil area, particularly with vertical restraints, but not exclusively so. Courts split every which way, and a trial can turn on the expertise of one economic witness against another. There is no certainty, and in the absence of knowledge, wise counsel is hard to find. But the stakes remain high. Perhaps indicment and prison do not hang in the balance, but treble damages, and even class action treble damages, loom almost as large among corporate nightmares.

So the prudent avoid risks, and thus the hope of gain, and the reckless seek gain, and risk disaster. Do they have to shoot craps with their corporate futures, with stockholders' savings, with the jobs of their employees? If we were a self-righteous government, a bunch of arrogant grey bureaucrats in grey buildings in Washington, who wanted to keep their cards face down, we might do that.

But we won't play that game. We get paid to play fair, and if we lose, we lose. If there is anything we can tell you or your clients to prevent them from becoming defendants, then we have a lawyer's obligation to do it.

So we take our role as educators seriously, and we are not even slightly ashamed to spend our time and the taxpayers' money trying to assure that those of you who counsel corporate clients have every bit as much knowledge and expertise as we have. We are not interested in piling up statistics of convictions. We believe it is sound policy to spend money and time trying to prevent violations of the law. That means guidelines, detailed, quantitative guidelines. They will not be easy, and they will not win headlines, but American business, and the American taxpayers, and the American consumers deserve no less.

In summary, the Antitrust Division has a vital role in the tough world facing American business. American business is facing foreign competition of a caliber and toughness we have never seen before. American knowhow and the ability of Americans to adapt and deal with this new and dangerous environment is being tested daily and will be tested even more in the next decade and beyond. The only way we will survive this competitive onslaught intact is to become tougher competitors ourselves, and antitrust policy has a significant role to play in that struggle.

We must avoid the habits of thought that cast antitrust policy as the enemy of business strength and prosperity. Antitrust policy exists to foster competition, not to stifle it. Wherever we can remove ambiguity or unfounded fears that inhibit sound business decisions and risks we have an affirmative obligation to do so — and we will.

At the same time, we have an equally strong obligation to crack down on that small minority of American business that has responded to the challenge of competition by hiding inside price fixing or bid rigging conspiracies. Such people are thieves and felons, and if we can make cases against them, and have the evidence to convict them, we should put them behind bars — and we will do just that.

Time will tell how well we meet both tasks. I hope I have made clear that we take both very seriously.

CHAIRMAN WOOD: I know I speak for all of you in thanking Paul for sharing with us his thoughts on his agenda for the future. I can assure you, Paul, that we will all be watching intently, and eagerly awaiting the execution of that agenda.

This concludes the Annual Dinner, and I thank you all very much for coming.

FOOTNOTES

* Assistant Attorney General, Antitrust Division, Department of Justice.

1. Standard Oil Co. v. United States, 221, U.S. 1, 57-59 (1911).
2. Standard Oil Co. v. United States, 337 U.S. 293, 306-07 (1949).
3. *Id.* at 308-14.
4. United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967).
5. White Motor Co. v. United States, 372 U.S. 253 (1963).
6. Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977).
7. Dos Santos v. Columbus-Cuneo-Cabrini Medical Center, 684 F.2d 1346 (7th Cir. 1982).
8. Hyde v. Jefferson Parish Hosp. Dist. No. 2 686 F.2d 286 (5th Cir. 1982), *rev'd* 104 S. Ct. *1551* (1984).
9. Battle v. Lubrizol Corp., 673 F.2d 984 (8th Cir. 1982), *affd en banc by an equally divided court*, 712 F.2d 1238 (8th Cir. 1983), *petition for cert. filed*, 52 U.S.L.W. 3210 (U.S. Sept. 9, 1983)(No. 83-431); Roesch, Inc. v. Star Cooler Corp., 671 F.2d 1168 (8th Cir. 1982), *affd en banc by an equally divided court*, 712 F.2d 1235 (8th Cir. 1983), *petition for cert. filed*, 52 U.S.L.W. 3191 (U.S. Sept. 9, 1983)(No. 83-412).
10. Battle v. Lubrizol Corp., 712 F.2d 1238 (8th Cir. 1983), *petition for cert. filed*, 52 U.S.L.W. 3210 (U.S. Sept. 9, 1983) (No. 83-431); Roesch, Inc. v. Star Cooler Corp., 712 F.2d 1235 (8th Cir. 1983), petition for cert. filed, 52 U.S.L.W. 3191 (U.S. Sept. 9, 1983) (No. 83-412).
11. United State Dep't of Justice Merger Guidelines - 1982, *reprinted in* 2 Trade Reg. Rep. (CCH) ¶¶4501-05.
12. United States Dep't of Justice Merger Guidelines - 1968, *reprinted in* 2 Trade Reg. Rep. (CCH) ¶4510.