7. Unreasonableness

Antitrust Law

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Topics

- Review of elements of a Section 1 prima facie case
- Reasonableness in the early law
- Operationalizing unreasonableness in light of the goals of antitrust law
- Proving unreasonable restraints today
  - The per se rule
  - The rule of reason
  - The "quick look"

Elements of a Section 1 Prima Facie Case

Sherman Act § 1—Creates Offense

- Creates the offense of a "contract, combination . . . or conspiracy, in restraint of trade or commerce"

> **Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal.** Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.[1]

[1] 15 U.S.C. § 1.

Elements of a Section 1 Offense

- Recall that there are four elements of *every* Section 1 offense
  1. A plurality of actors with the legal capacity to conspire with one another (*Copperweld*, *American Needle*),
  2. An agreement ("contract, combination . . . or conspiracy") among these actors,
  3. Whose object is a "restraint of trade or commerce"
  4. That is unreasonable within the meaning of the antitrust laws (*Standard Oil*)

These notes focus on the fourth element

Reasonableness in the Early Law

The Early Law

- Common law
  - Restraints in the common law cases were noncompetition covenants
  - Contracts in restraint of trade (nonreciprocal and ancillary)
    - General restraints
      - Restraints that were unrestricted in the coverage
      - Conclusively presumed to be unlawful
    - Partial restraints
      - Restraints that were limited in their coverage in product, time, and geography
      - Lawful if they—
        - were ancillary to a legitimate business purpose (e.g., the sale of a business)
        - were no broader than necessary to accomplish this business purpose, and
        - did not harm the public
  - Combinations/conspiracies in restraint of trade (reciprocal and nonancillary)
    - Generally unenforceable as nonancilliary restraints that raise prices and reduce output
    - A few cases accepted "destructive competition" as a cognizable business purpose that could justify the restraint
  - Actions at common law against restraints sound only in contract
    - No criminal or quasi-tort actions

The Early Law

- Early Sherman Act cases
  - *Trans-Missouri* read the language of the Sherman Act literally to prohibit *every* restraint of trade[1]
    - Irrelevant whether the challenged restraint would have been reasonable at common law
  - *Joint Traffic* reaffirmed the "every restraint" rule
    - But sought to limit its scope "only to those contracts whose direct and immediate effect is a restraint upon interstate commerce"[2]
  - But a "effect of commerce" limitation not workable
    - As geographic markets of firms expanded with improved technology and broader and more reliable transportation and communications network, restraints that increased efficiency could nonetheless affect commerce and therefore be unlawful
    - Needed a different limiting principle

[1] United States v. Trans-Missouri Freight Ass'n, 166 U.S. 290, 312 (1897) (Peckham, J.).
[2] United States v. Joint-Traffic Ass'n, 171 U.S. 505, 568 (1898) (Peckham, J.).

Standard Oil[1]

- Holdings
  - Rejected the *Trans-Missouri*/*Joint Traffic* “every restraint” rule
  - Sherman Act was to be construed and applied to restraints using “reason” in light of the historical concerns about the “evils of monopoly”
    - Higher prices
    - Reduced output
    - Reduced product or service quality
  - Sherman Act was designed to be adaptable using reason to new forms of contracts and combinations as they emerge
  - Prohibited restraints can be shown be either—
    - their inherent nature, or
    - their actual purpose and effect [of restraining trade and bringing about evils of monopoly]
  - Reaffirmed results (but not reasoning) of *Trans-Missouri* and *Joint Traffic*
    - Horizontal price fixing arrangements that by their inherent nature raise prices
      - “Reasonableness” of price is irrelevant
      - Elimination of “destructive competition” is not a justification for a price-increasing restraint

[1] Standard Oil Co. v. United States, 221 U.S. 1 (1911) (White, C.J.).

The Modern Approach

- Continues to use White's *Standard Oil* analysis
- But some of the language has morphed
  - Restraints prohibited by the Sherman Act are called *unreasonable* restraints
    - NOT congruent with unreasonable restraints under the common law
      - E.g., an overbroad nonreciprocal ancilliary restraint need not violate the Sherman Act, even though it is unreasonable and hence unenforceable at common law
      - *Aside*: Most states have adopted the late nineteen century common law approach as part of their law of contracts in assessing the enforceability of noncompetition covenants
  - Restraints prohibited by the Sherman Act because of their inherent nature
    - are called *per se unlawful*
    - are subject to Sherman Act scrutiny under the *per se rule*
  - Restraints prohibited by the Sherman Act because of their actual purpose and effect are evaluated under the *rule of reason*
    - Restraints that do not violate the Sherman Act under the rule of reason are called *reasonable*

Operationalizing Unreasonableness in Light of the Goals of Antitrust Law

Unreasonableness under the Sherman Act

- Unreasonableness is measured against the objectives or goals the antitrust laws are deemed to promote
  - This is Chief Justice White's rule in *Standard Oil*
- These goals are a political value judgment
  - But historically made by courts using the common law approach
  - By not Congress through legislation
- Antitrust goals may
  - Differ across jurisdictions
  - Differ within a given jurisdiction over time
- As the operative antitrust goals change, the antitrust rules are likely to change as well

Antitrust Goals

- The early objective was the prevention of the “evils of monopoly”
- Other goals that have had some traction at some point in Sherman Act history include—
  - Promoting the prospects of survival of small businesses
  - Keeping industrial concentration below certain thresholds
  - Minimizing restraints on freedom of choice of economic actors
  - Promoting the operation of the “competitive process”
  - Maximizing allocative efficiency
  - Maximizing total surplus
  - Maximizing consumer surplus
  - Maximizing consumer welfare

Unreasonableness under the Sherman Act

- A given jurisdiction may have multiple—and not always consistent—goals at the same time
- Different jurisdictions can have very different goals
  - Early E.U.: Unifying the member countries into a single market
  - Many Eastern European countries: Prevent new government-sponsored monopolies and break up old ones
  - Some countries (China?): Protect national industries against foreign competition

Evolving Antitrust Goals in the United States

- Look at three time periods since World War II
  - The "boom" times (circa 1950 to 1972)
  - The "malaise" period (circa 1973 to 1982)
  - The modern period (circa since 1982)

> *Hypothesis*: U.S. antitrust goals change in response to changes in macroeconomic conditions and U.S. international competitiveness

The “Boom” Times (circa 1950 to 1972)

- Enormous tightening of antitrust rules
  - Further tightening on horizontal price fixing
    - Actually begin somewhat earlier (*Socony-Vacuum*)
    - Easing of rules to find concerted action (*Container Corp*.)
  - Horizontal mergers—close to per se unlawful
    - E.g., *Brown Shoe*, *PNB*, *Pabst/Blast*, *Von's Grocery*, *Potter Stewart rule*, 1 968 Merger Guidelines
  - Vertical mergers—close to per se unlawful
    - *DuPont/GM*
  - Conglomerate mergers seriously challenged
    - *P&G*, *Falstaff*, *El Paso Natural Gas*, the DOJ potential competition campaign
  - Tightening of Section 2 prohibitions and enforcement
    - *Alcoa*
    - *Grinnell*, *IBM* (filed 1969), *AT&T* (filed 1974)
    - “Shared monopoly” theory

The “Boom” Times (circa 1950 to 1972)

- Enormous tightening of antitrust rules
  - Nonprice vertical restraints—per se unlawful
    - *Albrecht*
    - *Schwinn* (1967) (overruling *White Motor* (1963))
  - Reinforcement of tying arrangements as per se illegal
    - *Northern Pacific* (1958)
  - Tightening of rules on refusals to deal
    - *Associated Press* (1945) (horizontal boycott)
    - *Klor's* (1959) (secondary boycott)
  - Horizontal combinations/joint ventures
    - *Sealy*
    - *Topco*
  - Remedies and procedure
    - *DuPont* (1957) (essentially finding that the DOJ cannot be time-barred in a government injunctive actions where there continue to be effects traceable to an acquisition that occurred 30 years earlier)
    - *Hanover Shoe* (1968) (holding that Clayton Act § 4 does not recognize a “passing on” defense)

The "Boom" Times (circa 1950 to 1972)

- Economic conditions—Let the good times roll

Indicator	1950-1972
Real GDP (average annual growth)[1]	4.1%
Nonfarm business productivity (average annual rate)[2]	2.8%
Inflation (average annual change Dec. to Dec.)[3]	2.6% Max = 6.2%
Bank prime loan rate (annual—data series starts in 1956)[4]	5.8% Max =8.0%
Unemployment (average monthly rate)[5]	4.6% Max = 7.5%
Median real family income (average annual change)[6]	3.3%

The "Boom" Times (circa 1950 to 1972)

- Great concern following WWII about—
  - The economic and political power of large industrial concentrations
  - The loss of opportunity for small business when competing with large enterprises
  - The spread of multistate enterprises and the loss of local control over industry
- Strong political pressures to do address these concerns
- Congress, courts, and antitrust enforcement officials responded

The "Boom" Times (circa 1950 to 1972)

- The revealed goals
  - Minimize industrial concentration beyond certain bounds
  - Maximize the prospects of survival of small businesses
  - Minimize restraints on freedom of choice of economic actors
- Observations
  - Willingness to trade off some industrial efficiency, increased production, and lower prices to promote these goals
  - Not clear how much appreciation there was of what was being traded off
  - But it did not matter practically—the growth in the economy turned the losses into noise

The “Maliase” Period (circa 1973 to 1982)

- Courts begin to “loosen” antitrust restrictions and adopt a more economic approach to antitrust analysis
  - Horizontal mergers—near per se illegality replaced by effects analysis
    - *General Dynamics*
  - Potential competition mergers—Courts rejected DOJ's prosecution campaign
  - Section 2
    - General rejection of “shared monopoly” as an actionable theory of harm
  - Nonprice vertical restraints—returned to rule of reason treatment
    - *GTE Sylvania*
  - Robinson-Patman Act
    - DOJ urging repeal as anticompetitive
  - Antitrust (prudential) standing
    - *Brunswick*

Note: The appellation for this period was suggested by a speech by President Carter. *See* Pres. Jimmy Carter, Crisis of Confidence, Televised Addressed to the Nation (July 15, 1979) (popularly known as the “Malaise Speech”).

The “Maliase” Period (circa 1973 to 1982)

- “Stagflation” gripped the nation
  - Significant inflation as a result of the Mideast oil shocks in 1973 and 1979 and the easy monetary policy of the late 1960s
  - “Productivity crisis” from the obsolescence of “old economy” and equipment
- Substantial concern about U.S. competitiveness in the world market (especially against Japan) in areas that since WWII that had been traditional American strengths (e.g., automobiles, steel)
- The growing influx of imported manufacturing goods threatened some American industries in the domestic market (e.g., consumer electronics)
- Gasoline shortages/price controls

The "Maliase" Period (circa 1973 to 1982)

- Economic conditions—Not good times

Indicator	1950-1972	1973-1982
Real GDP (average annual growth)[1]	4.1%	2.4%
Nonfarm business productivity (average annual rate)[2]	2.8%	1.0%
Inflation (average annual change Dec. to Dec.)[3]	2.6% Max = 6.2%	8.7% Max = 13.3%
Bank prime loan rate (annual—data series starts in 1956)[4]	5.8% Max =8.0%	11.10% Max = 18.9%
Unemployment (average monthly rate)[5]	4.6% Max = 7.5%	7.0% Max = 10.8%
Median real family income (average annual change)[6]	3.3%	-0.2%

The "Maliase" Period (circa 1973 to 1982)

- Sentiment toward business
  - Government policies generally needed to be revised to:
    - Foster America's industrial competitiveness
    - Revive the nation's industrial base
    - Return to the country to the post-WWII standards of steady growth, low inflation, and low unemployment
  - WWII concerns about the evils of large industrial concentrations largely had dissipated
    - Could not afford to act on the concerns in any event, especially given the perceived success of the Japanese keiretsu

The "Maliase" Period (circa 1973 to 1982)

- Rapidly emerging perception/consensus that—
  - Many antitrust rules impeded efficient business operations and constrained competitiveness
  - Antitrust was a blunt and unnecessary instrument for achieving distributional goals
  - To the extent that distribution goals remain relevant, other government instruments might be better suited to achieving them
- Strong political pressures to do address these concerns
- First courts, and then reluctantly antitrust enforcement officials, and finally Congress responded

The "Maliase" Period (circa 1973 to 1982)

- The revealed antitrust goal
  - Maximize output and industrial productivity

- Big open question:

How should antitrust rules be fashioned to achieve this goal?

The Modern Period (circa 1982 to present)

- Antitrust rules refashioned
  - No change in strict prohibitions and aggressive enforcement against “garden variety” horizontal price fixing
  - But new limitations on finding concerted action
    - Single entities: *Copperweld, American Needle*
    - From circumstantial evidence: *Matsushita, Business Elecs.*, *Brooke Group*
  - New possibilities of removing horizontal conduct from per se treatment
    - *BMI*
  - Horizontal mergers require affirmative finding of anticompetitive effect
    - 1982 DOJ Merger Guidelines
  - Vertical mergers require affirmative finding of anticompetitive effect
    - Only episodic government actions:
  - Conglomerate merger theories of harm abandoned

The Modern Period (circa 1982 to present)

- Antitrust rules refashioned
  - Significant loosing of restrictions on dominant firm behavior
    - *Spectrum Sports*, *Brooke Group, Trinko*, *Linkline , Weyerhauser ,* DOJ Section 2 Report (but see *Aspen Skiing,* withdrawal of Section 2 report)
    - Only episodic government actions (*Microsoft*, *American Airlines, Intel*)
  - Significant loosing of restrictions on distributional restraints
    - *Monsanto, Kahn, Leegin* (but see *Kodak*)
  - New requirement for finding illegal tying arrangements
    - *Jefferson Parish*
  - Remedies and procedure
    - *Empagran* , *Twombly*

  - Foreign Trade Antitrust Improvements Act of 1982
  - National Productivity and Innovation Act of 1983
  - National Cooperative Research Act of 1984

The Modern Period (circa 1982 to present)

- Economic conditions—recovering, then pretty good (then not too good)

Indicator	1973-1982	1983-2006
Real GDP (average annual growth)[1]	2.4%	3.4%
Nonfarm business productivity (average annual rate)[2]	1.0%	2.2%
Inflation (average annual change Dec. to Dec.)[3]	8.7% Max = 13.3%	3.1% Max = 6.1%
Bank prime loan rate (annual—data series starts in 1956)[4]	11.1% Max = 18.9%	8.0% Max = 12.0%
Unemployment (average monthly rate)[5]	7.0% Max = 10.8%	5.9% Max = 10.4%
Median real family income (average annual change)[6]	-0.2%	0.9%

The Modern Period (circa 1982 to present)

- Continued concern about increasing industrial output and productivity
  - Economic indicators during period have an upside-down “U” shape:
    - Recovering—not too gracefully—from the 1970s during 1983-1992
    - Reach affirmatively good times during 1993-2000 (which ended with the dot.com bust)
    - More stagnant times during 2001-2006 (with slow but steady recovery aided by an easy money policy and resulting in an asset bubble and significant overleveraging)
    - Financial crisis, deep recession, and very slow recovery since 2007
  - But sustained growth, like that found in the post-WWII period, never returned to the U.S.
    - U.S. never politically regained the “luxury” of trading off output and efficiency for deconcentration/small business/freedom of economic choice concerns

The Modern Period (circa 1982 to present)

- Prevailing goal in the United States
  - Prevent the creation or exercise of market power to the detriment of customers
  - Usually manifested in actual or threatened —
    - Higher prices
    - Reduced market output
    - Reduced market product or service quality
    - Reduced rates of technological innovation or product improvement

    Compared to what would have existed in the absence of the challenged restraint and with no offsetting customer benefits.
  - Practical corollaries (lexicographically ordered)
    - Allow restraints that increase market output
    - Allow restraints that decrease market prices

      In long-term equilibrium
    - Prohibit restraints that decrease market output
    - Prohibit restraints that increase prices (without an offsetting customer benefit, such as improved

The Operative Goal Today

- Prevent the creation or exercise of market power to the detriment of customers
  - Usually manifested in actual or threatened —
    - Higher prices
    - Reduced market output
    - Reduced market product or service quality
    - Reduced rates of technological innovation or product improvement

    Compared to what would have existed in the absence of the challenged restraint and with no offsetting customer benefits.
  - Major practical implications (lexicographically ordered):
    - Prohibit restraints that decrease long-run market output
    - Permit restraints that increase long-run market output (even if prices increase)
    - Prohibit restraints that increase prices when there is no offsetting output effect
    - Do not intervene when there is no adverse output or price effect

Proving Unreasonableness Today

Proving Unreasonableness

- *Standard Oil* created (in modern terms) two methods of proving that a challenged restraint is unreasonable:
  - The *per se rule*—a conclusive presumption of unreasonableness based on the inherent nature of the restraint
  - The *rule of reason*—requires the plaintiff to prove though affirmative evidence that the likely effect of the restraint is to be anticompetitive[1]
- Modern courts have developed a third method of proving that a challenged restraint is unreasonable:
  - The *"quick look"*—a rebuttable presumption of unreasonableness based on the apparently inherently anticompetitive nature of the restraint
    - The quick look is sometimes called the *truncated or abbreviated rule of reason* or *inherently suspect analysis*

[1] *Anticompetitive* means that the restraint creates an effect that the operative goals of antitrust law would prohibit.

The "Pigeonholing" Approach

- U.S. antitrust law follows a "pigeonholing" approach
  - Courts have classified common business practices as subject to either the per se rule or the rule of reason
  - The per se illegal categories are important but limited and have been declining in number since 1977
  - The rule of reason is the default category for any restraint that does not fall into a per se illegal category
  - The quick look so far has ben used infrequently and is very ad hoc
    - Applies to restraints that appear to be inherently anticompetitive but do not fall within a per se unlawful category

The Per Se Rule

- *The per se rule*: A conclusive presumption of unreasonableness based on the inherent nature of the restraint
  - Sufficient for plaintiff to prove that the challenged restraint falls into a category of restraints judicially recognized to be per se unlawful (e.g., horizontal price fixing)
    - Can use direct or circumstantial evidence to prove categorization
  - Not necessary that restraint actually or likely be anticompetitive
  - Lack of market power or anticompetitive effect *not* a defense to a per se unlawful violation
- Rationale
  - The per se rule is essentially a rule of efficiency
    - The idea is that the probability that per se illegal conduct is anticompetitive is so high that the costs associated with performing a full competitive analysis outweighs the expected social benefits from identifying and avoiding the few overinclusiveness errors that might otherwise occur[1]

[1] *See* Arizona v. Maricopa County Med. Soc'y, 457 U.S. 332, 344 (1982).

The Per Se Rule

- Characteristics of per se unlawful restraints
  - "[F]acially appears to be one that would always or almost always tend to restrict competition and decrease output," rather than one designed to "increase economic efficiency and render markets more, rather than less, competitive"[1]
  - "Plainly" or "manifestly" anticompetitive[2]
  - "[P]ernicious effect on competition and lack . . . any redeeming virtue"[3]

[1] Broadcast Music, Inc. v. CBS, 441 U.S. 1, 19-20 (1979).
[2] E.g., Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 886 (2007).
[3] Northern Pac. Ry. Co. v. United States, 356 U.S. 1, 5 (1958).

The Per Se Rule

- Classifying business conduct as per se unlawful
  - “It is only after considerable experience with certain business relationships that courts classify them as per se violations.”[1]
  - Then only when this experience “enables the Court to predict with confidence that the rule of reason will condemn it.”[2]
  - Courts will not apply the per se rule to restraints “where the economic impact of certain practices is not immediately obvious.”[3]

[1] United States v. Topco Assocs., Inc., 405 U.S. 596, 405 U.S. 607-08 (1972).
[2] Arizona v. Maricopa County Med. Soc'y, 457 U.S. 332, 344 (1982).
[3] Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 551 U.S. 877, 887 (2007).

The Per Se Rule

- Current per se unlawful categories

Business practice	Key precedents
Horizontal price fixing	United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940); United States v. Trenton Potteries Co., 273 U.S. 392 (1927); Standard Oil Co. v. United States, 221 U.S. 1 (1911).
Bid rigging	United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 175 U.S. 211 (1899).
Maximum price fixing	Arizona v. Maricopa County Medical Society, 457 U.S. 332 (1982).
Fixing of one aspect of price	Catalano, Inc. v. Target Sales, Inc., 446 U.S. 643 (1980).
Horizontal market allocation (territories or customers) (Unit 8)	Palmer v. BRG of Ga., Inc., 498 U.S. 46 (1990) (per curiam); United States v. Topco Associates, Inc., 405 U.S. 596 (1972).
Certain tying arrangements* (Unit 22)	Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2 (1984); Northern Pac. R. Co. v. United States, 356 U.S. 1, 5 (1958).
Certain group boycotts* (Unit 8)	Klor's, Inc. v. Broadway–Hale Stores, Inc., 359 U.S. 207 (1959); Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co., 472 U.S. 284 (1985); Fashion Originators' Guild of America, Inc. v. FTC, 312 U.S. 457 (1941).

* Subject to preconditions before the per se rule applies.

The Per Se Rule

- Abrogated per se unlawful categories

Business practice	Per se	Abrogated
Minimum resale price maintenance (Unit 23)	Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911)	Leegin Creative Leather Prods, Inc. v. PSKS, Inc., 551 U.S. 877 (2007)
Maximum resale price maintenance (Unit 23)	Albrecht v. Herald Co., 390 U.S. 145 (1968)	State Oil Co. v. Kahn, 522 U.S. 2 (1997)
Nonprice vertical restraints (Unit 21)	United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967)	Continental T.V., Inc. v. GTE Sylvania, 433 U.S. 36 (1977)

  - Essentially, as freedom of economic choice declined as an antitrust goal and economic efficiency became more important, these vertical practices not longer qualified as having a necessarily anticompetitive effect

The Per Se Rule

- Creating new per se unlawful categories
  - Courts in general, and the Supreme Court in particular, have resisted many invitations to
    - create new categories of per se illegal categories of conduct, or
    - to apply the per se rule on an ad hoc basis
  - The last per se unlawful category created by the courts was nonprice vertical restraints in 1967, and that lasted for only ten years before the category was returned to rule of reason treatment

The Rule of Reason

- *The rule of reason*: Requires the plaintiff to prove though affirmative evidence that the likely effect of the restraint is to be anticompetitive
  - *Anticompetitive* means that the restraint creates an effect that the operative goals of antitrust law would prohibit
- Default rule
  - If the challenged conduct does not fall within a category of per se unlawful restraints, it will be assessed under the rule of reason
    - If restraint is not per se illegal but is obviously anticompetitive and lacking any apparent procompetitive justification, it may be assessed under the quick look (see below)

The *Chicago Board of Trade* Rule

- The classic formulation of the rule of reason

> But the legality of an agreement or regulation cannot be determined by so simple a test, as whether it restrains competition. Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates, and perhaps thereby promotes competition, or whether it is such as may suppress or even destroy competition. To determine that question, the court must ordinarily consider the facts peculiar to the business to which the restraint is applied, its condition before and after the restraint was imposed, the nature of the restraint, and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation, or the reverse, but because knowledge of intent may help the court to interpret facts and to predict consequences.[1]

[1] Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918).

The Rule of Reason

- Proving a rule of reason violation
  - *Central question*: Is the restraint contrary to the currently operative goals of antitrust law?
  - Today, this means does the restraint—
    - Increase prices
    - Decrease market output
    - Decrease the rate of technological innovation or product improvement

    compared to what would have been the case in the absence of the restraint (the "but for" world) without a procompetitive justification?
  - Procompetitive justifications
    - In modern terms, means a consumer welfare-increasing effect
    - Hard to find these in practice
      - Very few cases have been successfully defended on this ground
    - Usual example: Creation of a new product or service (or a significant product improvement) that
      - would not exist in the absence of the restraint, and
      - Increases aggregate consumer welfare over what would have existed in the absence of the restraint

The Rule of Reason

- Proving a rule of reason violation
  - General rules
    - Not necessary to prove an actual anticompetitive effect
      - A reasonably probable anticompetitive effect is sufficient
    - Not necessary to prove purpose
      - Although purpose (intent) may be probative of likely effect
    - Can use direct or circumstantial evidence to prove likely effect
  - Burden-shifting approach
    1. Plaintiff must show that the challenged restraint imposes a “gross” anticompetitive effect
    2. Burden shifts to the defendant to show that there is a consumer welfare-enhancing justification for the restraint
    3. Burden shifts back to plaintiff to show that the procompetitive effect could have been achieved through a less restrictive means

The Rule of Reason: Burden-Shifting Approach

1. Plaintiff must show that the challenged restraint imposes a “gross” anticompetitive effect
   a. *First requirement*: Requires restraint to be *directionally anticompetitive*
      - Must show that the restraint is does or is likely to—
        - Increases prices
        - Reduces output
        - Reduces the rate of technological innovation or product improvement
      - Proof may be indirect
        - For example, a refusal by dentists to prove copies of x-rays for services billed to an insurance company is probative of:
          - Increased prices paid by insureds, since their insurance companies will not be able to monitor and control medically unnecessary dental services
          - Increased prices charged by dentists, since dentists will be able to charge for medically unnecessary dental services (which should have a quality-adjusted price of zero)

The Rule of Reason: Burden-Shifting Approach

1. Plaintiff must show that the challenged restraint imposes a “gross” anticompetitive effect
    b. *Second requirement*: Requires proof that the restraint has (or perhaps is likely to have in the future) a *market-wide anticompetitive effect*
        - Usually proved by showing that the defendant(s) have market power in a properly defined “relevant market” in which the restraint operates
            - Requires full proof of the product and geographic dimensions of the relevant market[1]
            - Some circuits include proof of market power in a properly defined relevant market to be an essential element of a rule of reason prima facie case
            - Failure of proof on market definition and market power is probably the most frequently invoked reason when courts dismiss a rule of reason case
        - More recently, plaintiffs have sought to prove market-wide anticompetitive effect directly
            - Supported in principle by Supreme Court precedent
            - May involve *direct evidence* of market-wide anticompetitive effects (e.g., higher prices)
            - May involve *circumstantial evidence* of market-wide anticompetitive effects (e.g., a restraint on merchants in their ability to encourage customers to use different credit cards suggests higher credit card prices)

[1] We will examine this in detail in Unit 10: Market Definition.

The Rule of Reason: Burden-Shifting Approach

2. Burden shifts to the defendant to show that there is a consumer welfare-enhancing justification for the restraint
   - Usually interpreted to require that the restraint's *net* effective be procompetitive (consumer welfare-enhancing)
   - Hard to find in practice (much less prove)
     - Very few cases have been successfully defended on this ground
   - Usual example: Creation of a new product or service (or a significant product improvement) that
     - would not exist in the absence of the restraint, and
     - Increases aggregate consumer welfare over what would have existed in the absence of the restraint
   - Usual articulation of test suggests that defendant has both—
     - Burden of production, and
     - Burden of persuasion

   Query: Should the defendant have the burden of persuasion? That is, should the defendant only have to come forward with evidence that the restraint has a procompetitive justification, at which point the burden of persuasion returns to the plaintiff to prove that the net effect of the restraint decreases consumer welfare?

The Rule of Reason: Burden-Shifting Approach

3. Burden shifts back to plaintiff to show that the procompetitive effect could have been achieved through a less restrictive means
   - Echoes the overbreadth approach of the common law in assessing restraints of trade
   - Very rare to find a case that gets this far
     - The *O'Bannon/NCAA* "likeness" case is one of the rare exceptions
   - Queries
     - Should it matter that the restraint is the "least restrictive" if the net result of the challenged restraint is to increase consumer welfare over what it would have been in the absence of the restraint, even if some other less restrictive restraint would have increase consumer welfare even more?
     - If the rule requires only that the restraint increase consumer welfare but not maximize it, would that change in the result in *O'Bannon/NCAA*? (And if its does, would that be good or bad from a societal perspective?)

The Rule of Reason

- Concluding observation
  - Note the sensitivity of the rule of reason analysis to the “but for” world, that is, the counterfactual world in which the restraint does not exist.
    - The choice of the “but for” world affects all three steps in a rule of reason analysis[1]
    - *Query*: What is the proper “but for” world in *O’Bannon/NCAA*?
      - Absolute chaos, where every school adopts in own rule, which differ widely
      - Unilateral uniformity, where there is no NCAA-imposed rule but each school decides on its own that no compensation should be paid to student athletes for use of their likeness in TV and videogames
      - League uniformity, where separate (perhaps smaller) leagues form within the NCAA with each adopting its own compensation rule
      - Something else?

[1] Not surprisingly, proof of the but for world is also critical in the proof of damages, even in cases governed by the per se rule.

The Quick Look

- *The quick look*: A rebuttable presumption of unreasonableness based on the apparently inherently anticompetitive nature of the restraint[1]
  - Sometimes called the *truncated* or *abbreviated rule of reason* or *inherently suspect analysis*
  - Raises a rebuttable presumption of unreasonableness for restraints that
    - appear almost certain to be anticompetitive, but
    - do not trigger the conclusive presumption of unreasonableness of the per se rule because of a lack of judicial experience with them
  - Effectively shifts the burden of proof of the rule of reason
- Rationale
  - Conserves judicial and party resources by avoiding a full rule of reason analysis when the restraint and its effects strongly suggest that it is anticompetitive and hence unreasonable

[1] The key cases are California Dental Ass'n v. FTC, 526 U.S. 756 (1999); FTC v. Indiana Fed'n of Dentists, 476 U.S. 447 (1986);

The Quick Look

- Proving unreasonableness using the quick look
  - Two legs of a quick look analysis
    1. Showing the quick look should apply (as opposed to the default rule of reason)
    2. Showing that the restraint is unreasonable under the quick look

The Quick Look

- Proving unreasonableness using the quick look
  - Showing that the quick look applies
    - No fixed categories of business conduct to which the quick look applies
      - Application appears ad hoc (compare the application of the per se rule)
    - Plaintiff must show through direct evidence that the challenged restraint
      - has an obvious and substantial anticompetitive effect (usually on prices or output), and
      - (maybe) does not have any apparent procompetitive effects
        - Some courts indicate that the quick look is appropriate as long as it has an obvious and substantial anticompetitive effect even if there are some apparent procompetitive effects. This makes sense, since the purpose of the quick look is to decide the case on whether the defendant can show offsetting procompetitive effects.[1]
    - *California Dental* formulation
      - Quick look is appropriate only when "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets"[1]
    - *Dagher* formulation:
      - "To be sure, we have applied the quick look doctrine to business activities that are so plainly anticompetitive that courts need undertake only a cursory examination before imposing antitrust liability."[2]

[1] *See, e.g.*, Agnew v. National Collegiate Athletic Ass'n, 683 F.3d 328, 337 (7th Cir. 2012).
[2] California Dental Ass'n v. FTC, 526 U.S. 756, 770 (1999); *accord* FTC v. Actavis, Inc., 133 S. Ct. 2223, 2237 (2013).
[3] Texaco Inc. v. Dagher, 547 U.S. 1, 7 n.3 (2006).

The Quick Look

- Proving unreasonableness using the quick look
  - Showing that the quick look applies (con't)
    - Although not explicit in the cases, may also require that
      - The probability of an overinclusiveness error is small
      - The social loss of an overinclusiveness error is small[1]
    - A major advantage to plaintiffs of the quick look is that they do not have to prove a relevant market[2]

[1] In this context, an overinclusiveness ("Type 1") error is concluding that the restraint is unreasonable when in fact it is not.
[2] *See In re* Southeastern Milk Antitrust Litig., 739 F.3d 262, 275-76 (6th Cir. 2014); Agnew v. Nat'l Collegiate Athletic Ass'n, 683 F.3d 328, 337 (7th Cir. 2012).

Sources for Economic Charts

[1] Bureau of Economic Analysis, U.S. Dept. of Commerce, Gross Domestic Product: Percent Change from Preceding Period, Table 1.1.1.
[2] Bureau of Labor Statistics, U.S. Dept. of Labor, Nonfarm Business Labor Productivity (Output Per Hour), Series ID PRS85006092.
[3] Bureau of Labor Statistics, U.S. Dept. of Labor, Consumer Price Index: All Urban Consumers, Series CPI-U.
[4] Board of Governors of the Federal Reserve System, Selected Interest Rates (Daily), Series H.15.The bank prime rate hit its monthly maximum in August 1981 at 20.5%.
[5] Bureau of Labor Statistics, U.S. Dept. of Labor, Unemployment Rate (16 years and over), Series ID LNS14000000.
[6] U.S. Census Bureau, Table F-7. Type of Family (All Races) by Median and Mean Income (in 2011 CPI-U-RS adjusted dollars).