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Nonprice Vertical Restraints

CONTINENTAL T. V., INC., ET AL. *v.* GTE SYLVANIA INC.

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 76-15. Argued February 28, 1977—Decided June 23, 1977

In an attempt to improve its market position by attracting more aggressive and competent retailers, respondent manufacturer of television sets limited the number of retail franchises granted for any given area and required each franchisee to sell respondent's products only from the location or locations at which it was franchised. Petitioner Continental, one of respondent's franchised retailers, claimed that respondent had violated § 1 of the Sherman Act by entering into and enforcing franchise agreements that prohibited the sale of respondent's products other than from specified locations. The District Court rejected respondent's requested jury instruction that the location restriction was illegal only if it unreasonably restrained or suppressed competition. Instead, relying on *United States* v. *Arnold, Schwinn & Co.,* 388 U. S. 365, the District Court instructed the jury that it was a *per se* violation of § 1 if respondent entered into a contract, combination, or conspiracy with one or more of its retailers, pursuant to which it attempted to restrict the locations from which the retailers resold the merchandise they had purchased from respondent. The jury found that the location restriction violated § 1, and treble damages were assessed against respondent. Concluding that *Schwinn* was distinguishable, the Court of Appeals reversed, holding that respondent's location restriction had less potential for competitive harm than the restrictions invalidated in *Schwinn* and thus should be judged under the "rule of reason." *Held:*

1. The statement of the *per se* rule in *Schwinn* is broad enough to cover the location restriction used by respondent. And the retail-customer restriction in *Schwinn* is functionally indistinguishable from the location restriction here, the restrictions in both cases limiting the retailer's freedom to dispose of the purchased products and reducing, but not eliminating, intrabrand competition. Pp. 42-47.

2. The justification and standard for the creation of *per se* rules was stated in *Northern Pac. R. Co.* v. *United States,* 356 U. S. 1, 5: "There are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively

presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use." Under this standard, there is no justification for the distinction drawn in *Schwinn* between restrictions imposed in sale and nonsale transactions. Similarly, the facts of this case do not present a situation justifying a *per se* rule. Accordingly, the *per se* rule stated in *Schwinn* is overruled, and the location restriction used by respondent should be judged under the traditional rule-of-reason standard. Pp. 47–59.

537 F. 2d 980, affirmed.

Powell, J., delivered the opinion of the Court, in which Burger, C. J., and Stewart, Blackmun, and Stevens, JJ., joined. White, J., filed an opinion concurring in the judgment, *post*, p. 59. Brennan, J., filed a dissenting statement, in which Marshall, J., joined, *post*, p. 71. Rehnquist, J., took no part in the consideration or decision of the case.

Glenn E. Miller argued the cause for petitioners. With him on the briefs were *Lawrence A. Sullivan* and *Jesse Choper.*

M. Laurence Popofsky argued the cause for respondent. With him on the brief were *Richard L. Goff* and *Stephen V. Bomse.**

Mr. Justice Powell delivered the opinion of the Court.

Franchise agreements between manufacturers and retailers frequently include provisions barring the retailers from selling franchised products from locations other than those specified in the agreements. This case presents important questions concerning the appropriate antitrust analysis of these restrictions under § 1 of the Sherman Act, 26 Stat. 209, as amended, 15 U. S. C. § 1, and the Court's decision in *United States* v. *Arnold, Schwinn & Co.*, 388 U. S. 365 (1967).

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*Briefs of *amici curiae* urging affirmance were filed by *Lawrence T. Zimmerman* for the Associated Equipment Distributors; by *Lloyd N. Cutler, James S. Campbell, William T. Lake,* and *Donald F. Turner* for the Motor Vehicle Manufacturers Assn.; and by *Philip F. Zeidman* and *John A. Dienelt* for the International Franchise Assn.

I

Respondent GTE Sylvania Inc. (Sylvania) manufactures and sells television sets through its Home Entertainment Products Division. Prior to 1962, like most other television manufacturers, Sylvania sold its televisions to independent or company-owned distributors who in turn resold to a large and diverse group of retailers. Prompted by a decline in its market share to a relatively insignificant 1% to 2% of national television sales,[1] Sylvania conducted an intensive reassessment of its marketing strategy, and in 1962 adopted the franchise plan challenged here. Sylvania phased out its wholesale distributors and began to sell its televisions directly to a smaller and more select group of franchised retailers. An acknowledged purpose of the change was to decrease the number of competing Sylvania retailers in the hope of attracting the more aggressive and competent retailers thought necessary to the improvement of the company's market position.[2] To this end, Sylvania limited the number of franchises granted for any given area and required each franchisee to sell his Sylvania products only from the location or locations at which he was franchised.[3] A franchise did not constitute an exclusive territory, and Sylvania retained sole discretion to increase the number of retailers in an area in light of the success or failure of existing retailers in developing their market. The revised marketing strategy appears to have been successful during the period at issue here, for by 1965 Sylvania's share of national television sales had increased to approximately 5%, and the

[1] RCA at that time was the dominant firm with as much as 60% to 70% of national television sales in an industry with more than 100 manufacturers.

[2] The number of retailers selling Sylvania products declined significantly as a result of the change, but in 1965 there were at least two franchised Sylvania retailers in each metropolitan center of more than 100,000 population.

[3] Sylvania imposed no restrictions on the right of the franchisee to sell the products of competing manufacturers.

company ranked as the Nation's eighth largest manufacturer of color television sets.

This suit is the result of the rupture of a franchiser-franchisee relationship that had previously prospered under the revised Sylvania plan. Dissatisfied with its sales in the city of San Francisco,[4] Sylvania decided in the spring of 1965 to franchise Young Brothers, an established San Francisco retailer of televisions, as an additional San Francisco retailer. The proposed location of the new franchise was approximately a mile from a retail outlet operated by petitioner Continental T. V., Inc. (Continental), one of the most successful Sylvania franchisees.[5] Continental protested that the location of the new franchise violated Sylvania's marketing policy, but Sylvania persisted in its plans. Continental then canceled a large Sylvania order and placed a large order with Phillips, one of Sylvania's competitors.

During this same period, Continental expressed a desire to open a store in Sacramento, Cal., a desire Sylvania attributed at least in part to Continental's displeasure over the Young Brothers decision. Sylvania believed that the Sacramento market was adequately served by the existing Sylvania retailers and denied the request.[6] In the face of this denial, Continental advised Sylvania in early September 1965, that it was in the process of moving Sylvania merchandise from its San Jose, Cal., warehouse to a new retail location that it had leased in Sacramento. Two weeks later, allegedly for unrelated reasons, Sylvania's credit department reduced Conti-

[4] Sylvania's market share in San Francisco was approximately 2.5%—half its national and northern California average.

[5] There are in fact four corporate petitioners: Continental T. V., Inc., A & G Sales, Sylpac, Inc., and S. A. M. Industries, Inc. All are owned in large part by the same individual, and all conducted business under the trade style of "Continental T. V." We adopt the convention used by the court below of referring to petitioners collectively as "Continental."

[6] Sylvania had achieved exceptional results in Sacramento, where its market share exceeded 15% in 1965.

nental's credit line from $300,000 to $50,000.[7] In response to the reduction in credit and the generally deteriorating relations with Sylvania, Continental withheld all payments owed to John P. Maguire & Co., Inc. (Maguire), the finance company that handled the credit arrangements between Sylvania and its retailers. Shortly thereafter, Sylvania terminated Continental's franchises, and Maguire filed this diversity action in the United States District Court for the Northern District of California seeking recovery of money owed and of secured merchandise held by Continental.

The antitrust issues before us originated in cross-claims brought by Continental against Sylvania and Maguire. Most important for our purposes was the claim that Sylvania had violated § 1 of the Sherman Act by entering into and enforcing franchise agreements that prohibited the sale of Sylvania products other than from specified locations.[8] At the close of evidence in the jury trial of Continental's claims, Sylvania requested the District Court to instruct the jury that its location restriction was illegal only if it unreasonably restrained or suppressed competition. App. 5–6, 9–15. Relying on this Court's decision in *United States* v. *Arnold, Schwinn & Co., supra,* the District Court rejected the proffered instruction in favor of the following one:

> "Therefore, if you find by a preponderance of the evidence that Sylvania entered into a contract, combination or conspiracy with one or more of its dealers pursuant to which Sylvania exercised dominion or control over the

[7] In its findings of fact made in conjunction with Continental's plea for injunctive relief, the District Court rejected Sylvania's claim that its actions were prompted by independent concerns over Continental's credit. The jury's verdict is ambiguous on this point. In any event, we do not consider it relevant to the issue before us.

[8] Although Sylvania contended in the District Court that its policy was unilaterally enforced, it now concedes that its location restriction involved understandings or agreements with the retailers.

products sold to the dealer, after having parted with title and risk to the products, you must find any effort thereafter to restrict outlets or store locations from which its dealers resold the merchandise which they had purchased from Sylvania to be a violation of Section 1 of the Sherman Act, regardless of the reasonableness of the location restrictions." App. 492.

In answers to special interrogatories, the jury found that Sylvania had engaged "in a contract, combination or conspiracy in restraint of trade in violation of the antitrust laws with respect to location restrictions alone," and assessed Continental's damages at $591,505, which was trebled pursuant to 15 U. S. C. § 15 to produce an award of $1,774,515. App. 498, 501.[9]

On appeal, the Court of Appeals for the Ninth Circuit, sitting en banc, reversed by a divided vote. 537 F. 2d 980 (1976). The court acknowledged that there is language in *Schwinn* that could be read to support the District Court's instruction but concluded that *Schwinn* was distinguishable on several grounds. Contrasting the nature of the restrictions, their competitive impact, and the market shares of the franchisers in the two cases, the court concluded that Sylvania's location restriction had less potential for competitive harm than the restrictions invalidated in *Schwinn* and thus should be judged under the "rule of reason" rather than the *per se* rule stated in *Schwinn*. The court found support for its

[9] The jury also found that Maguire had not conspired with Sylvania with respect to this violation. Other claims made by Continental were either rejected by the jury or withdrawn by Continental. Most important was the jury's rejection of the allegation that the location restriction was part of a larger scheme to fix prices. A pendent claim that Sylvania and Maguire had willfully and maliciously caused injury to Continental's business in violation of California law also was rejected by the jury, and a pendent breach-of-contract claim was withdrawn by Continental during the course of the proceedings. The parties eventually stipulated to a judgment for Maguire on its claim against Continental.

position in the policies of the Sherman Act and in the decisions of other federal courts involving nonprice vertical restrictions.[10]

We granted Continental's petition for certiorari to resolve this important question of antitrust law. 429 U. S. 893 (1976).[11]

II

A

We turn first to Continental's contention that Sylvania's restriction on retail locations is a *per se* violation of § 1 of the Sherman Act as interpreted in *Schwinn*. The restrictions at issue in *Schwinn* were part of a three-tier distribution system comprising, in addition to Arnold, Schwinn & Co. (Schwinn), 22 intermediate distributors and a network of franchised retailers. Each distributor had a defined geographic area in which it had the exclusive right to supply franchised retailers. Sales to the public were made only through franchised retailers, who were authorized to sell Schwinn bicycles only from specified locations. In support of this limitation, Schwinn prohibited both distributors and retailers from selling Schwinn bicycles to nonfranchised retailers. At the retail level, therefore, Schwinn was able to control the number of retailers of

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[10] There were two major dissenting opinions. Judge Kilkenny argued that the present case is indistinguishable from *Schwinn* and that the jury had been correctly instructed. Agreeing with Judge Kilkenny's interpretation of *Schwinn*, Judge Browning stated that he found the interpretation responsive to and justified by the need to protect " 'individual traders from unnecessary restrictions upon their freedom of action.' " 537 F. 2d, at 1021. See n. 21, *infra*.

[11] This Court has never given plenary consideration to the question of the proper antitrust analysis of location restrictions. Before *Schwinn* such restrictions had been sustained in *Boro Hall Corp.* v. *General Motors Corp.*, 124 F. 2d 822 (CA2 1942). Since the decision in *Schwinn*, location restrictions have been sustained by three Courts of Appeals, including the decision below. *Salco Corp.* v. *General Motors Corp.*, 517 F. 2d 567 (CA10 1975); *Kaiser* v. *General Motors Corp.*, 396 F. Supp. 33 (ED Pa. 1975), affirmance order, 530 F. 2d 964 (CA3 1976).

its bicycles in any given area according to its view of the needs of that market.

As of 1967 approximately 75% of Schwinn's total sales were made under the "Schwinn Plan." Acting essentially as a manufacturer's representative or sales agent, a distributor participating in this plan forwarded orders from retailers to the factory. Schwinn then shipped the ordered bicycles directly to the retailer, billed the retailer, bore the credit risk, and paid the distributor a commission on the sale. Under the Schwinn Plan, the distributor never had title to or possession of the bicycles. The remainder of the bicycles moved to the retailers through the hands of the distributors. For the most part, the distributors functioned as traditional wholesalers with respect to these sales, stocking an inventory of bicycles owned by them to supply retailers with emergency and "fill-in" requirements. A smaller part of the bicycles that were physically distributed by the distributors were covered by consignment and agency arrangements that had been developed to deal with particular problems of certain distributors. Distributors acquired title only to those bicycles that they purchased as wholesalers; retailers, of course, acquired title to all of the bicycles ordered by them.

In the District Court, the United States charged a continuing conspiracy by Schwinn and other alleged co-conspirators to fix prices, allocate exclusive territories to distributors, and confine Schwinn bicycles to franchised retailers. Relying on *United States* v. *Bausch & Lomb Co.,* 321 U. S. 707 (1944), the Government argued that the nonprice restrictions were *per se* illegal as part of a scheme for fixing the retail prices of Schwinn bicycles. The District Court rejected the price-fixing allegation because of a failure of proof and held that Schwinn's limitation of retail bicycle sales to franchised retailers was permissible under § 1. The court found a § 1 violation, however, in "a conspiracy to divide certain borderline or overlapping counties in the territories served by four Midwestern cycle distributors." 237 F. Supp. 323, 342 (ND Ill. 1965). The court described the violation as a "division of territory by agreement between the distributors . . . horizontal in nature," and held that Schwinn's participation did not change that basic characteristic. *Ibid.* The District Court limited its injunction to apply only to the territorial restrictions on the resale of bicycles purchased by the distributors in their roles as wholesalers. *Ibid.*

Schwinn came to this Court on appeal by the United States from the District Court's decision. Abandoning its *per se* theories, the Government argued that Schwinn's prohibition against distributors' and retailers' selling Schwinn bicycles to nonfranchised retailers was unreasonable under § 1 and that the District Court's injunction against exclusive distributor territories should extend to all such restrictions regardless of the form of the transaction. The Government did not challenge the District Court's decision on price fixing, and Schwinn did not challenge the decision on exclusive distributor territories.

The Court acknowledged the Government's abandonment of its *per se* theories and stated that the resolution of the case would require an examination of "the specifics of the challenged practices and their impact upon the marketplace in order to make a judgment as to whether the restraint is or is not 'reasonable' in the special sense in which § 1 of the Sherman Act must be read for purposes of this type of inquiry." 388 U. S., at 374. Despite this description of its task, the Court proceeded to articulate the following "bright line" *per se* rule of illegality for vertical restrictions: "Under the Sherman Act, it is unreasonable without more for a manufacturer to seek to restrict and confine areas or persons with whom an article may be traded after the manufacturer has parted with dominion over it." *Id.*, at 379. But the Court expressly stated that the rule of reason governs when "the manufacturer retains title, dominion, and risk with respect to the product and the position and function of the dealer in question are, in fact, indistinguishable from those of an agent or salesman of the manufacturer." *Id.,* at 380.

Application of these principles to the facts of *Schwinn* produced sharply contrasting results depending upon the role played by the distributor in the distribution system. With respect to that portion of Schwinn's sales for which the distributors acted as ordinary wholesalers, buying and reselling Schwinn bicycles, the Court held that the territorial and customer restrictions challenged by the Government were *per se* illegal. But, with respect to that larger portion of Schwinn's sales in which the distributors functioned under the Schwinn Plan and under the less common consignment and agency arrangements, the Court held that the same restrictions should be judged under the rule of reason. The only retail restriction challenged by the Government prevented franchised retailers from supplying nonfranchised retailers. *Id.,* at 377. The Court apparently perceived no material distinction between the restrictions on distributors and retailers, for it held:

> "The principle is, of course, equally applicable to sales to retailers, and the decree should similarly enjoin the making of any sales to retailers upon any condition, agreement or understanding limiting the retailer's freedom as to where and to whom it will resell the products." *Id.,* at 378.

Applying the rule of reason to the restrictions that were not imposed in conjunction with the sale of bicycles, the Court had little difficulty finding them all reasonable in light of the competitive situation in "the product market as a whole." *Id.,* at 382.

B

In the present case, it is undisputed that title to the television sets passed from Sylvania to Continental. Thus, the *Schwinn per se* rule applies unless Sylvania's restriction on locations falls outside *Schwinn*'s prohibition against a manufacturer's attempting to restrict a "retailer's freedom as to where and to whom it will resell the products." *Id.*, at 378. As the Court of Appeals conceded, the language of *Schwinn* is clearly broad enough to apply to the present case. Unlike the Court of Appeals, however, we are unable to find a principled basis for distinguishing *Schwinn* from the case now before us.

Both Schwinn and Sylvania sought to reduce but not to eliminate competition among their respective retailers through the adoption of a franchise system. Although it was not one of the issues addressed by the District Court or presented on appeal by the Government, the Schwinn franchise plan included a location restriction similar to the one challenged here. These restrictions allowed Schwinn and Sylvania to regulate the amount of competition among their retailers by preventing a franchisee from selling franchised products from outlets other than the one covered by the franchise agreement. To exactly the same end, the Schwinn franchise plan included a companion restriction, apparently not found in the Sylvania plan, that prohibited franchised retailers from selling Schwinn products to nonfranchised retailers. In *Schwinn* the Court expressly held that this restriction was impermissible under the broad principle stated there. In intent and competitive impact, the retail-customer restriction in *Schwinn* is indistinguishable from the location restriction in the present case. In both cases the restrictions limited the freedom of the retailer to dispose of the purchased products as he desired. The fact that one restriction was addressed to territory and the other to customers is irrelevant to functional antitrust analysis and, indeed, to the language and broad thrust of the opinion in *Schwinn*.[12] As Mr. Chief Justice Hughes stated in

[12] The distinctions drawn by the Court of Appeals and endorsed in MR. JUSTICE WHITE's separate opinion have no basis in *Schwinn*. The intrabrand competitive impact of the restrictions at issue in *Schwinn*

Appalachian Coals, Inc. v. *United States,* 288 U. S. 344, 360, 377 (1933): "Realities must dominate the judgment. . . . The Anti-Trust Act aims at substance."

III

Sylvania argues that if *Schwinn* cannot be distinguished, it should be reconsidered. Although *Schwinn* is supported by the principle of *stare decisis, Illinois Brick Co.* v. *Illinois,* 431 U. S. 720, 736 (1977), we are convinced that the need for clarification of the law in this area justifies reconsideration. *Schwinn* itself was an abrupt and largely unexplained departure from *White Motor Co.* v. *United States,* 372 U. S. 253 (1963), where only four years earlier the Court had refused to endorse a *per se* rule for vertical restrictions. Since its announcement, *Schwinn* has been the subject of continuing controversy and confusion, both in the scholarly journals and in the federal courts. The great weight of scholarly opinion

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ranged from complete elimination to mere reduction; yet, the Court did not even hint at any distinction on this ground. Similarly, there is no suggestion that the *per se* rule was applied because of Schwinn's prominent position in its industry. That position was the same whether the bicycles were sold or consigned, but the Court's analysis was quite different. In light of MR. JUSTICE WHITE's emphasis on the "superior consumer acceptance" enjoyed by the Schwinn brand name, *post,* at 63, we note that the Court rejected precisely that premise in *Schwinn.* Applying the rule of reason to the restrictions imposed in nonsale transactions, the Court stressed that there was "no showing that [competitive bicycles were] not in all respects reasonably interchangeable as articles of competitive commerce with the Schwinn product" and that it did "not regard Schwinn's claim of product excellence as establishing the contrary." 388 U. S., at 381, and n. 7. Although *Schwinn* did hint at preferential treatment for new entrants and failing firms, the District Court below did not even submit Sylvania's claim that it was failing to the jury. Accordingly, MR. JUSTICE WHITE's position appears to reflect an extension of *Schwinn* in this regard. Having crossed the "failing firm" line, MR. JUSTICE WHITE attempts neither to draw a new one nor to explain why one should be drawn at all.

has been critical of the decision,[13] and a number of the federal courts confronted with analogous vertical restrictions have sought to limit its reach.[14] In our view, the experience of the

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[13] A former Assistant Attorney General in charge of the Antitrust Division has described *Schwinn* as "an exercise in barren formalism" that is "artificial and unresponsive to the competitive needs of the real world." Baker, Vertical Restraints in Times of Change: From *White* to *Schwinn* to Where?, 44 Antitrust L. J. 537 (1975). See, *e. g.,* Handler, The Twentieth Annual Antitrust Review—1967, 53 Va. L. Rev. 1667 (1967); McLaren, Territorial and Customer Restrictions, Consignments, Suggested Retail Prices and Refusals to Deal, 37 Antitrust L. J. 137 (1968); Pollock, Alternative Distribution Methods After *Schwinn,* 63 Nw. U. L. Rev. 595 (1968); Posner, Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions, 75 Colum. L. Rev. 282 (1975); Robinson, Recent Antitrust Developments: 1974, 75 Colum. L. Rev. 243 (1975); Note, Vertical Territorial and Customer Restrictions in the Franchising Industry, 10 Colum. J. L. & Soc. Prob. 497 (1974); Note, Territorial and Customer Restrictions: A Trend Toward a Broader Rule of Reason?, 40 Geo. Wash. L. Rev. 123 (1971); Note, Territorial Restrictions and Per Se Rules—A Re-evaluation of the *Schwinn* and *Sealy* Doctrines, 70 Mich. L. Rev. 616 (1972). But see Louis, Vertical Distributional Restraints Under *Schwinn* and *Sylvania:* An Argument for the Continuing Use of a Partial Per Se Approach, 75 Mich. L. Rev. 275 (1976); Zimmerman, Distribution Restrictions After *Sealy* and *Schwinn,* 12 Antitrust Bull. 1181 (1967). For a more inclusive list of articles and comments, see 537 F. 2d, at 988 n. 13.

[14] Indeed, as one commentator has observed, many courts "have struggled to distinguish or limit *Schwinn* in ways that are a tribute to judicial ingenuity." Robinson, *supra,* n. 13, at 272. Thus, the statement in *Schwinn* that post-sale vertical restrictions as to customers or territories are "unreasonable without more," 388 U. S., at 379, has been interpreted to allow an exception to the *per se* rule where the manufacturer proves "more" by showing that the restraints will protect consumers against injury and the manufacturer against product liability claims. See, *e. g., Tripoli Co.* v. *Wella Corp.,* 425 F. 2d 932, 936–938 (CA3 1970) (en banc). Similarly, the statement that Schwinn's enforcement of its restrictions had been " 'firm and resolute,' " 388 U. S., at 372, has been relied upon to distinguish cases lacking that element. See, *e. g., Janel Sales Corp.* v. *Lanvin Parfums, Inc.,* 396 F. 2d 398, 406 (CA2 1968). Other factual distinctions have been drawn to justify upholding territorial restrictions

past 10 years should be brought to bear on this subject of considerable commercial importance.

The traditional framework of analysis under § 1 of the Sherman Act is familiar and does not require extended discussion. Section 1 prohibits "[e]very contract, combination . . . , or conspiracy, in restraint of trade or commerce." Since the early years of this century a judicial gloss on this statutory language has established the "rule of reason" as the prevailing standard of analysis. *Standard Oil Co.* v. *United States,* 221 U. S. 1 (1911). Under this rule, the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition.[15] *Per se* rules of il-

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that would seem to fall within the scope of the *Schwinn per se* rule. See, *e. g., Carter-Wallace, Inc.* v. *United States,* 196 Ct. Cl. 35, 44–46, 449 F. 2d 1374, 1379–1380 (1971) (*per se* rule inapplicable when purchaser can avoid restraints by electing to buy product at higher price); *Colorado Pump & Supply Co.* v. *Febco, Inc.,* 472 F. 2d 637 (CA10 1973) (apparent territorial restriction characterized as primary responsibility clause). One Court of Appeals has expressly urged us to consider the need in this area for greater flexibility. *Adolph Coors Co.* v. *FTC,* 497 F. 2d 1178, 1187 (CA10 1974). The decision in *Schwinn* and the developments in the lower courts have been exhaustively surveyed in ABA Antitrust Section, Monograph No. 2, Vertical Restrictions Limiting Intrabrand Competition (1977) (ABA Monograph No. 2).

[15] One of the most frequently cited statements of the rule of reason is that of Mr. Justice Brandeis in *Chicago Bd. of Trade* v. *United States,* 246 U. S. 231, 238 (1918):

"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 legality are appropriate only when they relate to conduct that is manifestly anticompetitive. As the Court explained in *Northern Pac. R. Co.* v. *United States,* 356 U. S. 1, 5 (1958), "there are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use." [16]

In essence, the issue before us is whether *Schwinn*'s *per se* rule can be justified under the demanding standards of *Northern Pac. R. Co.* The Court's refusal to endorse a *per se* rule in *White Motor Co.* was based on its uncertainty as to whether vertical restrictions satisfied those standards. Addressing this question for the first time, the Court stated:

> "We need to know more than we do about the actual impact of these arrangements on competition to decide whether they have such a 'pernicious effect on competition and lack . . . any redeeming virtue' (*Northern Pac. R. Co.* v. *United States, supra,* p. 5) and therefore should

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knowledge of intent may help the court to interpret facts and to predict consequences."

[16] *Per se* rules thus require the Court to make broad generalizations about the social utility of particular commercial practices. The probability that anticompetitive consequences will result from a practice and the severity of those consequences must be balanced against its procompetitive consequences. Cases that do not fit the generalization may arise, but a *per se* rule reflects the judgment that such cases are not sufficiently common or important to justify the time and expense necessary to identify them. Once established, *per se* rules tend to provide guidance to the business community and to minimize the burdens on litigants and the judicial system of the more complex rule-of-reason trials, see *Northern Pac. R. Co.* v. *United States,* 356 U. S., at 5; *United States* v. *Topco Associates, Inc.,* 405 U. S. 596, 609–610 (1972), but those advantages are not sufficient in themselves to justify the creation of *per se* rules. If it were otherwise, all of antitrust law would be reduced to *per se* rules, thus introducing an unintended and undesirable rigidity in the law.

> be classified as *per se* violations of the Sherman Act." 372 U. S., at 263.

Only four years later the Court in *Schwinn* announced its sweeping *per se* rule without even a reference to *Northern Pac. R. Co.* and with no explanation of its sudden change in position.[17] We turn now to consider *Schwinn* in light of *Northern Pac. R. Co.*

The market impact of vertical restrictions[18] is complex because of their potential for a simultaneous reduction of intrabrand competition and stimulation of interbrand com-

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[17] After *White Motor Co.,* the Courts of Appeals continued to evaluate territorial restrictions according to the rule of reason. *Sandura Co.* v. *FTC,* 339 F. 2d 847 (CA6 1964); *Snap-On Tools Corp.* v. *FTC,* 321 F. 2d 825 (CA7 1963). For an exposition of the history of the antitrust analysis of vertical restrictions before *Schwinn,* see ABA Monograph No. 2, pp. 6–8.

[18] As in *Schwinn,* we are concerned here only with nonprice vertical restrictions. The *per se* illegality of price restrictions has been established firmly for many years and involves significantly different questions of analysis and policy. As MR. JUSTICE WHITE notes, *post,* at 69–70, some commentators have argued that the manufacturer's motivation for imposing vertical price restrictions may be the same as for nonprice restrictions. There are, however, significant differences that could easily justify different treatment. In his concurring opinion in *White Motor Co.* v. *United States,* MR. JUSTICE BRENNAN noted that, unlike nonprice restrictions, "[r]esale price maintenance is not only designed to, but almost invariably does in fact, reduce price competition not only *among* sellers of the affected product, but quite as much *between* that product and competing brands." 372 U. S., at 268. Professor Posner also recognized that "industry-wide resale price maintenance might facilitate cartelizing." Posner, *supra,* n. 13, at 294 (footnote omitted); see R. Posner, Antitrust: Cases, Economic Notes and Other Materials 134 (1974); E. Gellhorn, Antitrust Law and Economics 252 (1976); Note, 10 Colum. J. L. & Soc. Prob., *supra,* n. 13, at 498 n. 12. Furthermore, Congress recently has expressed its approval of a *per se* analysis of vertical price restrictions by repealing those provisions of the Miller-Tydings and McGuire Acts allowing fair-trade pricing at the option of the individual States. Consumer Goods Pricing Act of 1975, 89 Stat. 801, amending 15 U. S. C. §§ 1, 45 (a). No similar expression of congressional intent exists for nonprice restrictions.

petition.[19] Significantly, the Court in *Schwinn* did not distinguish among the challenged restrictions on the basis of their individual potential for intrabrand harm or interbrand benefit. Restrictions that completely eliminated intrabrand competition among Schwinn distributors were analyzed no differently from those that merely moderated intrabrand competition among retailers. The pivotal factor was the passage of title: All restrictions were held to be *per se* illegal where title had passed, and all were evaluated and sustained under the rule of reason where it had not. The location restriction at issue here would be subject to the same pattern of analysis under *Schwinn*.

It appears that this distinction between sale and nonsale transactions resulted from the Court's effort to accommodate the perceived intrabrand harm and interbrand benefit of vertical restrictions. The *per se* rule for sale transactions reflected the view that vertical restrictions are "so obviously destructive" of intrabrand competition[20] that their use would "open the door to exclusivity of outlets and limitation of ter-

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[19] Interbrand competition is the competition among the manufacturers of the same generic product—television sets in this case—and is the primary concern of antitrust law. The extreme example of a deficiency of interbrand competition is monopoly, where there is only one manufacturer. In contrast, intrabrand competition is the competition between the distributors—wholesale or retail—of the product of a particular manufacturer.

The degree of intrabrand competition is wholly independent of the level of interbrand competition confronting the manufacturer. Thus, there may be fierce intrabrand competition among the distributors of a product produced by a monopolist and no intrabrand competition among the distributors of a product produced by a firm in a highly competitive industry. But when interbrand competition exists, as it does among television manufacturers, it provides a significant check on the exploitation of intrabrand market power because of the ability of consumers to substitute a different brand of the same product.

[20] The Court did not specifically refer to intrabrand competition, but this meaning is clear from the context.

ritory further than prudence permits." 388 U. S., at 379–380.[21] Conversely, the continued adherence to the traditional rule of reason for nonsale transactions reflected the view that the restrictions have too great a potential for the promotion of interbrand competition to justify complete prohibition.[22]

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[21] The Court also stated that to impose vertical restrictions in sale transactions would "violate the ancient rule against restraints on alienation." 388 U. S., at 380. This isolated reference has provoked sharp criticism from virtually all of the commentators on the decision, most of whom have regarded the Court's apparent reliance on the "ancient rule" as both a misreading of legal history and a perversion of antitrust analysis. See, *e. g.,* Handler, *supra,* n. 13, at 1684–1686; Posner, *supra,* n. 13, at 295–296; Robinson, *supra,* n. 13, at 270–271; but see Louis, *supra,* n. 13, at 276 n. 6. We quite agree with MR. JUSTICE STEWART's dissenting comment in *Schwinn* that "the state of the common law 400 or even 100 years ago is irrelevant to the issue before us: the effect of the antitrust laws upon vertical distributional restraints in the American economy today." 388 U. S., at 392.

We are similarly unable to accept Judge Browning's interpretation of *Schwinn.* In his dissent below he argued that the decision reflects the view that the Sherman Act was intended to prohibit restrictions on the autonomy of independent businessmen even though they have no impact on "price, quality, and quantity of goods and services," 537 F. 2d, at 1019. This view is certainly not explicit in *Schwinn,* which purports to be based on an examination of the "impact [of the restrictions] upon the marketplace." 388 U. S., at 374. Competitive economies have social and political as well as economic advantages, see *e. g., Northern Pac. R. Co.* v. *United States,* 356 U. S., at 4, but an antitrust policy divorced from market considerations would lack any objective benchmarks. As Mr. Justice Brandeis reminded us: "Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence." *Chicago Bd. of Trade* v. *United States,* 246 U. S., at 238. Although MR. JUSTICE WHITE's opinion endorses Judge Browning's interpretation, *post,* at 66–68, it purports to distinguish *Schwinn* on grounds inconsistent with that interpretation, *post,* at 71.

[22] In that regard, the Court specifically stated that a more complete prohibition "might severely hamper smaller enterprises resorting to reasonable methods of meeting the competition of giants and of merchandising through independent dealers." 388 U. S., at 380. The Court also broadly hinted that it would recognize additional exceptions to the *per se*

The Court's opinion provides no analytical support for these contrasting positions. Nor is there even an assertion in the opinion that the competitive impact of vertical restrictions is significantly affected by the form of the transaction. Nonsale transactions appear to be excluded from the *per se* rule, not because of a greater danger of intrabrand harm or a greater promise of interbrand benefit, but rather because of the Court's unexplained belief that a complete *per se* prohibition would be too "inflexibl[e]." *Id.,* at 379.

Vertical restrictions reduce intrabrand competition by limiting the number of sellers of a particular product competing for the business of a given group of buyers. Location restrictions have this effect because of practical constraints on the effective marketing area of retail outlets. Although intrabrand competition may be reduced, the ability of retailers to exploit the resulting market may be limited both by the ability of consumers to travel to other franchised locations and, perhaps more importantly, to purchase the competing products of other manufacturers. None of these key variables, however, is affected by the form of the transaction by which a manufacturer conveys his products to the retailers.

Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products. These "redeeming virtues" are implicit in every decision sustaining vertical restrictions under the rule of reason. Economists have identified a num-

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rule for new entrants in an industry and for failing firms, both of which were mentioned in *White Motor* as candidates for such exceptions. 388 U. S., at 374. The Court might have limited the exceptions to the *per se* rule to these situations, which present the strongest arguments for the sacrifice of intrabrand competition for interbrand competition. Significantly, it chose instead to create the more extensive exception for nonsale transactions which is available to all businesses, regardless of their size, financial health, or market share. This broader exception demonstrates even more clearly the Court's awareness of the "redeeming virtues" of vertical restrictions.

ber of ways in which manufacturers can use such restrictions to compete more effectively against other manufacturers. See, *e. g.*, Preston, Restrictive Distribution Arrangements: Economic Analysis and Public Policy Standards, 30 Law & Contemp. Prob. 506, 511 (1965).[23] For example, new manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer. Established manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products. Service and repair are vital for many products, such as automobiles and major household appliances. The availability and quality of such services affect a manufacturer's goodwill and the competitiveness of his product. Because of market imperfections such as the so-called "free rider" effect, these services might not be provided by retailers in a purely competitive situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did. Posner, *supra,* n. 13, at 285; cf. P. Samuelson, Economics 506–507 (10th ed. 1976).

[23] Marketing efficiency is not the only legitimate reason for a manufacturer's desire to exert control over the manner in which his products are sold and serviced. As a result of statutory and common-law developments, society increasingly demands that manufacturers assume direct responsibility for the safety and quality of their products. For example, at the federal level, apart from more specialized requirements, manufacturers of consumer products have safety responsibilities under the Consumer Product Safety Act, 15 U. S. C. § 2051 *et seq.* (1970 ed., Supp. V), and obligations for warranties under the Consumer Product Warranties Act, 15 U. S. C. § 2301 *et seq.* (1970 ed., Supp. V). Similar obligations are imposed by state law. See, *e. g.*, Cal. Civ. Code Ann. § 1790 *et seq.* (West 1973). The legitimacy of these concerns has been recognized in cases involving vertical restrictions. See, *e. g., Tripoli Co.* v. *Wella Corp.*, 425 F. 2d 932 (CA3 1970).

Economists also have argued that manufacturers have an economic interest in maintaining as much intrabrand competition as is consistent with the efficient distribution of their products. Bork, The Rule of Reason and the Per Se Concept: Price Fixing and Market Division [II], 75 Yale L. J. 373, 403 (1966); Posner, *supra,* n. 13, at 283, 287–288.[24] Although the view that the manufacturer's interest necessarily corresponds with that of the public is not universally shared, even the leading critic of vertical restrictions concedes that *Schwinn's* distinction between sale and nonsale transactions is essentially unrelated to any relevant economic impact. Comanor, Vertical Territorial and Customer Restrictions: White Motor and Its Aftermath, 81 Harv. L. Rev. 1419, 1422 (1968).[25] Indeed, to the extent that the form of the transaction is related to interbrand benefits, the Court's distinction is inconsistent with its articulated concern for the ability of smaller firms to compete effectively with larger ones. Capital requirements and administrative expenses may prevent smaller firms from using the exception for nonsale transactions. See, *e. g.,* Baker, *supra,* n. 13, at 538; Phillips, *Schwinn* Rules and the "New Economics" of Vertical

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[24] "Generally a manufacturer would prefer the lowest retail price possible, once its price to dealers has been set, because a lower retail price means increased sales and higher manufacturer revenues." Note, 88 Harv. L. Rev. 636, 641 (1975). In this context, a manufacturer is likely to view the difference between the price at which it sells to its retailers and their price to the consumer as its "cost of distribution," which it would prefer to minimize. Posner, *supra,* n. 13, at 283.

[25] Professor Comanor argues that the promotional activities encouraged by vertical restrictions result in product differentiation and, therefore, a decrease in interbrand competition. This argument is flawed by its necessary assumption that a large part of the promotional efforts resulting from vertical restrictions will not convey socially desirable information about product availability, price, quality, and services. Nor is it clear that a *per se* rule would result in anything more than a shift to less efficient methods of obtaining the same promotional effects.

Relation, 44 Antitrust L. J. 573, 576 (1975); Pollock, *supra,* n. 13, at 610.[26]

We conclude that the distinction drawn in *Schwinn* between sale and nonsale transactions is not sufficient to justify the application of a *per se* rule in one situation and a rule of reason in the other. The question remains whether the *per se* rule stated in *Schwinn* should be expanded to include nonsale transactions or abandoned in favor of a return to the rule of reason. We have found no persuasive support for expanding the *per se* rule. As noted above, the *Schwinn* Court recognized the undesirability of "prohibit[ing] all vertical restrictions of territory and all franchising . . . ." 388 U. S., at 379–380.[27] And even Continental does not urge us to hold that all such restrictions are *per se* illegal.

We revert to the standard articulated in *Northern Pac. R. Co.,* and reiterated in *White Motor,* for determining whether vertical restrictions must be "conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use." 356 U. S., at 5. Such restrictions, in varying forms, are widely used in our free market economy. As indicated above, there is substantial scholarly and judicial au-

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[26] We also note that *per se* rules in this area may work to the ultimate detriment of the small businessmen who operate as franchisees. To the extent that a *per se* rule prevents a firm from using the franchise system to achieve efficiencies that it perceives as important to its successful operation, the rule creates an incentive for vertical integration into the distribution system, thereby eliminating to that extent the role of independent businessmen. See, *e. g.,* Keck, The *Schwinn* Case, 23 Bus. Law. 669 (1968); Pollock, *supra,* n. 13, at 608–610.

[27] Continental's contention that balancing intrabrand and interbrand competitive effects of vertical restrictions is not a "proper part of the judicial function," Brief for Petitioners 52, is refuted by *Schwinn* itself. *United States* v. *Topco Associates, Inc.,* 405 U. S., at 608, is not to the contrary, for it involved a horizontal restriction among ostensible competitors.

thority supporting their economic utility. There is relatively little authority to the contrary.[28] Certainly, there has been no showing in this case, either generally or with respect to Sylvania's agreements, that vertical restrictions have or are likely to have a "pernicious effect on competition" or that they "lack . . . any redeeming virtue." *Ibid.*[29] Accordingly, we conclude that the *per se* rule stated in *Schwinn* must be overruled.[30] In so holding we do not foreclose the possibility that particular applications of vertical restrictions might justify *per se* prohibition under *Northern Pac. R. Co.* But we do make clear that departure from the rule-of-reason standard

[28] There may be occasional problems in differentiating vertical restrictions from horizontal restrictions originating in agreements among the retailers. There is no doubt that restrictions in the latter category would be illegal *per se*, see, *e. g.*, *United States* v. *General Motors Corp.*, 384 U. S. 127 (1966); *United States* v. *Topco Associates, Inc.*, *supra*, but we do not regard the problems of proof as sufficiently great to justify a *per se* rule.

[29] The location restriction used by Sylvania was neither the least nor the most restrictive provision that it could have used. See ABA Monograph No. 2, pp. 20–25. But we agree with the implicit judgment in *Schwinn* that a *per se* rule based on the nature of the restriction is, in general, undesirable. Although distinctions can be drawn among the frequently used restrictions, we are inclined to view them as differences of degree and form. See Robinson, *supra*, n. 13, at 279–280; Averill, Sealy, Schwinn and Sherman One: An Analysis and Prognosis, 15 N. Y. L. F. 39, 65 (1969). We are unable to perceive significant social gain from channeling transactions into one form or another. Finally, we agree with the Court in *Schwinn* that the advantages of vertical restrictions should not be limited to the categories of new entrants and failing firms. Sylvania was faltering, if not failing, and we think it would be unduly artificial to deny it the use of valuable competitive tools.

[30] The importance of *stare decisis* is, of course, unquestioned, but as Mr. Justice Frankfurter stated in *Helvering* v. *Hallock*, 309 U. S. 106, 119 (1940), "*stare decisis* is a principle of policy and not a mechanical formula of adherence to the latest decision, however recent and questionable, when such adherence involves collision with a prior doctrine more embracing in its scope, intrinsically sounder, and verified by experience."

must be based upon demonstrable economic effect rather than—as in *Schwinn*—upon formalistic line drawing.

In sum, we conclude that the appropriate decision is to return to the rule of reason that governed vertical restrictions prior to *Schwinn*. When anticompetitive effects are shown to result from particular vertical restrictions they can be adequately policed under the rule of reason, the standard traditionally applied for the majority of anticompetitive practices challenged under § 1 of the Act. Accordingly, the decision of the Court of Appeals is

Affirmed.

MR. JUSTICE REHNQUIST took no part in the consideration or decision of this case.

MR. JUSTICE WHITE, concurring in the judgment.

Although I agree with the majority that the location clause at issue in this case is not a *per se* violation of the Sherman Act and should be judged under the rule of reason, I cannot agree that this result requires the overruling of *United States* v. *Arnold, Schwinn & Co.,* 388 U. S. 365 (1967). In my view this case is distinguishable from *Schwinn* because there is less potential for restraint of intrabrand competition and more potential for stimulating interbrand competition. As to intrabrand competition, Sylvania, unlike Schwinn, did not restrict the customers to whom or the territories where its purchasers could sell. As to interbrand competition, Sylvania, unlike Schwinn, had an insignificant market share at the time it adopted its challenged distribution practice and enjoyed no consumer preference that would allow its retailers to charge a premium over other brands. In two short paragraphs, the majority disposes of the view, adopted after careful analysis by the Ninth Circuit en banc below, that these differences provide a "principled basis for distinguishing *Schwinn*," *ante,* at 46, despite holdings by three Courts of Appeals and the District Court on remand in *Schwinn* that the *per se* rule established in that case does not apply to location clauses such as Sylvania's. To reach out to overrule one of this Court's recent interpretations of the Sherman Act, after such a cursory examination of the necessity for doing so, is surely an affront to the principle that considerations of *stare decisis* are to be given particularly strong weight in the area of statutory construction. *Illinois Brick Co.* v. *Illinois,* 431 U. S. 720, 736–737 (1977); *Runyon* v. *McCrary,* 427 U. S. 160, 175 (1976); *Edelman* v. *Jordan,* 415 U. S. 651, 671 (1974).

One element of the system of interrelated vertical restraints invalidated in *Schwinn* was a retail-customer restriction prohibiting franchised retailers from selling Schwinn products to nonfranchised retailers. The Court rests its inability to distinguish *Schwinn* entirely on this retail-customer restriction, finding it "[i]n intent and competitive impact . . . indistinguishable from the location restriction in the present case," because "[i]n both cases the restrictions limited the freedom of the retailer to dispose of the purchased products as he desired." *Ante,* at 46. The customer restriction may well have, however, a very different "intent and competitive impact" than the location restriction: It prevents discount stores from getting the manufacturer's product and thus prevents intrabrand price competition. Suppose, for example, that interbrand competition is sufficiently weak that the franchised retailers are able to charge a price substantially above wholesale. Under a location restriction, these franchisers are free to sell to discount stores seeking to exploit the potential for sales at prices below the prevailing retail level. One of the franchised retailers may be tempted to lower its price and act in effect as a wholesaler for the discount house in order to share in the profits to be had from lowering prices and expanding volume.[1]

[1] The franchised retailers would be prevented from engaging in discounting themselves if, under the *Colgate* doctrine, see *infra,* at 67, the

Under a retail customer restriction, on the other hand, the franchised dealers cannot sell to discounters, who are cut off altogether from the manufacturer's product and the opportunity for intrabrand price competition. This was precisely the theory on which the Government successfully challenged Schwinn's customer restrictions in this Court. The District Court in that case found that "[e]ach one of [Schwinn's franchised retailers] knows also that he is not a wholesaler and that he cannot sell as a wholesaler or act as an agent for some other unfranchised dealer, such as a discount house retailer who has not been franchised as a dealer by Schwinn." 237 F. Supp. 323, 333 (ND Ill. 1965). The Government argued on appeal, with extensive citations to the record, that the effect of this restriction was "to keep Schwinn products out of the hands of discount houses and other price cutters so as to discourage price competition in retailing . . . ." Brief for United States, O. T. 1966, No. 25, p. 26. See *id.*, at 29–37.[2]

It is true that, as the majority states, Sylvania's location restriction inhibited to some degree "the freedom of the retailer to dispose of the purchased products" by requiring the retailer to sell from one particular place of business. But the retailer is still free to sell to any type of customer—including discounters and other unfranchised dealers—from any area. I think this freedom implies a significant difference for the effect of a location clause on intrabrand competition. The

manufacturer could lawfully terminate dealers who did not adhere to his suggested retail price.

[2] Given the Government's emphasis on the inhibiting effect of the Schwinn restrictions on discounting activities, the Court may well have been referring to this effect when it condemned the restrictions as "obviously destructive of competition." 388 U. S., at 379. But the Court was also heavily influenced by its concern for the freedom of dealers to control the disposition of products they purchased from Schwinn. See *infra*, at 66–69. In any event, the record in *Schwinn* illustrates the potentially greater threat to intrabrand competition posed by customer as opposed to location restrictions.

District Court on remand in *Schwinn* evidently thought so as well, for after enjoining Schwinn's customer restrictions as directed by this Court it expressly sanctioned location clauses, permitting Schwinn to "designat[e] in its retailer franchise agreements the location of the place or places of business for which the franchise is issued." 291 F. Supp. 564, 565–566 (ND Ill. 1968).

An additional basis for finding less restraint of intrabrand competition in this case, emphasized by the Ninth Circuit en banc, is that *Schwinn* involved restrictions on competition among distributors at the wholesale level. As Judge Ely wrote for the six-member majority below:

> "[Schwinn] had created exclusive geographical sales territories for each of its 22 wholesaler bicycle distributors and had made each distributor the sole Schwinn outlet for the distributor's designated area. Each distributor was prohibited from selling to any retailers located outside its territory. . . .
>
> ". . . Schwinn's territorial restrictions requiring dealers to confine their sales to exclusive territories prescribed by Schwinn prevented a dealer from competing for customers outside his territory. . . . Schwinn's restrictions guaranteed each wholesale distributor that it would be absolutely isolated from all competition from other Schwinn wholesalers." 537 F. 2d 980, 989–990 (1976).

Moreover, like its franchised retailers, Schwinn's distributors were absolutely barred from selling to nonfranchised retailers, further limiting the possibilities of intrabrand price competition.

The majority apparently gives no weight to the Court of Appeals' reliance on the difference between the competitive effects of Sylvania's location clause and Schwinn's interlocking "system of vertical restraints affecting both wholesale and retail distribution." *Id.*, at 989. It also ignores post-*Schwinn* decisions of the Third and Tenth Circuits upholding the validity of location clauses similar to Sylvania's here. *Salco Corp.* v. *General Motors Corp.*, 517 F. 2d 567 (CA10 1975); *Kaiser* v. *General Motors Corp.*, 530 F. 2d 964 (CA3 1976), aff'g 396 F. Supp. 33 (ED Pa. 1975). Finally, many of the scholarly authorities the majority cites in support of its overruling of *Schwinn* have not had to strain to distinguish location clauses from the restrictions invalidated there. *E. g.*, Robinson, Recent Antitrust Developments: 1974, 75 Colum. L. Rev. 243, 278 (1975) (outcome in *Sylvania* not preordained by *Schwinn* because of marked differences in the vertical restraints in the two cases); McLaren, Territorial and Customer Restrictions, Consignments, Suggested Retail Prices and Refusals to Deal, 37 Antitrust L. J. 137, 144–145 (1968) (by implication *Schwinn* exempts location clauses from its *per se* rule); Pollock, Alternative Distribution Methods After *Schwinn*, 63 Nw. U. L. Rev. 595, 603 (1968) ("Nor does the *Schwinn* doctrine outlaw the use of a so-called 'location clause' . . .").

Just as there are significant differences between *Schwinn* and this case with respect to intrabrand competition, there are also significant differences with respect to interbrand competition. Unlike Schwinn, Sylvania clearly had no economic power in the generic product market. At the time they instituted their respective distribution policies, Schwinn was "the leading bicycle producer in the Nation," with a national market share of 22.5%, 388 U. S., at 368, 374, whereas Sylvania was a "faltering, if not failing" producer of television sets, with "a relatively insignificant 1% to 2%" share of the national market in which the dominant manufacturer had a 60% to 70% share. *Ante*, at 38, 58 n. 29. Moreover, the Schwinn brand name enjoyed superior consumer acceptance and commanded a premium price as, in the District Court's words, "the Cadillac of the bicycle industry." 237 F. Supp., at 335. This premium gave Schwinn dealers a margin of protection from interbrand competition and created the possibilities for price cutting by discounters that the Government argued were forestalled by Schwinn's customer restrictions.[3] Thus, judged by the criteria economists use to measure market power—product differentiation and market share [4]—Schwinn enjoyed a substantially stronger position in the bicycle market than did Sylvania in the television market. This Court relied on Schwinn's market position as one reason not to apply the rule of reason to the vertical restraints challenged there. "Schwinn was not a newcomer, seeking to break into or stay in the bicycle business. It was not a 'failing company.' On the contrary, at the initiation of these practices, it was the leading bicycle producer in the Nation." 388 U. S., at 374. And the Court of Appeals below found "another significant distinction between our case and *Schwinn*" in Sylvania's "precarious market share," which "was so small when it adopted its locations practice that it was threatened with expulsion from the television market." 537 F. 2d, at 991.[5]

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[3] Relying on the finding of the District Court, the Government argued: "[T]he declared purpose of the Schwinn franchising system [was] to establish and exploit a distinctive identity and superior consumer acceptance for the Schwinn brand name as the Cadillac of bicycles, thereby enabling the charging of a premium price . . . . This scheme could not possibly succeed, and doubtless would long ago have been abandoned, if in the consumer's mind other bicycles were just as good as Schwinn's." Brief for United States, O. T. 1966, No. 25, p. 36.

[4] See, *e. g.*, F. Scherer, Industrial Market Structure and Economics Performance 10–11 (1970); P. Samuelson, Economics 485–491 (10th ed. 1976).

[5] Schwinn's national market share declined to 12.8% in the 10 years following the institution of its distribution program, at which time it ranked second behind a firm with a 22.8% share. 388 U. S., at 368–369. In the three years following the adoption of its locations practice, Sylvania's national market share increased to 5%, placing it eighth among manufacturers of color television sets. *Ante,* at 38–39. At this time Sylvania's shares of the San Francisco, Sacramento, and northern Cali-

In my view there are at least two considerations, both relied upon by the majority to justify overruling *Schwinn,* that would provide a "principled basis" for instead refusing to extend *Schwinn* to a vertical restraint that is imposed by a "faltering" manufacturer with a "precarious" position in a generic product market dominated by another firm. The first is that, as the majority puts it, "when interbrand competition exists, as it does among television manufacturers, it provides a significant check on the exploitation of intrabrand market power because of the ability of consumers to substitute a different brand of the same product." *Ante,* at 52 n. 19. See also *ante,* at 54.[6] Second is the view, argued forcefully in the economic literature cited by the majority, that the potential benefits of vertical restraints in promoting interbrand competition are particularly strong where the manufacturer imposing the restraints is seeking to enter a new market or to expand a small market share. *Ibid.*[7] The majority even recognizes that *Schwinn* "hinted" at an exception for new entrants and failing firms from its *per se* rule. *Ante,* at 53–54, n. 22.

In other areas of antitrust law, this Court has not hesitated to base its rules of *per se* illegality in part on the defendant's market power. Indeed, in the very case from which the majority draws its standard for *per se* rules, *Northern Pac. R. Co.* v. *United States,* 356 U. S. 1, 5 (1958), the

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fornia markets were respectively 2.5%, 15%, and 5%. *Ante,* at 39 nn. 4, 6. The District Court made no findings as to Schwinn's share of local bicycle markets.

[6] For an extensive discussion of this effect of interbrand competition, see ABA Antitrust Section, Monograph No. 2, Vertical Restrictions Limiting Intrabrand Competition 60–67 (1977).

[7] Preston, Restrictive Distribution Arrangements: Economic Analysis and Public Policy Standards, 30 Law & Contemp. Prob. 506, 511 (1965); Posner, Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions, 75 Colum. L. Rev. 282, 293 (1975); Scherer, *supra,* n. 4, at 510.

Court stated the reach of the *per se* rule against tie-ins under § 1 of the Sherman Act as extending to all defendants with "sufficient economic power with respect to the tying product to appreciably restrain free competition in the market for the tied product . . . ." 356 U. S., at 6. And the Court subsequently approved an exception to this *per se* rule for "infant industries" marketing a new product. *United States* v. *Jerrold Electronics Corp.,* 187 F. Supp. 545 (ED Pa. 1960), aff'd *per curiam,* 365 U. S. 567 (1961). See also *United States* v. *Philadelphia Nat. Bank,* 374 U. S. 321, 363 (1963), where the Court held presumptively illegal a merger "which produces a firm controlling an undue percentage share of the relevant market . . . ." I see no doctrinal obstacle to excluding firms with such minimal market power as Sylvania's from the reach of the *Schwinn* rule.[8]

I have, moreover, substantial misgivings about the approach the majority takes to overruling *Schwinn.* The reason for the distinction in *Schwinn* between sale and nonsale transactions was not, as the majority would have it, "the Court's effort to accommodate the perceived intrabrand harm and interbrand benefit of vertical restrictions," *ante,* at 52; the reason was rather, as Judge Browning argued in dissent below, the notion in many of our cases involving vertical restraints that inde-

[8] Cf. *Sandura Co.* v. *FTC*, 339 F. 2d 847, 850 (CA6 1964) (territorial restrictions on distributors imposed by small manufacturer "competing with and losing ground to the 'giants' of the floor-covering industry" is not *per se* illegal); Baker, Vertical Restraints in Times of Change: From *White* to *Schwinn* to Where?, 44 Antitrust L. J. 537, 545–547 (1975) (presumptive illegality of territorial restrictions imposed by manufacturer with "any degree of market power"). The majority's failure to use the market share of Schwinn and Sylvania as a basis for distinguishing these cases is the more anomalous for its reliance, see *infra,* at 68–70, on the economic analysis of those who distinguish the anticompetitive effects of distribution restraints on the basis of the market shares of the distributors. See Posner, *supra,* at 299; Bork, The Rule of Reason and the Per Se Concept: Price Fixing and Market Division [II], 75 Yale L. J. 373, 391–429 (1966).

pendent businessmen should have the freedom to dispose of the goods they own as they see fit. Thus the first case cited by the Court in *Schwinn* for the proposition that "restraints upon alienation . . . are beyond the power of the manufacturer to impose upon its vendees and . . . are violations of § 1 of the Sherman Act," 388 U. S., at 377, was this Court's seminal decision holding a series of resale-price-maintenance agreements *per se* illegal, *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.,* 220 U. S. 373 (1911). In *Dr. Miles* the Court stated that "a general restraint upon alienation is ordinarily invalid," citing Coke on Littleton, and emphasized that the case involved "agreements restricting the freedom of trade on the part of dealers who own what they sell." *Id.,* at 404, 407–408. Mr. Justice Holmes stated in dissent: "If [the manufacturer] should make the retail dealers also agents in law as well as in name and retain the title until the goods left their hands I cannot conceive that even the present enthusiasm for regulating the prices to be charged by other people would deny that the owner was acting within his rights." *Id.,* at 411.

This concern for the freedom of the businessman to dispose of his own goods as he sees fit is most probably the explanation for two subsequent cases in which the Court allowed manufacturers to achieve economic results similar to that in *Dr. Miles* where they did not impose restrictions on dealers who had purchased their products. In *United States* v. *Colgate & Co.,* 250 U. S. 300 (1919), the Court found no antitrust violation in a manufacturer's policy of refusing to sell to dealers who failed to charge the manufacturer's suggested retail price and of terminating dealers who did not adhere to that price. It stated that the Sherman Act did not "restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal." *Id.,* at 307. In *United States* v. *General Electric Co.,* 272 U. S. 476 (1926), the Court upheld resale-price-maintenance agreements made by a patentee with its dealers who obtained its goods on a consignment basis. The Court distinguished *Dr. Miles* on the ground that the agreements there were "contracts of sale rather than of agency" and involved "an attempt by the Miles Medical Company . . . to hold its purchasers, after the purchase at full price, to an obligation to maintain prices on a resale by them." 272 U. S., at 487. By contrast, a manufacturer was free to contract with his *agents* to "[fix] the price by which his agents transfer the title from him directly to [the] consumer . . . however comprehensive as a mass or whole in [the] effect [of these contracts]." *Id.*, at 488. Although these two cases have been called into question by subsequent decisions, see *United States* v. *Parke, Davis & Co.*, 362 U. S. 29 (1960), and *Simpson* v. *Union Oil Co.*, 377 U. S. 13 (1964), their rationale runs through our case law in the area of distributional restraints. In *Kiefer-Stewart Co.* v. *Joseph E. Seagram & Sons*, 340 U. S. 211, 213 (1951), the Court held that an agreement to fix resale prices was *per se* illegal under § 1 because "such agreements, no less than those to fix minimum prices, cripple the freedom of traders and thereby restrain their ability to sell in accordance with their own judgment." Accord, *Albrecht* v. *Herald Co.*, 390 U. S. 145, 152 (1968). See generally Judge Browning's dissent below, 537 F. 2d, at 1018–1022; ABA Antitrust Section, Monograph No. 2, Vertical Restrictions Limiting Intrabrand Competition 29–31, 82–83, 87–91, 96–97 (1977); Blake & Jones, Toward a Three-Dimensional Antitrust Policy, 65 Colum. L. Rev. 422, 427–436 (1965).

After summarily rejecting this concern, reflected in our interpretations of the Sherman Act, for "the autonomy of independent businessmen," *ante*, at 53 n. 21, the majority not surprisingly finds "no justification" for *Schwinn*'s distinction between sale and nonsale transactions because the distinction is "essentially unrelated to any relevant economic impact." *Ante*, at 56. But while according some weight to the businessman's interest in controlling the terms on which he trades in his own goods may be anathema to those who view the Sherman Act as directed solely to economic efficiency,[9] this principle is without question more deeply embedded in our cases than the notions of "free rider" effects and distributional efficiencies borrowed by the majority from the "new economics of vertical relationships." *Ante,* at 54–57. Perhaps the Court is right in partially abandoning this principle and in judging the instant nonprice vertical restraints solely by their "relevant economic impact"; but the precedents which reflect this principle should not be so lightly rejected by the Court. The rationale of *Schwinn* is no doubt difficult to discern from the opinion, and it may be wrong; it is not, however, the aberration the majority makes it out to be here.

I have a further reservation about the majority's reliance on "relevant economic impact" as the test for retaining *per se* rules regarding vertical restraints. It is common ground among the leading advocates of a purely economic approach to the question of distribution restraints that the economic arguments in favor of allowing vertical nonprice restraints generally apply to vertical price restraints as well.[10] Although

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[9] *E. g.,* Bork, Legislative Intent and the Policy of the Sherman Act, 9 J. Law & Econ. 7 (1966); Bork, The Rule of Reason and the Per Se Concept: Price Fixing and Market Division [I], 74 Yale L. J. 775 (1965).

[10] Professor Posner writes, for example:

"There is no basis for choosing between [price fixing and market division] on social grounds. If resale price maintenance is like dealer price fixing, and therefore bad, a manufacturer's assignment of exclusive sales territories is like market division, and therefore bad too . . . .

. . . . .

"[If helping new entrants break into a market] is a good justification for exclusive territories, it is an equally good justification for resale price maintenance, which as we have seen is simply another method of dealing with the free-rider problem. . . . In fact, *any* argument that can be made on behalf of exclusive territories can also be made on behalf of resale price maintenance." Posner, *supra,* n. 7, at 292–293. (Footnote omitted.)

See Bork, *supra,* n. 8, at 391–464.

the majority asserts that "the *per se* illegality of price restrictions . . . involves significantly different questions of analysis and policy," *ante*, at 51 n. 18, I suspect this purported distinction may be as difficult to justify as that of *Schwinn* under the terms of the majority's analysis. Thus Professor Posner, in an article cited five times by the majority, concludes: "I believe that the law should treat price and nonprice restrictions the same and that it should make no distinction between the imposition of restrictions in a sale contract and their imposition in an agency contract." Posner, *supra*, n. 7, at 298. Indeed, the Court has already recognized that resale price maintenance may increase output by inducing "demand-creating activity" by dealers (such as additional retail outlets, advertising and promotion, and product servicing) that outweighs the additional sales that would result from lower prices brought about by dealer price competition. *Albrecht* v. *Herald Co.*, *supra*, at 151 n. 7. These same output-enhancing possibilities of nonprice vertical restraints are relied upon by the majority as evidence of their social utility and economic soundness, *ante*, at 55, and as a justification for judging them under the rule of reason. The effect, if not the intention, of the Court's opinion is necessarily to call into question the firmly established *per se* rule against price restraints.

Although the case law in the area of distributional restraints has perhaps been less than satisfactory, the Court would do well to proceed more deliberately in attempting to improve it. In view of the ample reasons for distinguishing *Schwinn* from this case and in the absence of contrary congressional action, I would adhere to the principle that

> "each case arising under the Sherman Act must be determined upon the particular facts disclosed by the record, and . . . the opinions in those cases must be read in the light of their facts and of a clear recognition of the essential differences in the facts of those cases, and in the facts of any new case to which the rule of earlier decisions

is to be aplied." *Maple Flooring Mfrs. Assn.* v. *United States,* 268 U. S. 563, 579 (1925).

In order to decide this case, the Court need only hold that a location clause imposed by a manufacturer with negligible economic power in the product market has a competitive impact sufficiently less restrictive than the *Schwinn* restraints to justify a rule-of-reason standard, even if the same weight is given here as in *Schwinn* to dealer autonomy. I therefore concur in the judgment.

MR. JUSTICE BRENNAN, with whom MR. JUSTICE MARSHALL joins, dissenting.

I would not overrule the *per se* rule stated in *United States* v. *Arnold, Schwinn & Co.,* 388 U. S. 365 (1967), and would therefore reverse the decision of the Court of Appeals for the Ninth Circuit.

Tying Arrangements

JEFFERSON PARISH HOSPITAL DISTRICT NO. 2 ET AL. *v.* HYDE

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 82–1031. Argued November 2, 1983—Decided March 27, 1984

A hospital governed by petitioners has a contract with a firm of anesthesiologists requiring all anesthesiological services for the hospital's patients to be performed by that firm. Because of this contract, respondent anesthesiologist's application for admission to the hospital's medical staff was denied. Respondent then commenced an action in Federal District Court, claiming that the exclusive contract violated § 1 of the Sherman Act, and seeking declaratory and injunctive relief. The District Court denied relief, finding that the anticompetitive consequences of the contract were minimal and outweighed by benefits in the form of improved patient care. The Court of Appeals reversed, finding the contract illegal *"per se."* The court held that the case involved a "tying arrangement" because the users of the hospital's operating rooms (the tying product) were compelled to purchase the hospital's chosen anesthesiological services (the tied product), that the hospital possessed sufficient market power in the tying market to coerce purchasers of the tied product, and that since the purchase of the tied product constituted a "not insubstantial amount of interstate commerce," the tying arrangement was therefore illegal *"per se."*

Held: The exclusive contract in question does not violate § 1 of the Sherman Act. Pp. 9–32.

(a) Any inquiry into the validity of a tying arrangement must focus on the market or markets in which the two products are sold, for that is where the anticompetitive forcing has its impact. Thus, in this case the analysis of the tying issue must focus on the hospital's sale of services to its patients, rather than its contractual arrangements with the providers of anesthesiological services. In making that analysis, consideration must be given to whether petitioners are selling two separate products that may be tied together, and, if so, whether they have used their market power to force their patients to accept the tying arrangement. Pp. 9–18.

(b) No tying arrangement can exist here unless there is a sufficient demand for the purchase of anesthesiological services separate from hospital services to identify a distinct product market in which it is efficient to offer anesthesiological services separately from hospital services. The fact that the exclusive contract requires purchase of two services that would otherwise be purchased separately does not make the contract illegal. Only if patients are forced to purchase the contracting firm's services as a result of the hospital's market power would the arrangement have anticompetitive consequences. If no forcing is present, patients are free to enter a competing hospital and to use another anesthesiologist instead of the firm. Pp. 18–25.

(c) The record does not provide a basis for applying the *per se* rule against tying to the arrangement in question. While such factors as the Court of Appeals relied on in rendering its decision—the prevalence of health insurance as eliminating a patient's incentive to compare costs, and patients' lack of sufficient information to compare the quality of the medical care provided by competing hospitals—may generate "market power" in some abstract sense, they do not generate the kind of market power that justifies condemnation of tying. Tying arrangements need only be condemned if they restrain competition on the merits by forcing purchases that would not otherwise be made. The fact that patients of the hospital lack price consciousness will not force them to take an anesthesiologist whose services they do not want. Similarly, if the patients cannot evaluate the quality of anesthesiological services, it follows that they are indifferent between certified anesthesiologists even in the absence of a tying arrangement. Pp. 26–29.

(d) In order to prevail in the absence of *per se* liability, respondent has the burden of showing that the challenged contract violated the Sherman Act because it unreasonably restrained competition, and no such showing has been made. The evidence is insufficient to provide a basis for finding that the contract, as it actually operates in the market, has unreasonably restrained competition. All the record establishes is that the choice of anesthesiologists at the hospital has been limited to one of the four doctors who are associated with the contracting firm. If respondent were admitted to the hospital's staff, the range of choice would be enlarged, but the most significant restraints on the patient's freedom to select a specific anesthesiologist would nevertheless remain. There is no evidence that the price, quality, or supply or demand for either the "tying product" or the "tied product" has been adversely affected by the exclusive contract, and no showing that the market as a whole has been affected at all by the contract. Pp. 29–32.

686 F. 2d 286, reversed and remanded.

STEVENS, J., delivered the opinion of the Court, in which BRENNAN, WHITE, MARSHALL, and BLACKMUN, JJ., joined. BRENNAN, J., filed a concurring opinion, in which MARSHALL, J., joined, *post*, p. 32. O'CON-

NOR, J., filed an opinion concurring in the judgment, in which BURGER, C. J., and POWELL and REHNQUIST, JJ., joined, *post*, p. 32.

Frank H. Easterbrook argued the cause for petitioners. With him on the briefs were *Lucas J. Giordano*, *Thomas J. Reed*, and *Henry S. Allen, Jr.*

Jerrold J. Ganzfried argued the cause for the United States as *amicus curiae* urging reversal. With him on the brief were *Solicitor General Lee*, *Assistant Attorney General Baxter*, *Deputy Solicitor General Wallace*, *Deputy Assistant Attorney General Lipsky*, *Barry Grossman*, and *Andrea Limmer*.

John M. Landis argued the cause for respondent. With him on the brief was *Phillip A. Wittman*.*

JUSTICE STEVENS delivered the opinion of the Court.

At issue in this case is the validity of an exclusive contract between a hospital and a firm of anesthesiologists. We must decide whether the contract gives rise to a *per se* violation of § 1 of the Sherman Act[1] because every patient undergoing

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*Briefs of *amici curiae* urging reversal were filed for the American Hospital Association by *Richard L. Epstein*, *Robert W. McCann*, and *John J. Miles;* for the College of American Pathologists by *Jack R. Bierig;* and for the National Association of Private Psychiatric Hospitals by *Joel I. Klein*.

Briefs of *amici curiae* urging affirmance were filed for the American Society of Anesthesiologists, Inc., by *John Landsdale, Jr.*, and *Michael Scott;* for the Association of American Physicians & Surgeons, Inc., by *Kent Masterson Brown;* and for the Louisiana State Medical Society by *Henry B. Alsobrook, Jr.*, *Frank M. Adkins*, and *Richard B. Eason II*.

Briefs of *amici curiae* were filed for the American Association of Nurse Anesthetists by *Phil David Fine*, *Robert F. Sylvia*, *Richard E. Verville*, and *Susan M. Jenkins;* and for the Louisiana Hospital Association et al. by *Ricardo M. Guevara*.

[1] Section 1 of the Sherman Act states: "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 . . . ." 26 Stat. 209, as amended, 15 U. S. C. § 1. Respondent has

surgery at the hospital must use the services of one firm of anesthesiologists, and, if not, whether the contract is nevertheless illegal because it unreasonably restrains competition among anesthesiologists.

In July 1977, respondent Edwin G. Hyde, a board-certified anesthesiologist, applied for admission to the medical staff of East Jefferson Hospital. The credentials committee and the medical staff executive committee recommended approval, but the hospital board denied the application because the hospital was a party to a contract providing that all anesthesiological services required by the hospital's patients would be performed by Roux & Associates, a professional medical corporation. Respondent then commenced this action seeking a declaratory judgment that the contract is unlawful and an injunction ordering petitioners to appoint him to the hospital staff.[2] After trial, the District Court denied relief, finding that the anticompetitive consequences of the Roux contract were minimal and outweighed by benefits in the form of improved patient care. 513 F. Supp. 532 (ED La. 1981). The Court of Appeals reversed because it was persuaded that the contract was illegal *"per se."* 686 F. 2d 286 (CA5 1982). We granted certiorari, 460 U. S. 1021 (1983), and now reverse.

I

In February 1971, shortly before East Jefferson Hospital opened, it entered into an "Anesthesiology Agreement" with Roux & Associates (Roux), a firm that had recently been organized by Dr. Kermit Roux. The contract provided that any anesthesiologist designated by Roux would be admitted to the hospital's medical staff. The hospital agreed to

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standing to enforce § 1 by virtue of § 4 of the Clayton Act, 38 Stat. 731, as amended, 15 U. S. C. § 15.

[2] In addition to seeking relief under the Sherman Act, respondent's complaint alleged violations of 42 U. S. C. § 1983 and state law. The District Court rejected these claims. The Court of Appeals passed only on the Sherman Act claim.

provide the space, equipment, maintenance, and other supporting services necessary to operate the anesthesiology department. It also agreed to purchase all necessary drugs and other supplies. All nursing personnel required by the anesthesia department were to be supplied by the hospital, but Roux had the right to approve their selection and retention.[3] The hospital agreed to "restrict the use of its anesthesia department to Roux & Associates and [that] no other persons, parties or entities shall perform such services within the Hospital for the ter[m] of this contract." App. 19.[4]

The 1971 contract provided for a 1-year term automatically renewable for successive 1-year periods unless either party elected to terminate. In 1976, a second written contract was executed containing most of the provisions of the 1971 agreement. Its term was five years and the clause excluding other anesthesiologists from the hospital was deleted;[5] the hospital nevertheless continued to regard itself as committed to a closed anesthesiology department. Only Roux was permitted to practice anesthesiology at the hospital. At the

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[3] The contract required all of the physicians employed by Roux to confine their practice of anesthesiology to East Jefferson.

[4] Originally Roux agreed to provide at least two full-time anesthesiologists acceptable to the hospital's credentials committee. Roux agreed to furnish additional anesthesiologists as necessary. The contract also provided that Roux would designate one of its qualified anesthesiologists to serve as the head of the hospital's department of anesthesia.

The fees for anesthesiological services are billed separately to the patients by the hospital. They cover the hospital's costs and the professional services provided by Roux. After a deduction of eight percent to provide a reserve for uncollectible accounts, the fees are divided equally between Roux and the hospital.

[5] "Roux testified that he requested the omission of the exclusive language in his 1976 contract because he believes a surgeon or patient is entitled to the services of the anesthesiologist of his choice. He admitted that he and others in his group did work outside East Jefferson following the 1976 contract but felt he was not in violation of the contract in light of the changes made in it." 513 F. Supp. 532, 537 (ED La. 1981).

time of trial the department included four anesthesiologists. The hospital usually employed 13 or 14 certified registered nurse anesthetists.[6]

The exclusive contract had an impact on two different segments of the economy: consumers of medical services, and providers of anesthesiological services. Any consumer of medical services who elects to have an operation performed at East Jefferson Hospital may not employ any anesthesiologist not associated with Roux. No anesthesiologists except those employed by Roux may practice at East Jefferson.

There are at least 20 hospitals in the New Orleans metropolitan area and about 70 percent of the patients living in Jefferson Parish go to hospitals other than East Jefferson. Because it regarded the entire New Orleans metropolitan area as the relevant geographic market in which hospitals compete, this evidence convinced the District Court that East Jefferson does not possess any significant "market power"; therefore it concluded that petitioners could not use the Roux contract to anticompetitive ends.[7] The same evidence led the Court of Appeals to draw a different conclusion. Noting that 30 percent of the residents of the parish go to East Jefferson Hospital, and that in fact "patients tend to choose hospitals by location rather than price or quality," the Court of

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[6] Approximately 875 operations are performed at the hospital each month; as many as 12 or 13 operating rooms may be in use at one time.

[7] The District Court found:

"The impact on commerce resulting from the East Jefferson contract is minimal. The contract is restricted in effect to one hospital in an area containing at least twenty others providing the same surgical services. It would be a different situation if Dr. Roux had exclusive contracts in several hospitals in the relevant market. As pointed out by plaintiff, the majority of surgeons have privileges at more than one hospital in the area. They have the option of admitting their patients to another hospital where they can select the anesthesiologist of their choice. Similarly a patient can go to another hospital if he is not satisfied with the physicians available at East Jefferson." *Id.*, at 541.

Appeals concluded that the relevant geographic market was the East Bank of Jefferson Parish. 686 F. 2d, at 290. The conclusion that East Jefferson Hospital possessed market power in that area was buttressed by the facts that the prevalence of health insurance eliminates a patient's incentive to compare costs, that the patient is not sufficiently informed to compare quality, and that family convenience tends to magnify the importance of location.[8]

The Court of Appeals held that the case involves a "tying arrangement" because the "users of the hospital's operating rooms (the tying product) are also compelled to purchase the hospital's chosen anesthesia service (the tied product)." *Id.*, at 289. Having defined the relevant geographic market for the tying product as the East Bank of Jefferson Parish, the court held that the hospital possessed "sufficient market power in the tying market to coerce purchasers of the tied product." *Id.*, at 291. Since the purchase of the tied product constituted a "not insubstantial amount of interstate commerce," under the Court of Appeals' reading of our decision in *Northern Pacific R. Co.* v. *United States*, 356 U. S. 1, 11 (1958), the tying arrangement was therefore illegal *"per se."*[9]

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[8] While the Court of Appeals did discuss the impact of the contract upon patients, it did not discuss its impact upon anesthesiologists. The District Court had referred to evidence that in the entire State of Louisiana there are 156 anesthesiologists and 345 hospitals with operating rooms. The record does not tell us how many of the hospitals in the New Orleans metropolitan area have "open" anesthesiology departments and how many have closed departments. Respondent, for example, practices with two other anesthesiologists at a hospital which has an open department; he previously practiced for several years in a different New Orleans hospital and, prior to that, had practiced in Florida. The record does not tell us whether there is a shortage or a surplus of anesthesiologists in any part of the country, or whether they are thriving or starving.

[9] The Court of Appeals rejected as "clearly erroneous" the District Court's finding that the exclusive contract was justified by quality considerations. See 686 F. 2d, at 292.

II

Certain types of contractual arrangements are deemed unreasonable as a matter of law.[10] The character of the restraint produced by such an arrangement is considered a sufficient basis for presuming unreasonableness without the necessity of any analysis of the market context in which the arrangement may be found.[11] A price-fixing agreement between competitors is the classic example of such an arrangement. *Arizona* v. *Maricopa County Medical Society*, 457 U. S. 332, 343–348 (1982). It is far too late in the history of our antitrust jurisprudence to question the proposition that certain tying arrangements pose an unacceptable risk of stifling competition and therefore are unreasonable *"per se."*[12] The rule was first enunciated in *International Salt Co.* v. *United States*, 332 U. S. 392, 396 (1947),[13] and has been en-

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[10] "For example, where a complaint charges that the defendants have engaged in price fixing, or have concertedly refused to deal with nonmembers of an association, or have licensed a patented device on condition that unpatented materials be employed in conjunction with the patented device, then the amount of commerce involved is immaterial because such restraints are illegal *per se.*" *United States* v. *Columbia Steel Co.*, 334 U. S. 495, 522–523 (1948) (footnotes omitted).

[11] See, *e. g.*, *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 49–50 (1977).

[12] The District Court intimated that the principles of *per se* liability might not apply to cases involving the medical profession. 513 F. Supp., at 543–544. The Court of Appeals rejected this approach. 686 F. 2d, at 292–294. In this Court, petitioners "assume" that the same principles apply to the provision of professional services as apply to other trades or businesses. Brief for Petitioners 4, n. 2. See generally *National Society of Professional Engineers* v. *United States*, 435 U. S. 679 (1978).

[13] The roots of the doctrine date at least to *Motion Picture Patents Co.* v. *Universal Film Co.*, 243 U. S. 502 (1917), a case holding that the sale of a patented film projector could not be conditioned on its use only with the patentee's films, since this would have the effect of extending the scope of the patent monopoly. See also *Henry* v. *Dick Co.*, 224 U. S. 1, 70–73 (1912) (White, C. J., dissenting).

dorsed by this Court many times since.[14] The rule also reflects congressional policies underlying the antitrust laws. In enacting § 3 of the Clayton Act, 38 Stat. 731, 15 U. S. C. § 14, Congress expressed great concern about the anticompetitive character of tying arrangements. See H. R. Rep. No. 627, 63d Cong., 2d Sess., 10–13 (1914); S. Rep. No. 698, 63d Cong., 2d Sess., 6–9 (1914).[15] While this case

[14] See *United States Steel Corp.* v. *Fortner Enterprises*, 429 U. S. 610, 619–621 (1977); *Fortner Enterprises* v. *United States Steel Corp.*, 394 U. S. 495, 498–499 (1969); *White Motor Co.* v. *United States*, 372 U. S. 253, 262 (1963); *Brown Shoe Co.* v. *United States*, 370 U. S. 294, 330 (1962); *United States* v. *Loew's Inc.*, 371 U. S. 38 (1962); *Northern Pacific R. Co.* v. *United States*, 356 U. S. 1, 5 (1958); *Black* v. *Magnolia Liquor Co.*, 355 U. S. 24, 25 (1957); *Times-Picayune Publishing Co.* v. *United States*, 345 U. S. 594, 608–609 (1953); *Standard Oil Co. of California* v. *United States*, 337 U. S. 293, 305–306 (1949).

[15] See also 51 Cong. Rec. 9072 (1914) (remarks of Rep. Webb); *id.*, at 9084 (remarks of Rep. Madden); *id.*, at 9090 (remarks of Rep. Mitchell); *id.*, at 9160–9164 (remarks of Rep. Floyd); *id.*, at 9184–9185 (remarks of Rep. Helvering); *id.*, at 9409 (remarks of Rep. Gardner); *id.*, at 9410 (remarks of Rep. Mitchell); *id.*, at 9553–9554 (remarks of Rep. Barkley); *id.*, at 14091–14097 (remarks of Sen. Reed); *id.*, at 14094 (remarks of Sen. Walsh); *id.*, at 14209 (remarks of Sen. Shields); *id.*, at 14226 (remarks of Sen. Reed); *id.*, at 14268 (remarks of Sen. Reed); *id.*, at 14599 (remarks of Sen. White); *id.*, at 15991 (remarks of Sen. Martine); *id.*, at 16146 (remarks of Sen. Walsh); Spivack, The Chicago School Approach to Single Firm Exercises of Monopoly Power: A Response, 52 Antitrust L. J. 651, 664–665 (1983). For example, the House Report on the Clayton Act stated:

"The public is compelled to pay a higher price and local customers are put to the inconvenience of securing many commodities in other communities or through mail-order houses that can not be procured at their local stores. The price is raised as an inducement. This is the local effect. Where the concern making these contracts is already great and powerful, such as the United Shoe Machinery Co., the American Tobacco Co., and the General Film Co., the exclusive or 'tying' contract made with local dealers becomes one of the greatest agencies and instrumentalities of monopoly ever devised by the brain of man. It completely shuts out competitors, not only from trade in which they are already engaged, but from the opportunities to build up trade in any community where these great and powerful combinations are operating under this system and practice. By this method and practice the Shoe Machinery Co. has built up a monopdoes not arise under the Clayton Act, the congressional finding made therein concerning the competitive consequences of tying is illuminating, and must be respected.[16]

It is clear, however, that not every refusal to sell two products separately can be said to restrain competition. If each of the products may be purchased separately in a competitive market, one seller's decision to sell the two in a single package imposes no unreasonable restraint on either market, par-

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oly that owns and controls the entire machinery now being used by all great shoe-manufacturing houses of the United States. No independent manufacturer of shoe machines has the slightest opportunity to build up any considerable trade in this country while this condition obtains. If a manufacturer who is using machines of the Shoe Machinery Co. were to purchase and place a machine manufacturered by any independent company in his establishment, the Shoe Machinery Co. could under its contracts withdraw all their machinery from the establishment of the shoe manufacturer and thereby wreck the business of the manufacturer. The General Film Co., by the same method practiced by the Shoe Machinery Co. under the lease system, has practically destroyed all competition and acquired a virtual monopoly of all films manufactured and sold in the United States. When we consider contracts of sales made under this system, the result to the consumer, the general public, and the local dealer and his business is even worse than under the lease system." H. R. Rep. No. 627, 63d Cong., 2d Sess., 12–13 (1914).

Similarly, Representative Mitchell said: "[M]onopoly has been built up by these 'tying' contracts so that in order to get one machine one must take all of the essential machines, or practically all. Independent companies who have sought to enter the field have found that the markets have been preempted . . . . The manufacturers do not want to break their contracts with these giant monopolies, because, if they should attempt to install machinery, their business might be jeopardized and all of the machinery now leased by these giant monopolies would be removed from their places of business. No situation cries more urgently for relief than does this situation, and this bill seeks to prevent exclusive 'tying' contracts that have brought about a monopoly, alike injurious to the small dealers, to the manufacturers, and grossly unfair to those who seek to enter the field of competition and to the millions of consumers." 51 Cong. Rec. 9090 (1914).

[16] See generally, *e. g., Hodel* v. *Virginia Surface Mining & Reclamation Assn.*, 452 U. S. 264, 276–277 (1981); *New Orleans* v. *Dukes*, 427 U. S. 297, 303–304 (1976) *(per curiam).*

ticularly if competing suppliers are free to sell either the entire package or its several parts.[17] For example, we have written that "if one of a dozen food stores in a community were to refuse to sell flour unless the buyer also took sugar it would hardly tend to restrain competition in sugar if its competitors were ready and able to sell flour by itself." *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 7.[18] Buyers often find package sales attractive; a seller's decision to offer such packages can merely be an attempt to compete effectively—conduct that is entirely consistent with the Sherman Act. See *Fortner Enterprises* v. *United States Steel Corp.*, 394 U. S. 495, 517–518 (1969) *(Fortner I)* (WHITE, J., dissenting); *id.*, at 524–525 (Fortas, J., dissenting).

Our cases have concluded that the essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms. When such "forcing" is present, competition on the merits in the market for the tied item is restrained and the Sherman Act is violated.

> "Basic to the faith that a free economy best promotes the public weal is that goods must stand the cold test of competition; that the public, acting through the market's impersonal judgment, shall allocate the Nation's resources and thus direct the course its economic development will take. . . . By conditioning his sale of one commodity on

[17] "Of course where the buyer is free to take either product by itself there is no tying problem even though the seller may also offer the two items as a unit at a single price." *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 6, n. 4.

[18] Thus, we have held that a seller who ties the sale of houses to the provision of credit simply as a way of effectively competing in a competitive market does not violate the antitrust laws. "The unusual credit bargain offered to Fortner proves nothing more than a willingness to provide cheap financing in order to sell expensive houses." *United States Steel Corp.* v. *Fortner Enterprises*, 429 U. S., at 622 (footnote omitted).

> the purchase of another, a seller coerces the abdication of buyers' independent judgment as to the 'tied' product's merits and insulates it from the competitive stresses of the open market. But any intrinsic superiority of the 'tied' product would convince freely choosing buyers to select it over others anyway." *Times-Picayune Publishing Co.* v. *United States*, 345 U. S. 594, 605 (1953).[19]

Accordingly, we have condemned tying arrangements when the seller has some special ability—usually called "mar-

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[19] Accord, *Fortner I*, 394 U. S., at 508–509; *Atlantic Refining Co.* v. *FTC*, 381 U. S. 357, 369–371 (1965); *United States* v. *Loew's Inc.*, 371 U. S., at 44–45; *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 6. For example, JUSTICE WHITE has written:

"There is general agreement in the cases and among commentators that the fundamental restraint against which the tying proscription is meant to guard is the use of power over one product to attain power over another, or otherwise to distort freedom of trade and competition in the second product. This distortion injures the buyers of the second product, who because of their preference for the seller's brand of the first are artificially forced to make a less than optimal choice in the second. And even if the customer is indifferent among brands of the second product and therefore loses nothing by agreeing to use the seller's brand of the second in order to get his brand of the first, such tying agreements may work significant restraints on competition in the tied product. The tying seller may be working toward a monopoly position in the tied product and, even if he is not, the practice of tying forecloses other sellers of the tied product and makes it more difficult for new firms to enter that market. They must be prepared not only to match existing sellers of the tied product in price and quality, but to offset the attraction of the tying product itself. Even if this is possible through simultaneous entry into production of the tying product, entry into both markets is significantly more expensive than simple entry into the tied market, and shifting buying habits in the tied product is considerably more cumbersome and less responsive to variations in competitive offers. In addition to these anticompetitive effects in the tied product, tying arrangements may be used to evade price control in the tying product through clandestine transfer of the profit to the tied product; they may be used as a counting device to effect price discrimination; and they may be used to force a full line of products on the customer so as to extract more easily from him a monopoly return on one unique product in the line." *Fortner I*, 394 U. S., at 512–514 (dissenting opinion) (footnotes omitted).

ket power"—to force a purchaser to do something that he would not do in a competitive market. See *United States Steel Corp.* v. *Fortner Enterprises*, 429 U. S. 610, 620 (1977) *(Fortner II); Fortner I*, 394 U. S., at 503–504; *United States* v. *Loew's Inc.*, 371 U. S. 38, 45, 48, n. 5 (1962); *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 6–7.[20] When "forcing" occurs, our cases have found the tying arrangement to be unlawful.

Thus, the law draws a distinction between the exploitation of market power by merely enhancing the price of the tying product, on the one hand, and by attempting to impose restraints on competition in the market for a tied product, on the other. When the seller's power is just used to maximize its return in the tying product market, where presumably its product enjoys some justifiable advantage over its competitors, the competitive ideal of the Sherman Act is not necessarily compromised. But if that power is used to impair competition on the merits in another market, a potentially inferior product may be insulated from competitive pressures.[21] This impairment could either harm existing competitors or create barriers to entry of new competitors in the market for the tied product, *Fortner I*, 394 U. S., at 509,[22] and can in-

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[20] This type of market power has sometimes been referred to as "leverage." Professors Areeda and Turner provide a definition that suits present purposes. "'Leverage' is loosely defined here as a supplier's power to induce his customer for one product to buy a second product from him that would not otherwise be purchased solely on the merit of that second product." 5 P. Areeda & D. Turner, Antitrust Law ¶1134a, p. 202 (1980).

[21] See Report of the Attorney General's National Committee to Study the Antitrust Laws 145 (1955); Craswell, Tying Requirements in Competitive Markets: The Consumer Protection Issues, 62 B. U. L. Rev. 661, 666–668 (1982); Slawson, A Stronger, Simpler Tie-In Doctrine, 25 Antitrust Bull. 671, 676–684 (1980); Turner, The Validity of Tying Arrangements under the Antitrust Laws, 72 Harv. L. Rev. 50, 60–62 (1958).

[22] See 3 Areeda & Turner, *supra* n. 20, ¶733e (1978); C. Kaysen & D. Turner, Antitrust Policy 157 (1959); L. Sullivan, Law of Antitrust §156 (1977); O. Williamson, Markets and Hierarchies: Analysis and Anti-

crease the social costs of market power by facilitating price discrimination, thereby increasing monopoly profits over what they would be absent the tie, *Fortner II*, 429 U. S., at 617.[23] And from the standpoint of the consumer—whose interests the statute was especially intended to serve—the freedom to select the best bargain in the second market is impaired by his need to purchase the tying product, and perhaps by an inability to evaluate the true cost of either product when they are available only as a package.[24] In sum, to permit restraint of competition on the merits through tying arrangements would be, as we observed in *Fortner II*, to condone "the existence of power that a free market would not tolerate." 429 U. S., at 617 (footnote omitted).

Per se condemnation—condemnation without inquiry into actual market conditions—is only appropriate if the existence of forcing is probable.[25] Thus, application of the *per se* rule

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trust Implications 111 (1975); Pearson, Tying Arrangements and Antitrust Policy, 60 Nw. U. L. Rev. 626, 637–638 (1965).

[23] Sales of the tied item can be used to measure demand for the tying item; purchasers with greater needs for the tied item make larger purchases and in effect must pay a higher price to obtain the tying item. See P. Areeda, Antitrust Analysis ¶533 (2d ed. 1974); R. Posner, Antitrust Law 173–180 (1976); Sullivan, *supra* n. 22, § 156; Bowman, Tying Arrangements and the Leverage Problem, 67 Yale L. J. 19 (1957); Burstein, A Theory of Full-Line Forcing, 55 Nw. U. L. Rev. 62 (1960); Dam, Fortner Enterprises v. United States Steel: "Neither a Borrower, Nor a Lender Be," 1969 S. Ct. Rev. 1, 15–16; Ferguson, Tying Arrangements and Reciprocity: An Economic Analysis, 30 Law & Contemp. Prob. 552, 554–558 (1965); Markovits, Tie-Ins, Reciprocity, and the Leverage Theory, 76 Yale L. J. 1397 (1967); Pearson, *supra* n. 22, at 647–653; Sidak, Debunking Predatory Innovation, 83 Colum. L. Rev. 1121, 1127–1131 (1983); Stigler, United States v. Loew's Inc.: A Note on Block-Booking, 1963 S. Ct. Rev. 152.

[24] Especially where market imperfections exist, purchasers may not be fully sensitive to the price or quality implications of a tying arrangement, and hence it may impede competition on the merits. See Craswell, *supra* n. 21, at 675–679.

[25] The rationale for *per se* rules in part is to avoid a burdensome inquiry into actual market conditions in situations where the likelihood of anti-

focuses on the probability of anticompetitive consequences. Of course, as a threshold matter there must be a substantial potential for impact on competition in order to justify *per se* condemnation. If only a single purchaser were "forced" with respect to the purchase of a tied item, the resultant impact on competition would not be sufficient to warrant the concern of antitrust law. It is for this reason that we have refused to condemn tying arrangements unless a substantial volume of commerce is foreclosed thereby. See *Fortner I*, 394 U. S., at 501–502; *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 6–7; *Times-Picayune*, 345 U. S., at 608–610; *International Salt*, 332 U. S., at 396. Similarly, when a purchaser is "forced" to buy a product he would not have otherwise bought even from another seller in the tied-product market, there can be no adverse impact on competition because no portion of the market which would otherwise have been available to other sellers has been foreclosed.

Once this threshold is surmounted, *per se* prohibition is appropriate if anticompetitive forcing is likely. For example, if the Government has granted the seller a patent or similar monopoly over a product, it is fair to presume that the inability to buy the product elsewhere gives the seller market power. *United States* v. *Loew's Inc.*, 371 U. S., at 45–47. Any effort to enlarge the scope of the patent monopoly by using the market power it confers to restrain competition in the market for a second product will undermine competition on the merits in that second market. Thus, the sale or lease of a patented item on condition that the buyer make all his purchases of a separate tied product from the patentee is unlawful. See *United States* v. *Paramount Pictures, Inc.*, 334 U. S. 131, 156–159 (1948); *International Salt*, 332

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competitive conduct is so great as to render unjustified the costs of determining whether the particular case at bar involves anticompetitive conduct. See, *e. g.*, *Arizona* v. *Maricopa County Medical Society*, 457 U. S. 332, 350–351 (1982).

U. S., at 395–396; *International Business Machines Corp.* v. *United States*, 298 U. S. 131 (1936).

The same strict rule is appropriate in other situations in which the existence of market power is probable. When the seller's share of the market is high, see *Times-Picayune Publishing Co.* v. *United States*, 345 U. S., at 611–613, or when the seller offers a unique product that competitors are not able to offer, see *Fortner I*, 394 U. S., at 504–506, and n. 2, the Court has held that the likelihood that market power exists and is being used to restrain competition in a separate market is sufficient to make *per se* condemnation appropriate. Thus, in *Northern Pacific R. Co.* v. *United States*, 356 U. S. 1 (1958), we held that the railroad's control over vast tracts of western real estate, although not itself unlawful, gave the railroad a unique kind of bargaining power that enabled it to tie the sales of that land to exclusive, long-term commitments that fenced out competition in the transportation market over a protracted period.[26] When, however, the

[26] "As pointed out before, the defendant was initially granted large acreages by Congress in the several Northwestern States through which its lines now run. This land was strategically located in checkerboard fashion amid private holdings and within economic distance of transportation facilities. Not only the testimony of various witnesses but common sense makes it evident that this particular land was often prized by those who purchased or leased it and was frequently essential to their business activities. In disposing of its holdings the defendant entered into contracts of sale or lease covering at least several million acres of land which included 'preferential routing' clauses. The very existence of this host of tying arrangements is itself compelling evidence of the defendant's great power, at least where, as here, no other explanation has been offered for the existence of these restraints. The 'preferential routing' clauses conferred no benefit on the purchasers or lessees. While they got the land they wanted by yielding their freedom to deal with competing carriers, the defendant makes no claim that it came any cheaper than if the restrictive clauses had been omitted. In fact any such price reduction in return for rail shipments would have quite plainly constituted an unlawful rebate to the shipper. So far as the Railroad was concerned its purpose obviously was to fence out competitors, to stifle competition." 356 U. S., at 7–8 (footnote omitted).

seller does not have either the degree or the kind of market power that enables him to force customers to purchase a second, unwanted product in order to obtain the tying product, an antitrust violation can be established only by evidence of an unreasonable restraint on competition in the relevant market. See *Fortner I*, 394 U. S., at 499–500; *Times-Picayune Publishing Co.* v. *United States*, 345 U. S., at 614–615.

In sum, any inquiry into the validity of a tying arrangement must focus on the market or markets in which the two products are sold, for that is where the anticompetitive forcing has its impact. Thus, in this case our analysis of the tying issue must focus on the hospital's sale of services to its patients, rather than its contractual arrangements with the providers of anesthesiological services. In making that analysis, we must consider whether petitioners are selling two separate products that may be tied together, and, if so, whether they have used their market power to force their patients to accept the tying arrangement.

III

The hospital has provided its patients with a package that includes the range of facilities and services required for a variety of surgical operations.[27] At East Jefferson Hospital the package includes the services of the anesthesiologist.[28] Petitioners argue that the package does not involve a tying ar-

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[27] The physical facilities include the operating room, the recovery room, and the hospital room where the patient stays before and after the operation. The services include those provided by staff physicians, such as radiologists or pathologists, and interns, nurses, dietitians, pharmacists, and laboratory technicians.

[28] It is essential to differentiate between the Roux contract and the legality of the contract between the hospital and its patients. The Roux contract is nothing more than an arrangement whereby Roux supplies all of the hospital's needs for anesthesiological services. That contract raises only an exclusive-dealing question, see n. 51, *infra*. The issue here is whether the hospital's insistence that its patients purchase anesthesiological services from Roux creates a tying arrangement.

rangement at all—that they are merely providing a functionally integrated package of services.[29] Therefore, petitioners contend that it is inappropriate to apply principles concerning tying arrangements to this case.

Our cases indicate, however, that the answer to the question whether one or two products are involved turns not on the functional relation between them, but rather on the character of the demand for the two items.[30] In *Times-Picayune Publishing Co.* v. *United States*, 345 U. S. 594 (1953), the Court held that a tying arrangement was not present because the arrangement did not link two distinct markets for products that were distinguishable in the eyes of buyers.[31] In

[29] See generally Dolan & Ralston, Hospital Admitting Privileges and the Sherman Act, 18 Hous. L. Rev. 707, 756–758 (1981); Kissam, Webber, Bigus, & Holzgraefe, Antitrust and Hospital Privileges: Testing the Conventional Wisdom, 70 Calif. L. Rev. 595, 666–667 (1982).

[30] The fact that anesthesiological services are functionally linked to the other services provided by the hospital is not in itself sufficient to remove the Roux contract from the realm of tying arrangements. We have often found arrangements involving functionally linked products at least one of which is useless without the other to be prohibited tying devices. See *Mercoid Corp.* v. *Mid-Continent Co.*, 320 U. S. 661 (1944) (heating system and stoker switch); *Morton Salt Co.* v. *Suppiger Co.*, 314 U. S. 488 (1942) (salt machine and salt); *International Salt Co.* v. *United States*, 332 U. S. 392 (1947) (same); *Leitch Mfg. Co.* v. *Barber Co.*, 302 U. S. 458 (1938) (process patent and material used in the patented process); *International Business Machines Corp.* v. *United States*, 298 U. S. 131 (1936) (tabulators and tabulating punch cards); *Carbice Corp.* v. *American Patents Development Corp.*, 283 U. S. 27 (1931) (ice cream transportation package and coolant); *FTC* v. *Sinclair Refining Co.*, 261 U. S. 463 (1923) (gasoline and underground tanks and pumps); *United Shoe Machinery Co.* v. *United States*, 258 U. S. 451 (1922) (shoe machinery and supplies, maintenance, and peripheral machinery); *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545, 558–560 (ED Pa. 1960) (components of television antennas), aff'd, 365 U. S. 567 (1961) *(per curiam)*. In fact, in some situations the functional link between the two items may enable the seller to maximize its monopoly return on the tying item as a means of charging a higher rent or purchase price to a larger user of the tying item. See n. 23, *supra*.

[31] "The District Court determined that the Times-Picayune and the States were separate and distinct newspapers, though published under

Fortner I, the Court concluded that a sale involving two independent transactions, separately priced and purchased from the buyer's perspective, was a tying arrangement.[32] These

single ownership and control. But that readers consciously distinguished between these two publications does not necessarily imply that advertisers bought separate and distinct products when insertions were placed in the Times-Picayune and the States. So to conclude here would involve speculation that advertisers bought space motivated by considerations other than customer coverage; that their media selections, in effect, rested on generic qualities differentiating morning from evening readers in New Orleans. Although advertising space in the Times-Picayune, as the sole morning daily, was doubtless essential to blanket coverage of the local newspaper readership, nothing in the record suggests that advertisers viewed the city's newspaper readers, morning or evening, as other than fungible customer potential. We must assume, therefore, that the readership 'bought' by advertisers in the Times-Picayune was the selfsame 'product' sold by the States and, for that matter, the Item.

"The factual departure from the 'tying' cases then becomes manifest. The common core of the adjudicated unlawful tying arrangements is the forced purchase of a second distinct commodity with the desired purchase of a dominant 'tying' product, resulting in economic harm to competition in the 'tied' market. Here, however, two newspapers under single ownership at the same place, time, and terms sell indistinguishable products to advertisers; no dominant 'tying' product exists (in fact, since space in neither the Times-Picayune nor the States can be bought alone, one may be viewed as 'tying' as the other); no leverage in one market excludes sellers in the second, because for present purposes the products are identical and the market the same." 345 U. S., at 613–614 (footnote omitted).

[32] "There is, at the outset of every tie-in case, including the familiar cases involving physical goods, the problem of determining whether two separate products are in fact involved. In the usual sale on credit the seller, a single individual or corporation, simply makes an agreement determining when and how much he will be paid for his product. In such a sale the credit may constitute such an inseparable part of the purchase price for the item that the entire transaction could be considered to involve only a single product. It will be time enough to pass on the issue of credit sales when a case involving it actually arises. Sales such as that are a far cry from the arrangement involved here, where the credit is provided by one corporation on condition that a product be purchased from a separate corporation, and where the borrower contracts to obtain a large sum of money over and above that needed to pay the seller for the physical products purchased. Whatever the standards for determining exactly when a transaction in-

cases make it clear that a tying arrangement cannot exist unless two separate product markets have been linked.

The requirement that two distinguishable product markets be involved follows from the underlying rationale of the rule against tying. The definitional question depends on whether the arrangement may have the type of competitive consequences addressed by the rule.[33] The answer to the question whether petitioners have utilized a tying arrangement must be based on whether there is a possibility that the economic effect of the arrangement is that condemned by the rule against tying—that petitioners have foreclosed competition on the merits in a product market distinct from the market for the tying item.[34] Thus, in this case no tying arrangement can exist unless there is a sufficient demand for the purchase of anesthesiological services separate from hospital services

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volves only a 'single product,' we cannot see how an arrangement such as that present in this case could ever be said to involve only a single product." 394 U. S., at 507 (footnote omitted).

[33] Professor Dam has pointed out that the *per se* rule against tying can be coherent only if tying is defined by reference to the economic effect of the arrangement.

"[T]he definitional question is hard to separate from the question when tie-ins are harmful. Yet the decisions, in adopting the per se rule, have attempted to flee from that economic question by ruling that tying arrangements are presumptively harmful, at least whenever certain nominal threshold standards on power and foreclosure are met. The weakness of the per se methodology is that it places crucial importance on the definition of the practice. Once an arrangement falls within the defined limits, no justification will be heard. But a per se rule gives no economic standards for defining the practice. To treat the definitional question as an abstract inquiry into whether one or two products is involved is thus to compound the weakness of the per se approach." Dam, *supra* n. 23, at 19.

[34] Of course, the Sherman Act does not prohibit "tying"; it prohibits "contract[s] . . . in restraint of trade." Thus, in a sense the question whether this case involves "tying" is beside the point. The legality of petitioners' conduct depends on its competitive consequences, not on whether it can be labeled "tying." If the competitive consequences of this arrangement are not those to which the *per se* rule is addressed, then it should not be condemned irrespective of its label.

to identify a distinct product market in which it is efficient to offer anesthesiological services separately from hospital services.[35]

Unquestionably, the anesthesiological component of the package offered by the hospital could be provided separately and could be selected either by the individual patient or by one of the patient's doctors if the hospital did not insist on including anesthesiological services in the package it offers to its customers. As a matter of actual practice, anesthesiological services are billed separately from the hospital services petitioners provide. There was ample and uncontroverted testimony that patients or surgeons often request specific anesthesiologists to come to a hospital and provide anesthesia, and that the choice of an individual anesthesiologist separate from the choice of a hospital is particularly frequent in respondent's specialty, obstetric anesthesiology.[36] The Dis-

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[35] This approach is consistent with that taken by a number of lower courts. See *Moore* v. *Jas. H. Matthews & Co.*, 550 F. 2d 1207, 1214–1215 (CA9 1977); *Siegel* v. *Chicken Delight, Inc.*, 448 F. 2d 43, 48–49 (CA9 1971), cert. denied, 405 U. S. 955 (1972); *Washington Gas Light Co.* v. *Virginia Electric & Power Co.*, 438 F. 2d 248, 253 (CA4 1971); *Susser* v. *Carvel Corp.*, 332 F. 2d 505, 514 (CA2 1964), cert. dism'd, 381 U. S. 125 (1965); *United States* v. *Mercedes-Benz of North America, Inc.*, 517 F. Supp. 1369, 1379–1381 (ND Cal. 1981); *In re Data General Corp. Antitrust Litigation*, 490 F. Supp. 1089, 1104–1110 (ND Cal. 1980); *Jones* v. *247 East Chestnut Properties*, 1975–2 Trade Cases ¶ 60,491, pp. 67,162–67,163 (ND Ill. 1974); *N. W. Controls, Inc.* v. *Outboard Marine Corp.*, 333 F. Supp. 493, 501–504 (Del. 1971); *Teleflex Industrial Products, Inc.* v. *Brunswick Corp.*, 293 F. Supp. 107, 109, and n. 6 (ED Pa. 1968). See generally Ross, The Single Product Issue in Antitrust Tying: A Functional Approach, 23 Emory L. J. 963 (1974); Wheeler, Some Observations on Tie-ins, the Single-Product Defense, Exclusive Dealing and Regulated Industries, 60 Calif. L. Rev. 1557, 1558–1567, 1572–1573 (1972); Note, Product Separability: A Workable Standard to Identify Tie-In Arrangements Under the Antitrust Laws, 46 S. Cal. L. Rev. 160 (1972). See also *Fortner I*, 394 U. S., at 525 (Fortas, J., dissenting); Note, Tying Arrangements and the Single Product Issue, 31 Ohio St. L. J. 861 (1970).

[36] Testimony that patients and their physicians frequently do differentiate between hospital services and anesthesiological services, and request

trict Court found that "[t]he provision of anesthesia services is a medical service separate from the other services provided by the hospital." 513 F. Supp., at 540.[37] The Court of Appeals agreed with this finding, and went on to observe: "[A]n anesthesiologist is normally selected by the surgeon, rather than the patient, based on familiarity gained through a working relationship. Obviously, the surgeons who practice at East Jefferson Hospital do not gain familiarity with any anesthesiologists other than Roux and Associates." 686 F. 2d, at 291.[38] The record amply supports the conclusion that consumers differentiate between anesthesiological services and the other hospital services provided by petitioners.[39]

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specific anesthesiologists, was provided by Dr. Roux, Tr. 17, 20 (May 15, 1980, afternoon session), Dr. Hyde, *id.*, at 68–69, 72–74 (May 16, 1980), and other anesthesiologists as well, see *id.*, at 64, 87–88 (May 15, 1980, afternoon session) (testimony of Dr. Charles Eckert); *id.*, at 25–30, 33–34 (May 16, 1980) (testimony of Dr. John Adriani). There was no testimony that patients or their surgeons do not differentiate between anesthesiological services and hospital services when making purchasing decisions. As a statistical matter, only 27 percent of anesthesiologists have financial relationships with hospitals. American Medical Association, Socioeconomic Characteristics of Medical Practice: 1983, p. 12 (1983). In this respect anesthesiologists may differ from radiologists, pathologists, and other types of hospital-based physicians (HBPs). "In some respects anesthesiologists are more akin to office-based MDs (particularly surgeons) than other HBPs. Anesthesiologists' outputs are more discrete, and these HBPs are predominantly fee-for-service practitioners who directly provide services to patients." Steinwald, Hospital-Based Physicians: Current Issues and Descriptive Evidence, Health Care Financing Rev. 63, 69 (Summer 1980). See also *United States* v. *American Society of Anesthesiologists, Inc.*, 473 F. Supp. 147, 150 (SDNY 1979) ("By 1957 the salaried anesthesiologist had become the exception. Anesthesiologists began to establish independent practices and were able to obtain hospital privileges upon the same terms and conditions as other clinicians").

[37] Accordingly, in its conclusions of law the District Court treated the case as involving a tying arrangement. 513 F. Supp., at 542.

[38] Petitioners do not challenge these findings of the District Court and the Court of Appeals.

[39] One of the most frequently cited statements on this subject was made by Judge Van Dusen in *United States* v. *Jerrold Electronics Corp.*, 187

Thus, the hospital's requirement that its patients obtain necessary anesthesiological services from Roux combined the purchase of two distinguishable services in a single transaction.[40] Nevertheless, the fact that this case involves a re-

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F. Supp. 545 (ED Pa. 1960), aff'd, 365 U. S. 567 (1961) *(per curiam)*. While this statement was specifically made with respect to § 3 of the Clayton Act, 15 U. S. C. § 14, its analysis is also applicable to § 1 of the Sherman Act, since with respect to the definition of tying the standards used by the two statutes are the same. See *Times-Picayune*, 345 U. S., at 608–609.

"There are several facts presented in this record which tend to show that a community television antenna system cannot properly be characterized as a single product. Others who entered the community antenna field offered all of the equipment necessary for a complete system, but none of them sold their gear exclusively as a single package as did Jerrold. The record also establishes that the number of pieces in each system varied considerably so that hardly any two versions of the alleged product were the same. Furthermore, the customer was charged for each item of equipment and not a lump sum for the total system. Finally, while Jerrold had cable and antennas to sell which were manufactured by other concerns, it only required that the electronic equipment in the system be bought from it." 187 F. Supp., at 559.

The record here shows that other hospitals often permit anesthesiological services to be purchased separately, that anesthesiologists are not fungible in that the services provided by each are not precisely the same, that anesthesiological services are billed separately, and that the hospital required purchases from Roux even though other anesthesiologists were available and Roux had no objection to their receiving staff privileges at East Jefferson. Therefore, the *Jerrold* analysis indicates that there was a tying arrangement here. *Jerrold* also indicates that tying may be permissible when necessary to enable a new business to break into the market. See *id.*, at 555–558. Assuming this defense exists, and assuming it justified the 1971 Roux contract in order to give Roux an incentive to go to work at a new hospital with an uncertain future, that justification is inapplicable to the 1976 contract, since by then Roux was willing to continue to service the hospital without a tying arrangement.

[40] This is not to say that § 1 of the Sherman Act gives a purchaser the right to buy a product that the seller does not wish to offer for sale. A grocer may decide to carry four brands of cookies and no more. If the customer wants a fifth brand, he may go elsewhere but he cannot sue the grocer even if there is no other in town. However, in such a case the cus-

quired purchase of two services that would otherwise be purchased separately does not make the Roux contract illegal. As noted above, there is nothing inherently anticompetitive about packaged sales. Only if patients are forced to purchase Roux's services as a result of the hospital's market power would the arrangement have anticompetitive consequences. If no forcing is present, patients are free to enter a competing hospital and to use another anesthesiologist instead of Roux.[41] The fact that petitioners' patients are required to purchase two separate items is only the beginning of the appropriate inquiry.[42]

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tomer is free to purchase no cookies at all, while buying other needed food. If the grocer required the customer to buy an unwanted brand of cookies in order to buy other items which the customer needs and cannot readily obtain elsewhere, then a tying question arises. Cf. *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 7 (grocer selling flour can require customers to also buy sugar only "if its competitors were ready and able to sell flour by itself"). Here, the question is whether patients are forced to use an unwanted anesthesiologist in order to obtain needed hospital services.

[41] An examination of the reason or reasons why petitioners denied respondent staff privileges will not provide the answer to the question whether the package of services they offered to their patients is an illegal tying arrangement. As a matter of antitrust law, petitioners may give their anesthesiology business to Roux because he is the best doctor available, because he is willing to work long hours, or because he is the son-in-law of the hospital administrator without violating the *per se* rule against tying. Without evidence that petitioners are using market power to force Roux upon patients there is no basis to view the arrangement as unreasonably restraining competition whatever the reasons for its creation. Conversely, with such evidence, the *per se* rule against tying may apply. Thus, we reject the view of the District Court that the legality of an arrangement of this kind turns on whether it was adopted for the purpose of improving patient care.

[42] Petitioners argue and the District Court found that the exclusive contract had what it characterized as procompetitive justifications in that an exclusive contract ensures 24-hour anesthesiology coverage, enables flexible scheduling, and facilitates work routine, professional standards, and maintenance of equipment. The Court of Appeals held these findings to be clearly erroneous since the exclusive contract was not necessary to

IV

The question remains whether this arrangement involves the use of market power to force patients to buy services they would not otherwise purchase. Respondent's only basis for invoking the *per se* rule against tying and thereby avoiding analysis of actual market conditions is by relying on the preference of persons residing in Jefferson Parish to go to East Jefferson, the closest hospital. A preference of this kind, however, is not necessarily probative of significant market power.

Seventy percent of the patients residing in Jefferson Parish enter hospitals other than East Jefferson. 513 F. Supp., at 539. Thus East Jefferson's "dominance" over persons residing in Jefferson Parish is far from overwhelming.[43] The

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achieve these ends. Roux was willing to provide 24-hour coverage even without an exclusive contract and the credentials committee of the hospital could impose standards for staff privileges that would ensure staff would comply with the demands of scheduling, maintenance, and professional standards. 686 F. 2d, at 292. In the past, we have refused to tolerate manifestly anticompetitive conduct simply because the health care industry is involved. See *Arizona* v. *Maricopa Medical Society*, 457 U. S., at 348–351; *National Gerimedical Hospital* v. *Blue Cross*, 452 U. S. 378 (1981); *American Medical Assn.* v. *United States*, 317 U. S. 519, 528–529 (1943). Petitioners seek no special solicitude. See n. 12, *supra*. We have also uniformly rejected similar "goodwill" defenses for tying arrangements, finding that the use of contractual quality specifications are generally sufficient to protect quality without the use of a tying arrangement. See *Standard Oil Co. of California* v. *United States*, 337 U. S., at 305–306; *International Salt Co.* v. *United States*, 332 U. S., at 397–398; *International Business Machines Corp.* v. *United States*, 298 U. S., at 138–140. See generally Comment, Tying Arrangements under the Antitrust Laws: The "Integrity of the Product" Defense, 62 Mich. L. Rev. 1413 (1964). Since the District Court made no finding as to why contractual quality specifications would not protect the hospital, there is no basis for departing from our prior cases here.

[43] In fact its position in this market is not dissimilar from the market share at issue in *Times-Picayune*, which the Court found insufficient as a basis for inferring market power. See 345 U. S., at 611–613. Moreover,

fact that a substantial majority of the parish's residents elect not to enter East Jefferson means that the geographic data do not establish the kind of dominant market position that obviates the need for further inquiry into actual competitive conditions. The Court of Appeals acknowledged as much; it recognized that East Jefferson's market share alone was insufficient as a basis to infer market power, and buttressed its conclusion by relying on "market imperfections"[44] that permit petitioners to charge noncompetitive prices for hospital services: the prevalence of third-party payment for health care costs reduces price competition, and a lack of adequate information renders consumers unable to evaluate the quality of the medical care provided by competing hospitals. 686 F. 2d, at 290.[45] While these factors may generate "market power" in some abstract sense,[46] they do not generate the kind of market power that justifies condemnation of tying.

Tying arrangements need only be condemned if they restrain competition on the merits by forcing purchases that would not otherwise be made. A lack of price or quality

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in other antitrust contexts this Court has found that market shares comparable to that present here do not create an unacceptable likelihood of anticompetitive conduct. See *United States* v. *Connecticut National Bank*, 418 U. S. 656 (1974); *United States* v. *E. I. du Pont de Nemours & Co.*, 351 U. S. 377 (1956).

[44] The Court of Appeals acknowledged that absent these market imperfections, there was no basis for applying the *per se* rule against tying. "The contract at issue here involved only one hospital out of at least twenty in the area. Under the analysis applied to a truly competitive market, appellant has failed to prove an illegal tying arrangement." 686 F. 2d, at 290.

[45] Congress has found these market imperfections to exist. See *National Gerimedical Hospital* v. *Blue Cross*, 452 U. S., at 388, n. 13, 391–393, and n. 18; 42 U. S. C. §§300k, 300k–2(b); H. R. Conf. Rep. No. 96–420, pp. 57–58 (1979); S. Rep. No. 96–96, pp. 52–53 (1979).

[46] As an economic matter, market power exists whenever prices can be raised above the levels that would be charged in a competitive market. See *Fortner II*, 429 U. S., at 620; *Fortner I*, 394 U. S., at 503–504.

competition does not create this type of forcing. If consumers lack price consciousness, that fact will not force them to take an anesthesiologist whose services they do not want—their indifference to price will have no impact on their willingness or ability to go to another hospital where they can utilize the services of the anesthesiologist of their choice. Similarly, if consumers cannot evaluate the quality of anesthesiological services, it follows that they are indifferent between certified anesthesiologists even in the absence of a tying arrangement—such an arrangement cannot be said to have foreclosed a choice that would have otherwise been made "on the merits."

Thus, neither of the "market imperfections" relied upon by the Court of Appeals forces consumers to take anesthesiological services they would not select in the absence of a tie. It is safe to assume that every patient undergoing a surgical operation needs the services of an anesthesiologist; at least this record contains no evidence that the hospital "forced" any such services on unwilling patients.[47] The record therefore

[47] Nor is there an indication in the record that petitioners' practices have increased the social costs of their market power. Since patients' anesthesiological needs are fixed by medical judgment, respondent does not argue that the tying arrangement facilitates price discrimination. Where variable-quantity purchasing is unavailable as a means to enable price discrimination, commentators have seen less justification for condemning tying. See Dam, *supra* n. 23, at 15–17; Turner, *supra* n. 21, at 67–72. While tying arrangements like the one at issue here are unlikely to be used to facilitate price discrimination, they could have the similar effect of enabling hospitals "to evade price control in the tying product through clandestine transfer of the profit to the tied product. . . ." *Fortner I*, 394 U. S., at 513 (WHITE, J., dissenting). Insurance companies are the principal source of price restraint in the hospital industry; they place some limitations on the ability of hospitals to exploit their market power. Through this arrangement, petitioners may be able to evade that restraint by obtaining a portion of the anesthesiologists' fees and therefore realize a greater return than they could in the absence of the arrangement. This could also have an adverse effect on the anesthesiology market since it is possible that only less able anesthesiologists would be willing to give up

does not provide a basis for applying the *per se* rule against tying to this arrangement.

V

In order to prevail in the absence of *per se* liability, respondent has the burden of proving that the Roux contract violated the Sherman Act because it unreasonably restrained competition. That burden necessarily involves an inquiry into the actual effect of the exclusive contract on competition among anesthesiologists. This competition takes place in a market that has not been defined. The market is not necessarily the same as the market in which hospitals compete in offering services to patients; it may encompass competition among anesthesiologists for exclusive contracts such as the Roux contract and might be statewide or merely local.[48] There is, however, insufficient evidence in this record to provide a basis for finding that the Roux contract, as it actually operates in the market, has unreasonably restrained compe-

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part of their fees in return for the security of an exclusive contract. However, there are no findings of either the District Court or the Court of Appeals which indicate that this type of exploitation of market power has occurred here. The Court of Appeals found only that Roux's use of nurse anesthetists increased its and the hospital's profits, but there was no finding that nurse anesthetists might not be used with equal frequency absent the exclusive contract. Indeed, the District Court found that nurse anesthetists are utilized in all hospitals in the area. 513 F. Supp., at 537, 543. Moreover, there is nothing in the record which details whether this arrangement has enhanced the value of East Jefferson's market power or harmed quality competition in the anesthesiology market.

[48] While there was some rather impressionistic testimony that the prevalence of exclusive contracts tended to discourage young doctors from entering the market, the evidence was equivocal and neither the District Court nor the Court of Appeals made any findings concerning the contract's effect on entry barriers. Respondent does not press the point before this Court. It is possible that under some circumstances an exclusive contract could raise entry barriers since anesthesiologists could not compete for the contract without raising the capital necessary to run a hospitalwide operation. However, since the hospital has provided most of the capital for the exclusive contractor in this case, that problem does not appear to be present.

tition. The record sheds little light on how this arrangement affected consumer demand for separate arrangements with a specific anesthesiologist.[49] The evidence indicates that some surgeons and patients preferred respondent's services to those of Roux, but there is no evidence that any patient who was sophisticated enough to know the difference between two anesthesiologists was not also able to go to a hospital that would provide him with the anesthesiologist of his choice.[50]

In sum, all that the record establishes is that the choice of anesthesiologists at East Jefferson has been limited to one of the four doctors who are associated with Roux and therefore have staff privileges.[51] Even if Roux did not have an exclusive contract, the range of alternatives open to the patient would be severely limited by the nature of the transaction and the hospital's unquestioned right to exercise some control over the identity and the number of doctors to whom it accords staff privileges. If respondent is admitted to the staff of East Jefferson, the range of choice will be enlarged from

[49] While it is true that purchasers may not be fully sensitive to the price or quality implications of a tying arrangement, so that competition may be impeded, see n. 24, *supra*, this depends on an empirical demonstration concerning the effect of the arrangement on price or quality, and the record reveals little if anything about the effect of this arrangement on the market for anesthesiological services.

[50] If, as is likely, it is the patient's doctor and not the patient who selects an anesthesiologist, the doctor can simply take the patient elsewhere if he is dissatisfied with Roux. The District Court found that most doctors in the area have staff privileges at more than one hospital. 513 F. Supp., at 541.

[51] The effect of the contract, of course, has been to remove the East Jefferson Hospital from the market open to Roux's competitors. Like any exclusive-requirements contract, this contract could be unlawful if it foreclosed so much of the market from penetration by Roux's competitors as to unreasonably restrain competition in the affected market, the market for anesthesiological services. See generally *Tampa Electric Co.* v. *Nashville Coal Co.*, 365 U. S. 320 (1961); *Standard Oil Co. of California* v. *United States*, 337 U. S. 293 (1949). However, respondent has not attempted to make this showing.

four to five doctors, but the most significant restraints on the patient's freedom to select a specific anesthesiologist will nevertheless remain.[52] Without a showing of actual adverse effect on competition, respondent cannot make out a case under the antitrust laws, and no such showing has been made.

VI

Petitioners' closed policy may raise questions of medical ethics,[53] and may have inconvenienced some patients who would prefer to have their anesthesia administered by someone other than a member of Roux & Associates, but it does not have the obviously unreasonable impact on purchasers that has characterized the tying arrangements that this Court has branded unlawful. There is no evidence that the price, the quality, or the supply or demand for either the "tying product" or the "tied product" involved in this case has been adversely affected by the exclusive contract between Roux and the hospital. It may well be true that the contract made it necessary for Dr. Hyde and others to practice elsewhere, rather than at East Jefferson. But there has been no showing that the market as a whole has been affected at all by the contract. Indeed, as we previously noted, the record tells us very little about the market for the services of an-

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[52] The record simply tells us little if anything about the effect of this arrangement on price or quality of anesthesiological services. As to price, the arrangement did not lead to an increase in the price charged to the patient. 686 F. 2d, at 291. As to quality, the record indicates little more than that there have never been any complaints about the quality of Roux's services, and no contention that his services are in any respect inferior to those of respondent. Moreover, the self-interest of the hospital, as well as the ethical and professional norms under which it operates, presumably protect the quality of anesthesiological services. See Joint Commission on Accreditation of Hospitals, Accreditation Manual for Hospitals 3–10, 151–154 (1983).

[53] See App. A to Brief for American Society of Anesthesiologists, Inc., as *Amicus Curiae.*

esthesiologists. Yet that is the market in which the exclusive contract has had its principal impact. There is simply no showing here of the kind of restraint on competition that is prohibited by the Sherman Act. Accordingly, the judgment of the Court of Appeals is reversed, and the case is remanded to that court for further proceedings consistent with this opinion.[54]

It is so ordered.

JUSTICE BRENNAN, with whom JUSTICE MARSHALL joins, concurring.

As the opinion for the Court demonstrates, we have long held that tying arrangements are subject to evaluation for *per se* illegality under § 1 of the Sherman Act. Whatever merit the policy arguments against this longstanding construction of the Act might have, Congress, presumably aware of our decisions, has never changed the rule by amending the Act. In such circumstances, our practice usually has been to stand by a settled statutory interpretation and leave the task of modifying the statute's reach to Congress. See *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U. S. 752, 769 (1984) (BRENNAN, J., concurring). I see no reason to depart from that principle in this case and therefore join the opinion and judgment of the Court.

JUSTICE O'CONNOR, with whom THE CHIEF JUSTICE, JUSTICE POWELL, and JUSTICE REHNQUIST join, concurring in the judgment.

East Jefferson Hospital, a public hospital governed by petitioners, requires patients to use the anesthesiological services provided by Roux & Associates, as they are the only doctors authorized to administer anesthesia to patients in the hospital. The Court of Appeals found that this arrangement was a tie-in illegal under the Sherman Act. 686 F. 2d 286

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[54] The claims raised by respondent but not passed upon by the Court of Appeals remain open on remand. See n. 2, *supra*.

(CA5 1982). I concur in the Court's decision to reverse but write separately to explain why I believe the hospital-Roux contract, whether treated as effecting a tie between services provided to patients, or as an exclusive dealing arrangement between the hospital and certain anesthesiologists, is properly analyzed under the rule of reason.

I

Tying is a form of marketing in which a seller insists on selling two distinct products or services as a package. A supermarket that will sell flour to consumers only if they will also buy sugar is engaged in tying. Flour is referred to as the *tying* product, sugar as the *tied* product. In this case the allegation is that East Jefferson Hospital has unlawfully tied the sale of general hospital services and operating room facilities (the tying service) to the sale of anesthesiologists' services (the tied services). The Court has on occasion applied a *per se* rule of illegality in actions alleging tying in violation of § 1 of the Sherman Act. *International Salt Co.* v. *United States*, 332 U. S. 392 (1947).

Under the usual logic of the *per se* rule, a restraint on trade that rarely serves any purposes other than to restrain competition is illegal without proof of market power or anticompetitive effect. See, *e. g.*, *Northern Pacific R. Co.* v. *United States*, 356 U. S. 1, 5 (1958). In deciding whether an economic restraint should be declared illegal *per se*, "[t]he probability that anticompetitive consequences will result from a practice and the severity of those consequences [is] balanced against its procompetitive consequences. Cases that do not fit the generalization may arise, but a *per se* rule reflects the judgment that such cases are not sufficiently common or important to justify the time and expense necessary to identify them." *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 50, n. 16 (1977). See also *Arizona* v. *Maricopa County Medical Society*, 457 U. S. 332, 351 (1982). Only when there is very little loss to society from banning a restraint altogether is an inquiry into its costs in the individual case considered to be unnecessary.

Some of our earlier cases did indeed declare that tying arrangements serve "hardly any purpose beyond the suppression of competition." *Standard Oil Co. of California* v. *United States*, 337 U. S. 293, 305–306 (1949) (dictum). However, this declaration was not taken literally even by the cases that purported to rely upon it. In practice, a tie has been illegal only if the seller is shown to have "sufficient economic power with respect to the tying product to appreciably restrain free competition in the market for the tied product . . . ." *Northern Pacific R. Co.*, 356 U. S., at 6. Without "control or dominance over the tying product," the seller could not use the tying product as "an effectual weapon to pressure buyers into taking the tied item," so that any restraint of trade would be "insignificant." *Ibid.* The Court has never been willing to say of tying arrangements, as it has of price fixing, division of markets, and other agreements subject to *per se* analysis, that they are always illegal, without proof of market power or anticompetitive effect.

The *"per se"* doctrine in tying cases has thus always required an elaborate inquiry into the economic effects of the tying arrangement.[1] As a result, tying doctrine incurs the costs of a rule-of-reason approach without achieving its benefits: the doctrine calls for the extensive and time-consuming economic analysis characteristic of the rule of reason, but then may be interpreted to prohibit arrangements that economic analysis would show to be beneficial. Moreover, the *per se* label in the tying context has generated more confusion

[1] This inquiry has been required in analyzing both the prima facie case and affirmative defenses. Most notably, *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545, 559–560 (ED Pa. 1960), aff'd *per curiam*, 365 U. S. 567 (1961), upheld a requirement that buyers of television systems purchase the complete system, as well as installation and repair service, on the grounds that the tie assured that the systems would operate and thereby protected the seller's business reputation.

than coherent law because it appears to invite lower courts to omit the analysis of economic circumstances of the tie that has always been a necessary element of tying analysis.

The time has therefore come to abandon the *"per se"* label and refocus the inquiry on the adverse economic effects, and the potential economic benefits, that the tie may have. The law of tie-ins will thus be brought into accord with the law applicable to all other allegedly anticompetitive economic arrangements, except those few horizontal or quasi-horizontal restraints that can be said to have no economic justification whatsoever.[2] This change will rationalize rather than abandon tie-in doctrine as it is already applied.

II

Our prior opinions indicate that the purpose of tying law has been to identify and control those tie-ins that have a demonstrable exclusionary impact in the tied-product market, see *Times-Picayune Publishing Co.* v. *United States*, 345 U. S. 594, 605 (1953), or that abet the harmful exercise of market power that the seller possesses in the tying product market.[3] Under the rule of reason tying arrangements should be disapproved only in such instances.

Market power in the *tying* product may be acquired legitimately (*e. g.*, through the grant of a patent) or illegitimately (*e. g.*, as a result of unlawful monopolization). In either event, exploitation of consumers in the market for the tying

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[2] Tying law is particularly anomalous in this respect because arrangements largely indistinguishable from tie-ins are generally analyzed under the rule of reason. For example, the *"per se"* analysis of tie-ins subjects restrictions on a franchisee's freedom to purchase supplies to a more searching scrutiny than restrictions on his freedom to sell his products. Compare, *e. g.*, *Siegel* v. *Chicken Delight, Inc.*, 448 F. 2d 43 (CA9 1971), cert. denied, 405 U. S. 955 (1972), with *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36 (1977). And exclusive contracts that, like tie-ins, require the buyer to purchase a product from one seller are subject only to the rule of reason. See *infra*, at 44–45.

[3] See n. 4, *infra*.

product is a possibility that exists and that may be regulated under § 2 of the Sherman Act without reference to any tying arrangements that the seller may have developed. The existence of a tied product normally does not increase the profit that the seller with market power can extract from sales of the *tying* product. A seller with a monopoly on flour, for example, cannot increase the profit it can extract from flour consumers simply by forcing them to buy sugar along with their flour. Counterintuitive though that assertion may seem, it is easily demonstrated and widely accepted. See, *e. g.*, R. Bork, The Antitrust Paradox 372–374 (1978); P. Areeda, Antitrust Analysis 735 (3d ed. 1981).

Tying may be economically harmful primarily in the rare cases where power in the market for the tying product is used to create *additional* market power in the market for the *tied* product.[4] The antitrust law is properly concerned with

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[4] Tying might be undesirable in two other instances, but the hospital-Roux arrangement involves neither one.

In a regulated industry a firm with market power may be unable to extract a supercompetitive profit because it lacks control over the prices it charges for regulated products or services. Tying may then be used to extract that profit from sale of the unregulated, tied products or services. See *Fortner Enterprises, Inc.* v. *United States Steel Corp.*, 394 U. S. 495, 513 (1969) (WHITE, J., dissenting).

Tying may also help the seller engage in price discrimination by "metering" the buyer's use of the tying product. Cf. *International Business Machines Corp.* v. *United States*, 298 U. S. 131 (1936); *International Salt Co.* v. *United States*, 332 U. S. 392 (1947). Price discrimination may be independently unlawful, see 15 U. S. C. § 13. Price discrimination may, however, *decrease* rather than increase the economic costs of a seller's market power. See, *e. g.*, R. Bork, The Antitrust Paradox 398 (1978); P. Areeda, Antitrust Analysis 608–610 (3d ed. 1981); O. Williamson, Markets and Hierarchies: Analysis and Antitrust Implications 11–13 (1975). *United States Steel Corp.* v. *Fortner Enterprises, Inc.*, 429 U. S. 610, 617 (1977) *(Fortner II)*, did not hold that price discrimination in the form of a tie-in is always economically harmful; that case indicated only that price discrimination may indicate market power in the tying-product market. But there is no need in this case to address the problem of price discrimination facilitated by tying. The discussion herein is aimed only at tying arrangements as to which no price discrimination is alleged.

tying when, for example, the flour monopolist threatens to use its market power to acquire additional power in the sugar market, perhaps by driving out competing sellers of sugar, or by making it more difficult for new sellers to enter the sugar market. But such extension of market power is unlikely, or poses no threat of economic harm, unless the two markets in question and the nature of the two products tied satisfy three threshold criteria.[5]

First, the seller must have power in the tying-product market.[6] Absent such power tying cannot conceivably have any adverse impact in the tied-product market, and can be only procompetitive in the tying-product market.[7] If the

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[5] Wholly apart from market characteristics, a prerequisite to application of the Sherman Act is an effect on interstate commerce. See, *e. g.*, *McLain* v. *Real Estate Board of New Orleans*, 444 U. S. 232, 246 (1980); *Burke* v. *Ford*, 389 U. S. 320, 322 (1967). It is not disputed that such an impact is present here.

[6] The Court has failed in the past to define how much market power is necessary, but in the context of this case it is inappropriate to attempt to resolve that question. In *International Salt Co.* v. *United States*, *supra*, the Court assumed that a patent conferred market power and therefore sufficiently established "the tendency of the arrangement to accomplishment of monopoly." *Id.*, at 396. In its next tying case, *Times-Picayune Publishing Co.* v. *United States*, 345 U. S. 594 (1953), the Court distinguished *International Salt* in part by finding that there was no market "dominance," 345 U. S., at 610–613, after a careful consideration of the relevant market. Then, in *Northern Pacific R. Co.* v. *United States*, 356 U. S. 1, 6–8, 11 (1958), the Court required only a minimal showing of market power. More recently, in *Fortner II*, *supra*, the Court conducted a more extensive analysis of whether the tie was actually an exercise of market power, considering such factors as the size and profitability of the firm seeking to impose the tie, the character of the tying product, and the effects of the tie—the price charged for the products, the number of customers affected, the functional relation between the tied and tying product.

[7] A common misconception has been that a patent or copyright, a high market share, or a unique product that competitors are not able to offer suffices to demonstrate market power. While each of these three factors might help to give market power to a seller, it is also possible that a seller in these situations will have no market power: for example, a patent holder has no market power in any relevant sense if there are close substitutes for the patented product. Similarly, a high market share indicates market

seller of flour has no market power over flour, it will gain none by insisting that its buyers take some sugar as well. See *United States Steel Corp.* v. *Fortner Enterprises, Inc.*, 429 U. S. 610, 620 (1977) *(Fortner II); Fortner Enterprises, Inc.* v. *United States Steel Corp.*, 394 U. S. 495, 503–504 (1969) *(Fortner I); United States* v. *Loew's Inc.*, 371 U. S. 38, 45, 48, n. 5 (1962); *Northern Pacific R. Co.* v. *United States*, 356 U. S., at 6–7.

Second, there must be a substantial threat that the tying seller will acquire market power in the tied-product market. No such threat exists if the tied-product market is occupied by many stable sellers who are not likely to be driven out by the tying, or if entry barriers in the tied-product market are low. If, for example, there is an active and vibrant market for sugar—one with numerous sellers and buyers who do not deal in flour—the flour monopolist's tying of sugar to flour need not be declared unlawful. Cf. *Fortner II, supra,* at 617–618, and n. 8; *Fortner I, supra,* at 498–499; *Times-Picayune Publishing Co.* v. *United States*, 345 U. S., at 611; *Standard Oil Co. of California* v. *United States*, 337 U. S., at 305–306; *International Salt Co.* v. *United States*, 332

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power only if the market is properly defined to include all reasonable substitutes for the product. See generally Landes & Posner, Market Power in Antitrust Cases, 94 Harv. L. Rev. 937 (1981).

Nor does any presumption of market power find support in our prior cases. Although *United States* v. *Paramount Pictures, Inc.*, 334 U. S. 131 (1948), considered the legality of "block-booking" of motion pictures, which ties the purchase of rights to copyrighted motion pictures to purchase of other motion pictures of the same copyright holder, the Court did not analyze the arrangement with the schema of the tying cases. Rather, the Court borrowed the patent law principle of "patent misuse," which prevents the holder of a patent from using the patent to require his customers to purchase unpatented products. *Id.*, at 156–159. See, *e. g., Mercoid Corp.* v. *Mid-Continent Investment Co.*, 320 U. S. 661, 665 (1944). The "patent misuse" doctrine may have influenced the Court's willingness to strike down the arrangement at issue in *International Salt* as well, although the Court did not cite the doctrine in that case.

U. S., at 396. If, on the other hand, the tying arrangement is likely to erect significant barriers to entry into the tied-product market, the tie remains suspect. *Atlantic Refining Co.* v. *FTC*, 381 U. S. 357, 371 (1965).

Third, there must be a coherent economic basis for treating the tying and tied products as distinct. All but the simplest products can be broken down into two or more components that are "tied together" in the final sale. Unless it is to be illegal to sell cars with engines or cameras with lenses, this analysis must be guided by some limiting principle. For products to be treated as distinct, the tied product must, at a minimum, be one that some consumers might wish to purchase separately *without also purchasing the tying product.*[8] When the tied product has no use other than in conjunction with the tying product, a seller of the tying product can acquire no *additional* market power by selling the two products together. If sugar is useless to consumers except when used with flour, the flour seller's market power is projected into the sugar market whether or not the two products are actually sold together; the flour seller can exploit what market power it has over flour with or without the tie.[9] The flour seller will therefore have little incentive to monopolize the sugar market unless it can produce and distribute sugar more cheaply than other sugar sellers. And in this unusual case, where flour is monopolized and sugar is useful only when

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[8] Whether the tying product is one that consumers might wish to purchase without the tied product should be irrelevant. Once it is conceded that the seller has market power over the tying product it follows that the seller can sell the tying product on noncompetitive terms. The injury to consumers does not depend on whether the seller chooses to charge a supercompetitive price, or charges a competitive price but insists that consumers also buy a product that they do not want.

[9] Cf. Areeda, *supra* n. 4, at 735; Ross, The Single Product Issue in Antitrust Tying: A Functional Approach, 23 Emory L. J. 963, 1010 (1974); Bowman, Tying Arrangements and the Leverage Problem, 67 Yale L. J. 19, 21–23 (1957).

used with flour, consumers will suffer no further economic injury by the monopolization of the sugar market.

Even when the tied product does have a use separate from the tying product, it makes little sense to label a package as two products without also considering the economic justifications for the sale of the package as a unit. When the economic advantages of joint packaging are substantial the package is not appropriately viewed as two products, and that should be the end of the tying inquiry. The lower courts largely have adopted this approach.[10] See, *e. g., Foster* v. *Maryland State Savings and Loan Assn.*, 191 U. S. App. D. C. 226, 228–231, 590 F. 2d 928, 930–933 (1978), cert. denied, 439 U. S. 1071 (1979); *Response of Carolina, Inc.* v. *Leasco Response, Inc.*, 537 F. 2d 1307, 1330 (CA5 1976); *Kugler* v. *AAMCO Automatic Transmissions, Inc.*, 460 F. 2d 1214 (CA8 1972); *ILC Peripherals Leasing Corp.* v. *International Business Machines Corp.*, 448 F. Supp. 228, 230

[10] The examination of the economic advantages of tying may properly be conducted as part of the rule-of-reason analysis, rather than at the threshold of the tying inquiry. This approach is consistent with this Court's occasional references to the problem. The Court has not heretofore had occasion to set forth any general criteria for determining when two apparently separate products are components of a single product for tying analysis. In *Times-Picayune Publishing Co.*, the Court held that advertising space in a morning newspaper was the same product as advertising space in the evening newspaper—access to readership of the respective newspapers—because the subscribers had no reason to distinguish among the readers of the two papers. 345 U. S., at 613–616. In *Fortner I*, the Court, reversing the grant of a motion for summary judgment, rejected the contention that credit could never be separate from the product for whose purchase credit was extended. 394 U. S., at 506–507. The Court disclaimed any determination of "the standards for determining exactly when a transaction involves only a single product." *Id.*, at 507. These cases indicate that consideration of whether a buyer might prefer to purchase one component without the other is one of the factors in tying analysis and, more generally, that economic analysis rather than mere conventional separability into different markets should determine whether one or two products are involved in the alleged tie.

(ND Cal. 1978); *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545, 563 (ED Pa. 1960), aff'd *per curiam*, 365 U. S. 567 (1961).

These three conditions—market power in the tying product, a substantial threat of market power in the tied product, and a coherent economic basis for treating the products as distinct—are only threshold requirements. Under the rule of reason a tie-in may prove acceptable even when all three are met. Tie-ins may entail economic benefits as well as economic harms, and if the threshold requirements are met these benefits should enter the rule-of-reason balance.

> "[Tie-ins] may facilitate new entry into fields where established sellers have wedded their customers to them by ties of habit and custom. *Brown Shoe Co.* v. *United States*, 370 U. S. 294, 330 (1962) . . . . They may permit clandestine price cutting in products which otherwise would have no price competition at all because of fear of retaliation from the few other producers dealing in the market. They may protect the reputation of the tying product if failure to use the tied product in conjunction with it may cause it to misfunction. . . . [Citing] *Pick Mfg. Co.* v. *General Motors Corp.*, 80 F. 2d 641 (C. A. 7th Cir. 1935), aff'd, 299 U. S. 3 (1936). And, if the tied and tying products are functionally related, they may reduce costs through economies of joint production and distribution." *Fortner I*, 394 U. S., at 514, n. 9 (WHITE, J., dissenting).

The ultimate decision whether a tie-in is illegal under the antitrust laws should depend upon the demonstrated economic effects of the challenged agreement. It may, for example, be entirely innocuous that the seller exploits its control over the tying product to "force" the buyer to purchase the tied product. For when the seller exerts market power only in the tying-product market, it makes no difference to him or his customers whether he exploits that power by raising the price of the tying product or by "forcing" customers to buy a tied product. See Markovits, Tie-Ins, Reciprocity and the Leverage Theory, 76 Yale L. J. 1397, 1397–1398 (1967); Burstein, A Theory of Full-Line Forcing, 55 Nw. U. L. Rev. 62, 62–63 (1960). On the other hand, tying may make the provision of packages of goods and services more efficient. A tie-in should be condemned only when its anticompetitive impact outweighs its contribution to efficiency.

III

Application of these criteria to the case at hand is straightforward.

Although the issue is in doubt, we may assume that the hospital does have market power in the provision of hospital services in its area. The District Court found to the contrary, 513 F. Supp. 532, 541 (ED La. 1981), but the Court of Appeals determined that the hospital does possess market power in an appropriately defined market. While appellate courts should normally defer to the district courts' findings on such fact-bound questions,[11] I shall assume for the purposes of this discussion that the Court of Appeals' determination that the hospital does have some power in the provision of hospital services in its local market is accepted.

Second, in light of the hospital's presumed market power, we may also assume that there is a substantial threat that East Jefferson will acquire market power over the provision of anesthesiological services in its market. By tying the sale of anesthesia to the sale of other hospital services the hospital can drive out other sellers of those services who might otherwise operate in the local market. The hospital may thus gain local market power in the provision of anesthesiology: anesthesiological services offered in the hospital's market, narrowly defined, will be purchased only from Roux, under the hospital's auspices.

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[11] See Fed. Rule Civ. Proc. 52(a); *Inwood Laboratories, Inc.* v. *Ives Laboratories, Inc.*, 456 U. S. 844, 855–858 (1982).

But the third threshold condition for giving closer scrutiny to a tying arrangement is not satisfied here: there is no sound economic reason for treating surgery and anesthesia as separate services. Patients are interested in purchasing anesthesia only in conjunction with hospital services,[12] so the hospital can acquire no *additional* market power by selling the two services together. Accordingly, the link between the hospital's services and anesthesia administered by Roux will affect neither the amount of anesthesia provided nor the combined price of anesthesia and surgery for those who choose to become the hospital's patients. In these circumstances, anesthesia and surgical services should probably not be characterized as distinct products for tying purposes.

Even if they are, the tying should not be considered a violation of § 1 of the Sherman Act because tying here cannot increase the seller's already absolute power over the volume of production of the tied product, which is an inevitable consequence of the fact that very few patients will choose to undergo surgery without receiving anesthesia. The hospital-Roux contract therefore has little potential to harm the patients. On the other side of the balance, the District Court found, and the Court of Appeals did not dispute, that the tie-in conferred significant benefits upon the hospital and the patients that it served.

The tie-in improves patient care and permits more efficient hospital operation in a number of ways. From the viewpoint of hospital management, the tie-in ensures 24-hour anesthesiology coverage, aids in standardization of procedures and efficient use of equipment, facilitates flexible scheduling of operations, and permits the hospital more effectively to monitor the quality of anesthesiological services. Further, the tying arrangement is advantageous to patients because, as the District Court found, the closed anesthesiology depart-

[12] While the record appears to be devoid of factual findings on this point the assumption is a safe one, and certainly one that finds no contradiction in the record.

ment places upon the hospital, rather than the individual patient, responsibility to select the physician who is to provide anesthesiological services. The hospital also assumes the responsibility that the anesthesiologist will be available, will be acceptable to the surgeon, and will provide suitable care to the patient. In assuming these responsibilities—responsibilities that a seriously ill patient frequently may be unable to discharge—the hospital provides a valuable service to its patients. And there is no indication that patients were dissatisfied with the quality of anesthesiology that was provided at the hospital or that patients wished to enjoy the services of anesthesiologists other than those that the hospital employed. Given this evidence of the advantages and effectiveness of the closed anesthesiology department, it is not surprising that, as the District Court found, such arrangements are accepted practice in the majority of hospitals of New Orleans and in the health care industry generally. Such an arrangement, which has little anticompetitive effect and achieves substantial benefits in the provision of care to patients, is hardly one that the antitrust law should condemn.[13] This conclusion reaffirms our threshold determination that the joint provision of hospital services and anesthesiology should not be viewed as involving a tie between distinct products, and therefore should require no additional scrutiny under the antitrust law.

IV

Whether or not the hospital-Roux contract is characterized as a tie between distinct products, the contract unquestionably does constitute exclusive dealing. Exclusive-dealing arrangements are independently subject to scrutiny under § 1 of the Sherman Act, and are also analyzed under the rule of

[13] The Court of Appeals disregarded the benefits of the tie because it found that there were less restrictive means of achieving them. In the absence of an adequate basis to expect any harm to competition from the tie-in, this objection is simply irrelevant.

reason. *Tampa Electric Co.* v. *Nashville Coal Co.*, 365 U. S. 320, 333–335 (1961).

The hospital-Roux arrangement could conceivably have an adverse effect on horizontal competition among anesthesiologists, or among hospitals. Dr. Hyde, who competes with the Roux anesthesiologists, and other hospitals in the area, who compete with East Jefferson, may have grounds to complain that the exclusive contract stifles horizontal competition and therefore has an adverse, albeit indirect, impact on consumer welfare even if it is not a tie.

Exclusive-dealing arrangements may, in some circumstances, create or extend market power of a supplier or the purchaser party to the exclusive-dealing arrangement, and may thus restrain horizontal competition. Exclusive dealing can have adverse economic consequences by allowing one supplier of goods or services unreasonably to deprive other suppliers of a market for their goods, or by allowing one buyer of goods unreasonably to deprive other buyers of a needed source of supply. In determining whether an exclusive-dealing contract is unreasonable, the proper focus is on the structure of the market for the products or services in question—the number of sellers and buyers in the market, the volume of their business, and the ease with which buyers and sellers can redirect their purchases or sales to others. Exclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal. *Standard Oil Co. of California* v. *United States*, 337 U. S. 293 (1949). When the sellers of services are numerous and mobile, and the number of buyers is large, exclusive-dealing arrangements of narrow scope pose no threat of adverse economic consequences. To the contrary, they may be substantially procompetitive by ensuring stable markets and encouraging long-term, mutually advantageous business relationships.

At issue here is an exclusive-dealing arrangement between a firm of four anesthesiologists and one relatively small hospital. There is no suggestion that East Jefferson Hospital is likely to create a "bottleneck" in the availability of anesthesiologists that might deprive other hospitals of access to needed anesthesiological services, or that the Roux associates have unreasonably narrowed the range of choices available to other anesthesiologists in search of a hospital or patients that will buy their services. Cf. *Associated Press* v. *United States*, 326 U. S. 1 (1945). A firm of four anesthesiologists represents only a very small fraction of the total number of anesthesiologists whose services are available for hire by other hospitals, and East Jefferson is one among numerous hospitals buying such services. Even without engaging in a detailed analysis of the size of the relevant markets we may readily conclude that there is no likelihood that the exclusive-dealing arrangement challenged here will either unreasonably enhance the hospital's market position relative to other hospitals, or unreasonably permit Roux to acquire power relative to other anesthesiologists. Accordingly, this exclusive-dealing arrangement must be sustained under the rule of reason.

V

For these reasons I conclude that the hospital-Roux contract does not violate § 1 of the Sherman Act. Since anesthesia is a service useful to consumers only when purchased in conjunction with hospital services, the arrangement is not properly characterized as a tie between distinct products. It threatens no additional economic harm to consumers beyond that already made possible by any market power that the hospital may possess. The fact that anesthesia is used only together with other hospital services is sufficient, standing alone, to insulate from attack the hospital's decision to tie the two types of service.

Whether or not this case involves tying of distinct products, the hospital-Roux contract is subject to scrutiny under the rule of reason as an exclusive-dealing arrangement. Plainly, however, the arrangement forecloses only a small fraction of the markets in which anesthesiologists may sell their services, and a still smaller fraction of the market in which hospitals may secure anesthesiological services. The contract therefore survives scrutiny under the rule of reason.

The judgment of the Court of Appeals for the Fifth Circuit should be reversed, and the case should be remanded for any further proceedings on respondent's remaining claims. See *ante*, at 5, n. 2.

Syllabus

EASTMAN KODAK CO. *v.* IMAGE TECHNICAL SERVICES, INC., ET AL.

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 90–1029. Argued December 10, 1991—Decided June 8, 1992

After respondent independent service organizations (ISO's) began servicing copying and micrographic equipment manufactured by petitioner Eastman Kodak Co., Kodak adopted policies to limit the availability to ISO's of replacement parts for its equipment and to make it more difficult for ISO's to compete with it in servicing such equipment. Respondents then filed this action, alleging, *inter alia,* that Kodak had unlawfully tied the sale of service for its machines to the sale of parts, in violation of § 1 of the Sherman Act, and had unlawfully monopolized and attempted to monopolize the sale of service and parts for such machines, in violation of § 2 of that Act. The District Court granted summary judgment for Kodak, but the Court of Appeals reversed. Among other things, the appellate court found that respondents had presented sufficient evidence to raise a genuine issue concerning Kodak's market power in the service and parts markets, and rejected Kodak's contention that lack of market power in service and parts must be assumed when such power is absent in the equipment market.

Held:

1. Kodak has not met the requirements of Federal Rule of Civil Procedure 56(c) for an award of summary judgment on the § 1 claim. Pp. 461–479.

(a) A tying arrangement—*i. e.*, an agreement by a party to sell one product on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier—violates § 1 only if the seller has appreciable economic power in the tying product market. Pp. 461–462.

(b) Respondents have presented sufficient evidence of a tying arrangement to defeat a summary judgment motion. A reasonable trier of fact could find, first, that service and parts are two distinct products in light of evidence indicating that each has been, and continues in some circumstances to be, sold separately, and, second, that Kodak has tied the sale of the two products in light of evidence indicating that it would sell parts to third parties only if they agreed not to buy service from ISO's. Pp. 462–463.

(c) For purposes of determining appreciable economic power in the tying market, this Court's precedents have defined market power as the power to force a purchaser to do something that he would not do in a competitive market, and have ordinarily inferred the existence of such power from the seller's possession of a predominant share of the market. P. 464.

(d) Respondents would be entitled under such precedents to a trial on their claim that Kodak has sufficient power in the parts market to force unwanted purchases of the tied service market, based on evidence indicating that Kodak has control over the availability of parts and that such control has excluded service competition, boosted service prices, and forced unwilling consumption of Kodak service. Pp. 464–465.

(e) Kodak has not satisfied its substantial burden of showing that, despite such evidence, an inference of market power is unreasonable. Kodak's theory that its lack of market power in the primary equipment market precludes—as a matter of law—the possibility of market power in the derivative aftermarkets rests on the factual assumption that if it raised its parts or service prices above competitive levels, potential customers would simply stop buying its equipment. Kodak's theory does not accurately describe actual market behavior, since there is no evidence or assertion that its equipment sales dropped after it raised its service prices. Respondents offer a forceful reason for this discrepancy: the existence of significant information and switching costs that could create a less responsive connection between aftermarket prices and equipment sales. It is plausible to infer from respondents' evidence that Kodak chose to gain immediate profits by exerting market power where locked-in customers, high information costs, and discriminatory pricing limited, and perhaps eliminated, any long-term loss. Pp. 465–478.

(f) Nor is this Court persuaded by Kodak's contention that it is entitled to a legal presumption on the lack of market power because there is a significant risk of deterring procompetitive conduct. Because Kodak's service and parts policy is not one that appears always, or almost always, to enhance competition, the balance tips against summary judgment. Pp. 478–479.

2. Respondents have presented genuine issues for trial as to whether Kodak has monopolized, or attempted to monopolize, the service and parts markets in violation of § 2. Pp. 480–486.

(a) Respondents' evidence that Kodak controls nearly 100% of the parts market and 80% to 95% of the service market, with no readily available substitutes, is sufficient to survive summary judgment on the first element of the monopoly offense, the possession of monopoly power. Kodak's contention that, as a matter of law, a single brand of a product or service can never be a relevant market contravenes cases of this Court indicating that one brand of a product can constitute a separate market in some instances. The proper market definition in this case can be determined only after a factual inquiry into the commercial realities faced by Kodak equipment owners. Pp. 481–482.

(b) As to the second element of a § 2 claim, the willful use of monopoly power, respondents have presented evidence that Kodak took exclusionary action to maintain its parts monopoly and used its control over parts to strengthen its monopoly share of the service market. Thus, liability turns on whether valid business reasons can explain Kodak's actions. However, none of its asserted business justifications—a commitment to quality service, a need to control inventory costs, and a desire to prevent ISO's from free-riding on its capital investment—are sufficient to prove that it is entitled to a judgment as a matter of law. Pp. 482–486.

903 F. 2d 612, affirmed.

Blackmun, J., delivered the opinion of the Court, in which Rehnquist, C. J., and White, Stevens, Kennedy, and Souter, JJ., joined. Scalia, J., filed a dissenting opinion, in which O'Connor and Thomas, JJ., joined, *post,* p. 486.

Donn P. Pickett argued the cause for petitioner. With him on the briefs were *Daniel M. Wall, Alfred C. Pfeiffer, Jr.,* and *Jonathan W. Romeyn.*

Assistant Attorney General Rill argued the cause for the United States as *amicus curiae* urging reversal. With him on the brief were *Solicitor General Starr, Deputy Solicitor General Wallace, Christopher J. Wright, Catherine G. O'Sullivan,* and *Robert B. Nicholson.*

James A. Hennefer argued the cause for respondents. With him on the brief were *A. Kirk McKenzie, Douglas E. Rosenthal, Jonathan M. Jacobson,* and *Elinor R. Hoffmann.**

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*Briefs of *amici curiae* urging reversal were filed for the Computer and Business Equipment Manufacturers Association by *Simon Lazarus III;* for Digital Equipment Corp. et al. by *Kurt W. Melchior, Robert A. Skitol, James A. Meyers, Marcia Howe Adams, Ivor Cary Armistead III, Ronald A. Stern, Stephen Wasinger, James W. Olson, Carter G. Phillips, Ralph I. Miller,* and *Florinda J. Iascone;* for the Motor Vehicle Manufacturers Association of the United States, Inc., by *Thomas B. Leary, William H.*

JUSTICE BLACKMUN delivered the opinion of the Court.

This is yet another case that concerns the standard for summary judgment in an antitrust controversy. The

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Crabtree, and *Charles H. Lockwood II;* and for the National Electrical Manufacturers Association by *James S. Dittmar* and *James L. Messenger.*

Briefs of *amici curiae* urging affirmance were filed for the State of Ohio et al. by *Lee Fisher,* Attorney General of Ohio, *Simon Karas,* and *Elizabeth H. Watts* and *Marc B. Bandman,* Assistant Attorneys General, *James H. Evans,* Attorney General of Alabama, and *Marc Givhan,* Assistant Attorney General, *Charles E. Cole,* Attorney General of Alaska, and *James Forbes,* Assistant Attorney General, *Grant Woods,* Attorney General of Arizona, and *Jeri K. Auther,* Assistant Attorney General, *Winston Bryant,* Attorney General of Arkansas, and *Royce Griffin,* Deputy Attorney General, *Daniel E. Lungren,* Attorney General of California, *Roderick E. Walston,* Chief Assistant Attorney General, *Sanford N. Gruskin,* Assistant Attorney General, and *Kathleen E. Foote,* Deputy Attorney General, *Richard Blumenthal,* Attorney General of Connecticut, and *Robert M. Langer,* Assistant Attorney General, *Robert A. Butterworth,* Attorney General of Florida, and *Jerome W. Hoffman,* Assistant Attorney General, *Warren Price III,* Attorney General of Hawaii, *Robert A. Marks,* Supervising Deputy Attorney General, and *Ted Clause,* Deputy Attorney General, *Larry EchoHawk,* Attorney General of Idaho, *Roland W. Burris,* Attorney General of Illinois, *Rosalyn Kaplan,* Solicitor General, and *Christine Rosso,* Senior Assistant Attorney General, *Bonnie J. Campbell,* Attorney General of Iowa, and *John R. Perkins,* Deputy Attorney General, *Robert T. Stephan,* Attorney General of Kansas, and *Mary Ann Heckman,* Assistant Attorney General, *Frederic J. Cowan,* Attorney General of Kentucky, and *James M. Ringo,* Assistant Attorney General, *William J. Guste, Jr.,* Attorney General of Louisiana, and *Anne F. Benoit,* Assistant Attorney General, *Michael E. Carpenter,* Attorney General of Maine, and *Stephen L. Wessler,* Deputy Attorney General, *J. Joseph Curran, Jr.,* Attorney General of Maryland, and *Robert N. McDonald* and *Ellen S. Cooper,* Assistant Attorneys General, *Scott Harshbarger,* Attorney General of Massachusetts, and *George K. Weber,* Assistant Attorney General, *Frank J. Kelley,* Attorney General of Michigan, *Hubert H. Humphrey III,* Attorney General of Minnesota, *Thomas F. Pursell,* Deputy Attorney General, and *James P. Spencer* and *Susan C. Gretz,* Special Assistant Attorneys General, *Frankie Sue Del Pappa,* Attorney General of Nevada, and *Rob Kirkman,* Deputy Attorney General, *Robert J. Del Tufo,* Attorney General of New Jersey, and *Laurel A. Price,* Deputy Attorney General, *Robert Abrams,* Attorney General of New York, *O. Peter Sherwood,* Soliciprincipal issue here is whether a defendant's lack of market power in the primary equipment market precludes—as a matter of law—the possibility of market power in derivative aftermarkets.

Petitioner Eastman Kodak Company manufactures and sells photocopiers and micrographic equipment. Kodak also sells service and replacement parts for its equipment. Respondents are 18 independent service organizations (ISO's) that in the early 1980's began servicing Kodak copying and micrographic equipment. Kodak subsequently adopted policies to limit the availability of parts to ISO's and to make it more difficult for ISO's to compete with Kodak in servicing Kodak equipment.

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tor General, and *George W. Sampson,* Assistant Attorney General, *Lacy H. Thornburg,* Attorney General of North Carolina, *James C. Gulick,* Special Deputy Attorney General, and *K. D. Sturgis,* Assistant Attorney General, *Dan Morales,* Attorney General of Texas, *Will Pryor,* First Assistant Attorney General, *Mary F. Keller,* Deputy Attorney General, and *Mark Tobey,* Assistant Attorney General, *R. Paul Van Dam,* Attorney General of Utah, and *Arthur M. Strong,* Assistant Attorney General, *Jeffrey L. Amestoy,* Attorney General of Vermont, and *Geoff Yudien,* Assistant Attorney General, *Kenneth O. Eikenberry,* Attorney General of Washington, and *Carol A. Smith,* Assistant Attorney General, and *Mario J. Palumbo,* Attorney General of West Virginia, and *Donna S. Quesenberry,* Assistant Attorney General; for the Automotive Warehouse Distributors Association et al. by *Donald A. Randall, Louis R. Marchese, Robert J. Verdisco,* and *Basil J. Mezines;* for Bell Atlantic Business Systems Services, Inc., by *Richard G. Taranto, Joel I. Klein,* and *John M. Kelleher;* for Grumman Corporation by *Patrick O. Killian;* for the National Association of State Purchasing Officials et al. by *Richard D. Monkman;* for the National Office Machine Dealers Association et al. by *Mark P. Cohen;* for the National Retail Federation by *Michael J. Altier;* for Public Citizen by *Alan B. Morrison;* for State Farm Mutual Automobile Insurance Co. et al. by *Melvin Spaeth, James F. Fitzpatrick,* and *Melvin C. Garbow.*

Briefs of *amici curiae* were filed for the California State Electronics Association et al. by *Richard I. Fine;* for Computer Service Network International by *Ronald S. Katz;* and for the National Electronics Sales and Service Dealers Association by *Ronald S. Katz.*

Respondents instituted this action in the United States District Court for the Northern District of California, alleging that Kodak's policies were unlawful under both § 1 and § 2 of the Sherman Act, 26 Stat. 209, as amended, 15 U. S. C. §§ 1 and 2 (1988 ed., Supp. II). After truncated discovery, the District Court granted summary judgment for Kodak. The Court of Appeals for the Ninth Circuit reversed. The appellate court found that respondents had presented sufficient evidence to raise a genuine issue concerning Kodak's market power in the service and parts markets. It rejected Kodak's contention that lack of market power in service and parts must be assumed when such power is absent in the equipment market. Because of the importance of the issue, we granted certiorari. 501 U. S. 1216 (1991).

I

A

Because this case comes to us on petitioner Kodak's motion for summary judgment, "[t]he evidence of [respondents] is to be believed, and all justifiable inferences are to be drawn in [their] favor." *Anderson* v. *Liberty Lobby, Inc.*, 477 U. S. 242, 255 (1986); *Matsushita Electric Industrial Co.* v. *Zenith Radio Corp.*, 475 U. S. 574, 587 (1986). Mindful that respondents' version of any disputed issue of fact thus is presumed correct, we begin with the factual basis of respondents' claims. See *Arizona* v. *Maricopa County Medical Society*, 457 U. S. 332, 339 (1982).

Kodak manufactures and sells complex business machines—as relevant here, high-volume photocopiers and micrographic equipment.[1] Kodak equipment is unique; micro-

[1] Kodak's micrographic equipment includes four different product areas. The first is capture products such as microfilmers and electronic scanners, which compact an image and capture it on microfilm. The second is equipment such as microfilm viewers and viewer/printers. This equipment is used to retrieve the images. The third is Computer Output Microform (COM) recorders, which are data-processing peripherals that record

graphic software programs that operate on Kodak machines, for example, are not compatible with competitors' machines. See App. 424–425, 487–489, 537. Kodak parts are not compatible with other manufacturers' equipment, and vice versa. See *id.*, at 432, 413–415. Kodak equipment, although expensive when new, has little resale value. See *id.*, at 358–359, 424–425, 427–428, 467, 505–506, 519–521.

Kodak provides service and parts for its machines to its customers. It produces some of the parts itself; the rest are made to order for Kodak by independent original-equipment manufacturers (OEM's). See *id.*, at 429, 465, 490, 496. Kodak does not sell a complete system of original equipment, lifetime service, and lifetime parts for a single price. Instead, Kodak provides service after the initial warranty period either through annual service contracts, which include all necessary parts, or on a per-call basis. See *id.*, at 98–99; Brief for Petitioner 3. It charges, through negotiations and bidding, different prices for equipment, service, and parts for different customers. See App. 420–421, 536. Kodak provides 80% to 95% of the service for Kodak machines. See *id.*, at 430.

Beginning in the early 1980's, ISO's began repairing and servicing Kodak equipment. They also sold parts and reconditioned and sold used Kodak equipment. Their customers were federal, state, and local government agencies, banks, insurance companies, industrial enterprises, and providers of specialized copy and microfilming services. See *id.*, at 417, 419–421, 492–493, 499, 516, 539. ISO's provide service at a price substantially lower than Kodak does. See *id.*, at 414, 451, 453–454, 469, 474–475, 488, 493, 536–537; Lodging 133. Some customers found that the ISO service was of higher quality. See App. 425–426, 537–538.

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computer-generated data onto microfilm. The fourth is Computer Assisted Retrieval (CAR) systems, which utilize computers to locate and retrieve micrographic images. See App. 156–158.

Some ISO customers purchase their own parts and hire ISO's only for service. See Lodging 144–147. Others choose ISO's to supply both service and parts. See *id.*, at 133. ISO's keep an inventory of parts, purchased from Kodak or other sources, primarily the OEM's.[2] See App. 99, 415–416, 490.

In 1985 and 1986, Kodak implemented a policy of selling replacement parts for micrographic and copying machines only to buyers of Kodak equipment who use Kodak service or repair their own machines. See Brief for Petitioner 6; App. 91–92, 98–100, 140–141, 171–172, 190, 442–447, 455–456, 483–484.

As part of the same policy, Kodak sought to limit ISO access to other sources of Kodak parts. Kodak and the OEM's agreed that the OEM's would not sell parts that fit Kodak equipment to anyone other than Kodak. See *id.*, at 417, 428–429, 447, 468, 474, 496. Kodak also pressured Kodak equipment owners and independent parts distributors not to sell Kodak parts to ISO's. See *id.*, at 419–420, 428–429, 483–484, 517–518, 589–590. In addition, Kodak took steps to restrict the availability of used machines. See *id.*, at 427–428, 465–466, 510–511, 520.

Kodak intended, through these policies, to make it more difficult for ISO's to sell service for Kodak machines. See *id.*, at 106–107, 171, 516. It succeeded. ISO's were unable to obtain parts from reliable sources, see *id.*, at 429, 468, 496, and many were forced out of business, while others lost substantial revenue. See *id.*, at 422, 458–459, 464, 468, 475–477, 482–484, 495–496, 501, 521. Customers were forced to switch to Kodak service even though they preferred ISO service. See *id.*, at 420–422.

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[2] In addition to the OEM's, other sources of Kodak parts include (1) brokers who would buy parts from Kodak, or strip used Kodak equipment to obtain the useful parts and resell them, (2) customers who buy parts from Kodak and make them available to ISO's, and (3) used equipment to be stripped for parts. See *id.*, at 419, 517; Brief for Petitioner 38.

B

In 1987, the ISO's filed the present action in the District Court, alleging, *inter alia,* that Kodak had unlawfully tied the sale of service for Kodak machines to the sale of parts, in violation of § 1 of the Sherman Act, and had unlawfully monopolized and attempted to monopolize the sale of service for Kodak machines, in violation of § 2 of that Act.[3]

Kodak filed a motion for summary judgment before respondents had initiated discovery. The District Court permitted respondents to file one set of interrogatories and one set of requests for production of documents and to take six depositions. Without a hearing, the District Court granted summary judgment in favor of Kodak. App. to Pet. for Cert. 29B.

As to the § 1 claim, the court found that respondents had provided no evidence of a tying arrangement between Kodak equipment and service or parts. See *id.,* at 32B–33B. The court, however, did not address respondents' § 1 claim that is at issue here. Respondents allege a tying arrangement not between Kodak *equipment* and service, but between Kodak *parts* and service. As to the § 2 claim, the District Court concluded that although Kodak had a "natural monopoly over the market for parts it sells under its name," a unilateral refusal to sell those parts to ISO's did not violate § 2.

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[3] Section 1 of the Sherman Act states in relevant part: "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." 15 U. S. C. § 1 (1988 ed., Supp. II).

Section 2 of the Sherman Act states: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $10,000,000 if a corporation, or, if any other person, $350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court." 15 U. S. C. § 2 (1988 ed., Supp. II).

The Court of Appeals for the Ninth Circuit, by a divided vote, reversed. 903 F. 2d 612 (1990). With respect to the § 1 claim, the court first found that whether service and parts were distinct markets and whether a tying arrangement existed between them were disputed issues of fact. *Id.*, at 615–616. Having found that a tying arrangement might exist, the Court of Appeals considered a question not decided by the District Court: Was there "an issue of material fact as to whether Kodak has sufficient economic power in the tying product market [parts] to restrain competition appreciably in the tied product market [service]." *Id.*, at 616. The court agreed with Kodak that competition in the equipment market might prevent Kodak from possessing power in the parts market, but refused to uphold the District Court's grant of summary judgment "on this theoretical basis" because "market imperfections can keep economic theories about how consumers will act from mirroring reality." *Id.*, at 617. Noting that the District Court had not considered the market power issue, and that the record was not fully developed through discovery, the court declined to require respondents to conduct market analysis or to pinpoint specific imperfections in order to withstand summary judgment.[4] "It is enough that [respondents] have presented evidence of actual events from which a reasonable trier of fact could conclude that . . . competition in the [equipment] market does not, in reality, curb Kodak's power in the parts market." *Ibid.*

[4] Specifically, the Court of Appeals explained that the District Court had denied the request for further discovery made by respondents in their opposition to Kodak's summary judgment motion: "For example, [respondents] requested to depose two ISO customers who allegedly would not sign accurate statements concerning Kodak's market power in the parts market. Not finding it necessary to reach the market power issue in its decision, the district court, of course, had no reason to grant this request." 903 F. 2d, at 617, n. 4.

The court then considered the three business justifications Kodak proffered for its restrictive parts policy: (1) to guard against inadequate service, (2) to lower inventory costs, and (3) to prevent ISO's from free-riding on Kodak's investment in the copier and micrographic industry. The court concluded that the trier of fact might find the product quality and inventory reasons to be pretextual and that there was a less restrictive alternative for achieving Kodak's quality-related goals. *Id.*, at 618–619. The court also found Kodak's third justification, preventing ISO's from profiting on Kodak's investments in the equipment markets, legally insufficient. *Id.*, at 619.

As to the § 2 claim, the Court of Appeals concluded that sufficient evidence existed to support a finding that Kodak's implementation of its parts policy was "anticompetitive" and "exclusionary" and "involved a specific intent to monopolize." *Id.*, at 620. It held that the ISO's had come forward with sufficient evidence, for summary judgment purposes, to disprove Kodak's business justifications. *Ibid.*

The dissent in the Court of Appeals, with respect to the § 1 claim, accepted Kodak's argument that evidence of competition in the equipment market "*necessarily* precludes power in the derivative market." *Id.*, at 622 (emphasis in original). With respect to the § 2 monopolization claim, the dissent concluded that, entirely apart from market power considerations, Kodak was entitled to summary judgment on the basis of its first business justification because it had "submitted extensive and undisputed evidence of a marketing strategy based on high-quality service." *Id.*, at 623.

II

A tying arrangement is "an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier." *Northern Pacific R. Co.* v. *United States*, 356 U. S. 1, 5–6

(1958). Such an arrangement violates § 1 of the Sherman Act if the seller has "appreciable economic power" in the tying product market and if the arrangement affects a substantial volume of commerce in the tied market. *Fortner Enterprises, Inc.* v. *United States Steel Corp.,* 394 U. S. 495, 503 (1969).

Kodak did not dispute that its arrangement affects a substantial volume of interstate commerce. It, however, did challenge whether its activities constituted a "tying arrangement" and whether Kodak exercised "appreciable economic power" in the tying market. We consider these issues in turn.

A

For respondents to defeat a motion for summary judgment on their claim of a tying arrangement, a reasonable trier of fact must be able to find, first, that service and parts are two distinct products, and, second, that Kodak has tied the sale of the two products.

For service and parts to be considered two distinct products, there must be sufficient consumer demand so that it is efficient for a firm to provide service separately from parts. *Jefferson Parish Hospital Dist. No. 2* v. *Hyde,* 466 U. S. 2, 21–22 (1984). Evidence in the record indicates that service and parts have been sold separately in the past and still are sold separately to self-service equipment owners.[5] Indeed, the development of the entire high-technology service industry is evidence of the efficiency of a separate market for service.[6]

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[5] The Court of Appeals found: "Kodak's policy of allowing customers to purchase parts on condition that they agree to service their own machines suggests that the demand for parts can be separated from the demand for service." *Id.,* at 616.

[6] *Amicus* briefs filed by various service organizations attest to the magnitude of the service business. See, *e. g.,* Brief for Computer Service Network International as *Amicus Curiae;* Brief for National Electronics Sales and Service Dealers Association as *Amicus Curiae;* Brief for Cali-

Kodak insists that because there is no demand for parts separate from service, there cannot be separate markets for service and parts. Brief for Petitioner 15, n. 3. By that logic, we would be forced to conclude that there can never be separate markets, for example, for cameras and film, computers and software, or automobiles and tires. That is an assumption we are unwilling to make. "We have often found arrangements involving functionally linked products at least one of which is useless without the other to be prohibited tying devices." *Jefferson Parish*, 466 U. S., at 19, n. 30.

Kodak's assertion also appears to be incorrect as a factual matter. At least some consumers would purchase service without parts, because some service does not require parts, and some consumers, those who self-service for example, would purchase parts without service.[7] Enough doubt is cast on Kodak's claim of a unified market that it should be resolved by the trier of fact.

Finally, respondents have presented sufficient evidence of a tie between service and parts. The record indicates that Kodak would sell parts to third parties only if they agreed not to buy service from ISO's.[8]

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fornia State Electronics Association et al. as *Amici Curiae;* Brief for National Office Machine Dealers et al. as *Amici Curiae.*

[7] The dissent suggests that parts and service are not separate products for tying purposes because all service may involve installation of parts. *Post*, at 494–495, n. 2. Because the record does not support this factual assertion, under the approach of both the Court and the concurrence in *Jefferson Parish Hospital Dist. No. 2* v. *Hyde*, 466 U. S. 2 (1984), Kodak is not entitled to summary judgment on whether parts and service are distinct markets.

[8] In a footnote, Kodak contends that this practice is only a unilateral refusal to deal, which does not violate the antitrust laws. See Brief for Petitioner 15, n. 4. Assuming, *arguendo*, that Kodak's refusal to sell parts to any company providing service can be characterized as a unilateral refusal to deal, its alleged sale of parts to third parties on condition that they buy service from Kodak is not. See 903 F. 2d, at 619.

B

Having found sufficient evidence of a tying arrangement, we consider the other necessary feature of an illegal tying arrangement: appreciable economic power in the tying market. Market power is the power "to force a purchaser to do something that he would not do in a competitive market." *Jefferson Parish,* 466 U. S., at 14.[9] It has been defined as "the ability of a single seller to raise price and restrict output." *Fortner,* 394 U. S., at 503; *United States* v. *E. I. du Pont de Nemours & Co.,* 351 U. S. 377, 391 (1956). The existence of such power ordinarily is inferred from the seller's possession of a predominant share of the market. *Jefferson Parish,* 466 U. S., at 17; *United States* v. *Grinnell Corp.,* 384 U. S. 563, 571 (1966); *Times-Picayune Publishing Co.* v. *United States,* 345 U. S. 594, 611–613 (1953).

1

Respondents contend that Kodak has more than sufficient power in the parts market to force unwanted purchases of the tied market, service. Respondents provide evidence that certain parts are available exclusively through Kodak. Respondents also assert that Kodak has control over the availability of parts it does not manufacture. According to respondents' evidence, Kodak has prohibited independent manufacturers from selling Kodak parts to ISO's, pressured Kodak equipment owners and independent parts distributors to deny ISO's the purchase of Kodak parts, and taken steps to restrict the availability of used machines.

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[9] "[T]he essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms. When such 'forcing' is present, competition on the merits in the market for the tied item is restrained and the Sherman Act is violated." *Jefferson Parish,* 466 U. S., at 12.

Respondents also allege that Kodak's control over the parts market has excluded service competition, boosted service prices, and forced unwilling consumption of Kodak service. Respondents offer evidence that consumers have switched to Kodak service even though they preferred ISO service, that Kodak service was of higher price and lower quality than the preferred ISO service, and that ISO's were driven out of business by Kodak's policies. Under our prior precedents, this evidence would be sufficient to entitle respondents to a trial on their claim of market power.

2

Kodak counters that even if it concedes monopoly *share* of the relevant parts market, it cannot actually exercise the necessary market *power* for a Sherman Act violation. This is so, according to Kodak, because competition exists in the equipment market.[10] Kodak argues that it could not have

[10] In their brief and at oral argument, respondents argued that Kodak's market share figures for high-volume copy machines, CAR systems, and micrographic-capture equipment demonstrate Kodak's market power in the equipment market. Brief for Respondents 16–18, 32–33; Tr. of Oral Arg. 28–31.

In the Court of Appeals, however, respondents did not contest Kodak's assertion that its market shares indicated a competitive equipment market. The Court of Appeals believed that respondents "do not dispute Kodak's assertion that it lacks market power in the [equipment] markets." 903 F. 2d, at 616, n. 3. Nor did respondents question Kodak's asserted lack of market power in their brief in opposition to the petition for certiorari, although they acknowledged that Kodak's entire case rested on its understanding that respondents were not disputing the existence of competition in the equipment market. Brief in Opposition 8.

Recognizing that on summary judgment we may examine the record *de novo* without relying on the lower courts' understanding, *United States* v. *Diebold, Inc.*, 369 U. S. 654, 655 (1962), respondents now ask us to decline to reach the merits of the questions presented in the petition, and instead to affirm the Ninth Circuit's judgment based on the factual dispute over market power in the equipment market. We decline respondents' invitation. We stated in *Oklahoma City* v. *Tuttle*, 471 U. S. 808, 816 (1985): "Our decision to grant certiorari represents a commitment of scarce judithe ability to raise prices of service and parts above the level that would be charged in a competitive market because any increase in profits from a higher price in the aftermarkets at least would be offset by a corresponding loss in profits from lower equipment sales as consumers began purchasing equipment with more attractive service costs.

Kodak does not present any actual data on the equipment, service, or parts markets. Instead, it urges the adoption of a substantive legal rule that "equipment competition precludes any finding of monopoly power in derivative aftermarkets." Brief for Petitioner 33. Kodak argues that such a rule would satisfy its burden as the moving party of showing "that there is no genuine issue as to any material fact" on the market power issue.[11] See Fed. Rule Civ. Proc. 56(c).

Legal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored

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cial resources with a view to deciding the merits of one or more of the questions presented in the petition." Because respondents failed to bring their objections to the premise underlying the questions presented to our attention in their opposition to the petition for certiorari, we decide those questions based on the same premise as the Court of Appeals, namely, that competition exists in the equipment market.

[11] Kodak argues that such a rule would be *per se,* with no opportunity for respondents to rebut the conclusion that market power is lacking in the parts market. See Brief for Petitioner 30–31 ("There is nothing that respondents could prove that would overcome Kodak's conceded lack of market power"); *id.,* at 30 (discovery is "pointless" once the "dispositive fact" of lack of market power in the equipment market is conceded); *id.,* at 22 (Kodak's lack of market power in the equipment market "dooms any attempt to extract monopoly profits" even in an allegedly imperfect market); *id.,* at 25 (it is "impossible" for Kodak to make more total profit by overcharging its existing customers for service).

As an apparent second-best alternative, Kodak suggests elsewhere in its brief that the rule would permit a defendant to meet its summary judgment burden under Federal Rule of Civil Procedure 56(c); the burden would then shift to the plaintiffs to "prove . . . that there is specific reason to believe that normal economic reasoning does not apply." Brief for Petitioner 30. This is the United States' position. See Brief for United States as *Amicus Curiae* 10–11.

in antitrust law. This Court has preferred to resolve antitrust claims on a case-by-case basis, focusing on the "particular facts disclosed by the record." *Maple Flooring Manufacturers Assn.* v. *United States*, 268 U. S. 563, 579 (1925); *Du Pont*, 351 U. S., at 395, n. 22; *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 70 (1977) (WHITE, J., concurring in judgment).[12] In determining the existence of market power, and specifically the "responsiveness of the sales of one product to price changes of the other," *Du Pont*, 351 U. S., at 400; see also *id.*, at 394–395, and 400–401, this Court has examined closely the economic reality of the market at issue.[13]

Kodak contends that there is no need to examine the facts when the issue is market power in the aftermarkets. A legal presumption against a finding of market power is warranted in this situation, according to Kodak, because the existence of market power in the service and parts markets absent power in the equipment market "simply makes no economic sense," and the absence of a legal presumption would deter procompetitive behavior. *Matsushita*, 475 U. S., at 587; *id.*, at 594–595.

Kodak analogizes this case to *Matsushita*, where a group of American corporations that manufactured or sold consumer electronic products alleged that their 21 Japanese counterparts were engaging in a 20-year conspiracy to price

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[12] See generally *Business Electronics Corp.* v. *Sharp Electronics Corp.*, 485 U. S. 717, 723–726 (1988); *FTC* v. *Indiana Federation of Dentists*, 476 U. S. 447, 458–459 (1986); *National Collegiate Athletic Assn.* v. *Board of Regents of Univ. of Okla.*, 468 U. S. 85, 100–104 (1984); *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S., at 59.

[13] See, *e. g., Jefferson Parish*, 466 U. S., at 26–29; *United States* v. *Connecticut National Bank*, 418 U. S. 656, 661–666 (1974); *United States* v. *Grinnell Corp.*, 384 U. S. 563, 571–576 (1966); *International Boxing Club of New York, Inc.* v. *United States*, 358 U. S. 242, 250–251 (1959); see also *Jefferson Parish*, 466 U. S., at 37, n. 6 (O'CONNOR, J., concurring) (citing cases and describing the careful consideration the Court gives to the particular facts when determining market power).

below cost in the United States in the hope of expanding their market share sometime in the future. After several years of detailed discovery, the defendants moved for summary judgment. *Id.*, at 577–582. Because the defendants had every incentive not to engage in the alleged conduct which required them to sustain losses for decades with no foreseeable profits, the Court found an "absence of any rational motive to conspire." *Id.*, at 597. In that context, the Court determined that the plaintiffs' theory of predatory pricing made no practical sense, was "speculative," and was not "reasonable." *Id.*, at 588, 590, 593, 595, 597. Accordingly, the Court held that a reasonable jury could not return a verdict for the plaintiffs and that summary judgment would be appropriate against them unless they came forward with more persuasive evidence to support their theory. *Id.*, at 587–588, 595–598.

The Court's requirement in *Matsushita* that the plaintiffs' claims make economic sense did not introduce a special burden on plaintiffs facing summary judgment in antitrust cases. The Court did not hold that if the moving party enunciates *any* economic theory supporting its behavior, regardless of its accuracy in reflecting the actual market, it is entitled to summary judgment. *Matsushita* demands only that the nonmoving party's inferences be reasonable in order to reach the jury, a requirement that was not invented, but merely articulated, in that decision.[14] If the plaintiff's theory is eco-

[14] See, *e. g., Anderson* v. *Liberty Lobby, Inc.*, 477 U. S. 242, 248 (1986) ("[S]ummary judgment will not lie . . . if the evidence is such that a reasonable jury could return a verdict for the nonmoving party"); *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U. S. 752, 768 (1984) (to survive summary judgment there must be evidence that "reasonably tends to prove" plaintiff's theory); *First National Bank of Arizona* v. *Cities Service Co.*, 391 U. S. 253, 288–289 (1968) (defendant meets his burden under Rule 56(c) when he "conclusively show[s] that the facts upon which [the plaintiff] relied to support his allegation were not susceptible of the interpretation which he sought to give them"); *Eastman Kodak Co. of New York* v. *Southern Photo Materials Co.*, 273 U. S. 359, 375 (1927). See also *H. L. Hayden*

nomically senseless, no reasonable jury could find in its favor, and summary judgment should be granted.

Kodak, then, bears a substantial burden in showing that it is entitled to summary judgment. It must show that despite evidence of increased prices and excluded competition, an inference of market power is unreasonable. To determine whether Kodak has met that burden, we must unravel the factual assumptions underlying its proposed rule that lack of power in the equipment market necessarily precludes power in the aftermarkets.

The extent to which one market prevents exploitation of another market depends on the extent to which consumers will change their consumption of one product in response to a price change in another, *i. e.*, the "cross-elasticity of demand." See *Du Pont*, 351 U. S., at 400; P. Areeda & L. Kaplow, Antitrust Analysis ¶ 342(c) (4th ed. 1988).[15] Ko-

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Co. of New York, Inc. v. *Siemens Medical Systems, Inc.*, 879 F. 2d 1005, 1012 (CA2 1989) ("[O]nly *reasonable* inferences can be drawn from the evidence in favor of the nonmoving party") (emphasis in original); *Arnold Pontiac-GMC, Inc.* v. *Budd Baer, Inc.*, 826 F. 2d 1335, 1339 (CA3 1987) (*Matsushita* directs us " 'to consider whether the inference of conspiracy is reasonable' "); *Instructional Systems Development Corp.* v. *Aetna Casualty & Surety Co.*, 817 F. 2d 639, 646 (CA10 1987) (summary judgment not appropriate under *Matsushita* when defendants "could reasonably have been economically motivated").

[15] What constrains the defendant's ability to raise prices in the service market is "the elasticity of demand faced by the defendant—the degree to which its sales fall . . . as its price rises." Areeda & Kaplow ¶ 342(c), p. 576.

Courts usually have considered the relationship between price in one market and demand in another in defining the relevant market. Because market power is often inferred from market share, market definition generally determines the result of the case. Pitofsky, New Definitions of Relevant Market and the Assault on Antitrust, 90 Colum. L. Rev. 1805, 1806–1813 (1990). Kodak chose to focus on market power directly rather than arguing that the relationship between equipment and service and parts is such that the three should be included in the same market definition. Whether considered in the conceptual category of "market definition" or "market power," the ultimate inquiry is the same—whether competition dak's proposed rule rests on a factual assumption about the cross-elasticity of demand in the equipment and aftermarkets: "If Kodak raised its parts or service prices above competitive levels, potential customers would simply stop buying Kodak equipment. Perhaps Kodak would be able to increase short term profits through such a strategy, but at a devastating cost to its long term interests."[16] Brief for Petitioner 12. Kodak argues that the Court should accept, as a matter of law, this "basic economic realit[y]," *id.*, at 24, that competition in the equipment market necessarily prevents market power in the aftermarkets.[17]

Even if Kodak could not raise the price of service and parts one cent without losing equipment sales, that fact would not disprove market power in the aftermarkets. The sales of even a monopolist are reduced when it sells goods at a monopoly price, but the higher price more than compensates for the loss in sales. Areeda & Kaplow ¶¶ 112 and 340(a). Kodak's claim that charging more for service and parts would be "a short-run game," Brief for Petitioner 26, is based on the false dichotomy that there are only two prices

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in the equipment market will significantly restrain power in the service and parts markets.

[16] The United States as *amicus curiae* in support of Kodak echoes this argument: "The ISOs' claims are implausible because Kodak lacks market power in the markets for its copier and micrographic equipment. Buyers of such equipment regard an increase in the price of parts or service as an increase in the price of the equipment, and sellers recognize that the revenues from sales of parts and service are attributable to sales of the equipment. In such circumstances, it is not apparent how an equipment manufacturer such as Kodak could exercise power in the aftermarkets for parts and service." Brief for United States as *Amicus Curiae* 8.

[17] It is clearly true, as the United States claims, that Kodak "cannot set service or parts prices without regard to the impact on the market for equipment." *Id.*, at 20. The fact that the cross-elasticity of demand is not zero proves nothing; the disputed issue is how much of an impact an increase in parts and service prices has on equipment sales and on Kodak's profits.

that can be charged—a competitive price or a ruinous one. But there could easily be a middle, optimum price at which the increased revenues from the higher priced sales of service and parts would more than compensate for the lower revenues from lost equipment sales. The fact that the equipment market imposes a restraint on prices in the aftermarkets by no means disproves the existence of power in those markets. See Areeda & Kaplow ¶ 340(b) ("[T]he existence of significant substitution in the event of *further* price increases or even at the *current* price does not tell us whether the defendant *already* exercises significant market power") (emphasis in original). Thus, contrary to Kodak's assertion, there is no immutable physical law—no "basic economic reality"—insisting that competition in the equipment market cannot coexist with market power in the aftermarkets.

We next consider the more narrowly drawn question: Does Kodak's theory describe actual market behavior so accurately that respondents' assertion of Kodak market power in the aftermarkets, if not impossible, is at least unreasonable?[18] Cf. *Matsushita Electric Industrial Co.* v. *Zenith Radio Corp.*, 475 U. S. 574 (1986).

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[18] Although Kodak repeatedly relies on *Continental T. V.* as support for its factual assertion that the equipment market will prevent exploitation of the service and parts markets, the case is inapposite. In *Continental T. V.*, the Court found that a manufacturer's policy restricting the number of retailers that were permitted to sell its product could have a procompetitive effect. See 433 U. S., at 55. The Court also noted that any negative effect of exploitation of the intrabrand market (the competition between retailers of the same product) would be checked by competition in the interbrand market (competition over the same generic product) because consumers would substitute a different brand of the same product. Unlike *Continental T. V.*, this case does not concern vertical relationships between parties on different levels of the same distribution chain. In the relevant market, service, Kodak and the ISO's are direct competitors; their relationship is horizontal. The interbrand competition at issue here is competition over the provision of service. Despite petitioner's best effort,

To review Kodak's theory, it contends that higher service prices will lead to a disastrous drop in equipment sales. Presumably, the theory's corollary is to the effect that low service prices lead to a dramatic increase in equipment sales. According to the theory, one would have expected Kodak to take advantage of lower priced ISO service as an opportunity to expand equipment sales. Instead, Kodak adopted a restrictive sales policy consciously designed to eliminate the lower priced ISO service, an act that would be expected to devastate either Kodak's equipment sales or Kodak's faith in its theory. Yet, according to the record, it has done neither. Service prices have risen for Kodak customers, but there is no evidence or assertion that Kodak equipment sales have dropped.

Kodak and the United States attempt to reconcile Kodak's theory with the contrary actual results by describing a "marketing strategy of spreading over time the total cost to the buyer of Kodak equipment." Brief for United States as *Amicus Curiae* 18; see also Brief for Petitioner 18. In other words, Kodak could charge subcompetitive prices for equipment and make up the difference with supracompetitive prices for service, resulting in an overall competitive price. This pricing strategy would provide an explanation for the theory's descriptive failings—if Kodak in fact had adopted it. But Kodak never has asserted that it prices its equipment or parts subcompetitively and recoups its profits through service. Instead, it claims that it prices its equipment comparably to its competitors and intends that both its equipment sales and service divisions be profitable. See App. 159–161, 170, 178, 188. Moreover, this hypothetical pricing strategy is inconsistent with Kodak's policy toward its self-service customers. If Kodak were underpricing its equipment, hoping to lock in customers and recover its losses in the service

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repeating the mantra "interbrand competition" does not transform this case into one over an agreement the manufacturer has with its dealers that would fall under the rubric of *Continental T. V.*

market, it could not afford to sell customers parts without service. In sum, Kodak's theory does not explain the actual market behavior revealed in the record.

Respondents offer a forceful reason why Kodak's theory, although perhaps intuitively appealing, may not accurately explain the behavior of the primary and derivative markets for complex durable goods: the existence of significant information and switching costs. These costs could create a less responsive connection between service and parts prices and equipment sales.

For the service-market price to affect equipment demand, consumers must inform themselves of the total cost of the "package"—equipment, service, and parts—at the time of purchase; that is, consumers must engage in accurate life-cycle pricing.[19] Life-cycle pricing of complex, durable equipment is difficult and costly. In order to arrive at an accurate price, a consumer must acquire a substantial amount of raw data and undertake sophisticated analysis. The necessary information would include data on price, quality, and availability of products needed to operate, upgrade, or enhance the initial equipment, as well as service and repair costs, including estimates of breakdown frequency, nature of repairs, price of service and parts, length of "downtime," and losses incurred from downtime.[20]

Much of this information is difficult—some of it impossible—to acquire at the time of purchase. During the life of a product, companies may change the service and parts prices, and develop products with more advanced features, a

[19] See Craswell, Tying Requirements in Competitive Markets: The Consumer Protection Issues, 62 B. U. L. Rev. 661, 676 (1982); Beales, Craswell, & Salop, The Efficient Regulation of Consumer Information, 24 J. Law & Econ. 491, 509–511 (1981); *Jefferson Parish,* 466 U. S., at 15.

[20] In addition, of course, in order to price accurately the equipment, a consumer would need initial purchase information such as prices, features, quality, and available warranties for different machinery with different capabilities, and residual value information such as the longevity of product use and its potential resale or trade-in value.

decreased need for repair, or new warranties. In addition, the information is likely to be customer specific; lifecycle costs will vary from customer to customer with the type of equipment, degrees of equipment use, and costs of downtime.

Kodak acknowledges the cost of information, but suggests, again without evidentiary support, that customer information needs will be satisfied by competitors in the equipment markets. Brief for Petitioner 26, n. 11. It is a question of fact, however, whether competitors would provide the necessary information. A competitor in the equipment market may not have reliable information about the lifecycle costs of complex equipment it does not service or the needs of customers it does not serve. Even if competitors had the relevant information, it is not clear that their interests would be advanced by providing such information to consumers. See 2 P. Areeda & D. Turner, Antitrust Law ¶ *404b1* (1978).[21]

Moreover, even if consumers were capable of acquiring and processing the complex body of information, they may choose not to do so. Acquiring the information is expensive. If the costs of service are small relative to the equipment price, or if consumers are more concerned about equipment capabilities than service costs, they may not find it cost efficient to

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[21] To inform consumers about Kodak, the competitor must be willing to forgo the opportunity to reap supracompetitive prices in its own service and parts markets. The competitor may anticipate that charging lower service and parts prices and informing consumers about Kodak in the hopes of gaining future equipment sales will cause Kodak to lower the price on its service and parts, canceling any gains in equipment sales to the competitor and leaving both worse off. Thus, in an equipment market with relatively few sellers, competitors may find it more profitable to adopt Kodak's service and parts policy than to inform the consumers. See 2 Areeda & Turner, Antitrust Law ¶ *404b1;* App. 177 (Kodak, Xerox, and IBM together have nearly 100% of relevant market).

Even in a market with many sellers, any one competitor may not have sufficient incentive to inform consumers because the increased patronage attributable to the corrected consumer beliefs will be shared among other competitors. Beales, Craswell, & Salop, 24 J. Law & Econ., at 503–504, 506.

compile the information. Similarly, some consumers, such as the Federal Government, have purchasing systems that make it difficult to consider the complete cost of the "package" at the time of purchase. State and local governments often treat service as an operating expense and equipment as a capital expense, delegating each to a different department. These governmental entities do not lifecycle price, but rather choose the lowest price in each market. See Brief for National Association of State Purchasing Officials et al. as *Amici Curiae;* Brief for State of Ohio et al. as *Amici Curiae;* App. 429–430.

As Kodak notes, there likely will be some large-volume, sophisticated purchasers who will undertake the comparative studies and insist, in return for their patronage, that Kodak charge them competitive lifecycle prices. Kodak contends that these knowledgeable customers will hold down the package price for all other customers. Brief for Petitioner 23, n. 9. There are reasons, however, to doubt that sophisticated purchasers will ensure that competitive prices are charged to unsophisticated purchasers, too. As an initial matter, if the number of sophisticated customers is relatively small, the amount of profits to be gained by supracompetitive pricing in the service market could make it profitable to let the knowledgeable consumers take their business elsewhere. More importantly, if a company is able to price discriminate between sophisticated and unsophisticated consumers, the sophisticated will be unable to prevent the exploitation of the uninformed. A seller could easily price discriminate by varying the equipment/parts/service package, developing different warranties, or offering price discounts on different components.

Given the potentially high cost of information and the possibility that a seller may be able to price discriminate between knowledgeable and unsophisticated consumers, it makes little sense to assume, in the absence of any evidentiary support, that equipment-purchasing decisions are based on an accurate assessment of the total cost of equipment, service, and parts over the lifetime of the machine.[22]

Indeed, respondents have presented evidence that Kodak practices price discrimination by selling parts to customers who service their own equipment, but refusing to sell parts to customers who hire third-party service companies. Companies that have their own service staff are likely to be high-volume users, the same companies for whom it is most likely to be economically worthwhile to acquire the complex information needed for comparative lifecycle pricing.

A second factor undermining Kodak's claim that supracompetitive prices in the service market lead to ruinous losses in equipment sales is the cost to current owners of switching to a different product. See Areeda & Turner ¶ 519a.[23] If the cost of switching is high, consumers who already have purchased the equipment, and are thus "locked in," will tolerate some level of service-price increases before changing equipment brands. Under this scenario, a seller profitably could maintain supracompetitive prices in the aftermarket if the switching costs were high relative to the increase in service prices, and the number of locked-in customers were high relative to the number of new purchasers.

Moreover, if the seller can price discriminate between its locked-in customers and potential new customers, this strategy is even more likely to prove profitable. The seller could simply charge new customers below-marginal cost on the equipment and recoup the charges in service, or offer pack-

[22] See Salop & Stiglitz, Bargains and Ripoffs: A Model of Monopolistically Competitive Price Dispersion, 44 Rev. Econ. Studies 493 (1977); Salop, Information and Market Structure—Information and Monopolistic Competition, 66 Am. Econ. Rev. 240 (1976); Stigler, The Economics of Information, 69 J. Pol. Econ. 213 (1961).

[23] A firm can exact leverage whenever other equipment is not a ready substitute. F. Scherer & D. Ross, Industrial Market Structure and Economic Performance 16–17 (3d ed. 1990).

ages with lifetime warranties or long-term service agreements that are not available to locked-in customers.

Respondents have offered evidence that the heavy initial outlay for Kodak equipment, combined with the required support material that works only with Kodak equipment, makes switching costs very high for existing Kodak customers. And Kodak's own evidence confirms that it varies the package price of equipment/parts/service for different customers.

In sum, there is a question of fact whether information costs and switching costs foil the simple assumption that the equipment and service markets act as pure complements to one another.[24]

We conclude, then, that Kodak has failed to demonstrate that respondents' inference of market power in the service and parts markets is unreasonable, and that, consequently, Kodak is entitled to summary judgment. It is clearly reasonable to infer that Kodak has market power to raise prices and drive out competition in the aftermarkets, since respondents offer direct evidence that Kodak did so.[25] It is also plausible, as discussed above, to infer that Kodak chose to gain immediate profits by exerting that market power where locked-in customers, high information costs, and discriminatory pricing limited and perhaps eliminated any long-

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[24] The dissent disagrees based on its hypothetical case of a tie between equipment and service. "The only thing lacking" to bring this case within the hypothetical case, states the dissent, "is concrete evidence that the restrictive parts policy was . . . generally known." *Post*, at 492. But the dissent's "only thing lacking" is the crucial thing lacking—evidence. Whether a tie between parts and service should be treated identically to a tie between equipment and service, as the dissent and Kodak argue, depends on whether the equipment market prevents the exertion of market power in the parts market. Far from being "anomalous," *post*, at 492–493, requiring Kodak to provide evidence on this factual question is completely consistent with our prior precedent. See, *e. g.*, n. 13, *supra.*

[25] Cf. *Instructional Systems*, 817 F. 2d, at 646 (finding the conspiracy reasonable under *Matsushita* because its goals were in fact achieved).

term loss. Viewing the evidence in the light most favorable to respondents, their allegations of market power "mak[e] . . . economic sense." Cf. *Matsushita*, 475 U. S., at 587.

Nor are we persuaded by Kodak's contention that it is entitled to a legal presumption on the lack of market power because, as in *Matsushita*, there is a significant risk of deterring procompetitive conduct. Plaintiffs in *Matsushita* attempted to prove the antitrust conspiracy "through evidence of rebates and other price-cutting activities." *Id.*, at 594. Because cutting prices to increase business is "the very essence of competition," the Court was concerned that mistaken inferences would be "especially costly" and would "chill the very conduct the antitrust laws are designed to protect." *Ibid.* See also *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U. S. 752, 763 (1984) (permitting inference of concerted action would "deter or penalize perfectly legitimate conduct"). But the facts in this case are just the opposite. The alleged conduct—higher service prices and market foreclosure—is facially anticompetitive and exactly the harm that antitrust laws aim to prevent. In this situation, *Matsushita* does not create any presumption in favor of summary judgment for the defendant.

Kodak contends that, despite the appearance of anticompetitiveness, its behavior actually favors competition because its ability to pursue innovative marketing plans will allow it to compete more effectively in the equipment market. Brief for Petitioner 40–41. A pricing strategy based on lower equipment prices and higher aftermarket prices could enhance equipment sales by making it easier for the buyer to finance the initial purchase.[26] It is undisputed that competition is enhanced when a firm is able to offer various marketing options, including bundling of support and maintenance service with the sale of equipment. Nor do such ac-

[26] It bears repeating that in this case Kodak has never claimed that it is in fact pursuing such a pricing strategy.

tions run afoul of the antitrust laws.[27] But the procompetitive effect of the specific conduct challenged here, eliminating all consumer parts and service options, is far less clear.[28]

We need not decide whether Kodak's behavior has any procompetitive effects and, if so, whether they outweigh the anticompetitive effects. We note only that Kodak's service and parts policy is simply not one that appears always or almost always to enhance competition, and therefore to warrant a legal presumption without any evidence of its actual economic impact. In this case, when we weigh the risk of deterring procompetitive behavior by proceeding to trial against the risk that illegal behavior will go unpunished, the balance tips against summary judgment. Cf. *Matsushita*, 475 U. S., at 594–595.

For the foregoing reasons, we hold that Kodak has not met the requirements of Federal Rule of Civil Procedure 56(c). We therefore affirm the denial of summary judgment on respondents' § 1 claim.[29]

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[27] See *Jefferson Parish*, 466 U. S., at 12 ("Buyers often find package sales attractive; a seller's decision to offer such packages can merely be an attempt to compete effectively—conduct that is entirely consistent with the Sherman Act"). See also Yates & DiResta, Software Support and Hardware Maintenance Practices: Tying Considerations, The Computer Lawyer, Vol. 8, No. 6, p. 17 (1991) (describing various service and parts policies that enhance quality and sales but do not violate the antitrust laws).

[28] Two of the largest consumers of service and parts contend that they are worse off when the equipment manufacturer also controls service and parts. See Brief for State Farm Mutual Automobile Insurance Co. et al. as *Amici Curiae;* Brief for State of Ohio et al. as *Amici Curiae.*

[29] The dissent urges a radical departure in this Court's antitrust law. It argues that because Kodak has only an "inherent" monopoly in parts for its equipment, *post,* at 489–490, the antitrust laws do not apply to its efforts to expand that power into other markets. The dissent's proposal to grant *per se* immunity to manufacturers competing in the service market would exempt a vast and growing sector of the economy from antitrust laws. Leaving aside the question whether the Court has the authority to

III

Respondents also claim that they have presented genuine issues for trial as to whether Kodak has monopolized, or at-

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make such a policy decision, there is no support for it in our jurisprudence or the evidence in this case.

Even assuming, despite the absence of any proof from the dissent, that all manufacturers possess some inherent market power in the parts market, it is not clear why that should immunize them from the antitrust laws in another market. The Court has held many times that power gained through some natural and legal advantage such as a patent, copyright, or business acumen can give rise to liability if "a seller exploits his dominant position in one market to expand his empire into the next." *Times-Picayune Publishing Co.* v. *United States,* 345 U. S. 594, 611 (1953); see, *e. g., Northern Pacific R. Co.* v. *United States,* 356 U. S. 1 (1958); *United States* v. *Paramount Pictures, Inc.,* 334 U. S. 131 (1948); *Leitch Mfg. Co.* v. *Barber Co.,* 302 U. S. 458, 463 (1938). Moreover, on the occasions when the Court has considered tying in derivative aftermarkets by manufacturers, it has not adopted any exception to the usual antitrust analysis, treating derivative aftermarkets as it has every other separate market. See *International Salt Co.* v. *United States,* 332 U. S. 392 (1947); *International Business Machines Corp.* v. *United States,* 298 U. S. 131 (1936); *United Shoe Machinery Corp.* v. *United States,* 258 U. S. 451 (1922). Our past decisions are reason enough to reject the dissent's proposal. See *Patterson* v. *McLean Credit Union,* 491 U. S. 164, 172–173 (1989) ("Considerations of *stare decisis* have special force in the area of statutory interpretation, for here, unlike in the context of constitutional interpretation, the legislative power is implicated, and Congress remains free to alter what we have done").

Nor does the record in this case support the dissent's proposed exemption for aftermarkets. The dissent urges its exemption because the tie here "does not permit the manufacturer to project power over a class of consumers distinct from that which it is already able to exploit (and fully) without the inconvenience of the tie." *Post,* at 498. Beyond the dissent's obvious difficulty in explaining why Kodak would adopt this expensive tying policy if it could achieve the same profits more conveniently through some other means, respondents offer an alternative theory, supported by the record, that suggests Kodak *is* able to exploit some customers who in the absence of the tie would be protected from increases in parts prices by knowledgeable customers. See *supra,* at 475–476.

At bottom, whatever the ultimate merits of the dissent's theory, at this point it is mere conjecture. Neither Kodak nor the dissent have provided tempted to monopolize, the service and parts markets in violation of § 2 of the Sherman Act. "The offense of monopoly under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *United States* v. *Grinnell Corp.,* 384 U. S., at 570–571.

A

The existence of the first element, possession of monopoly power, is easily resolved. As has been noted, respondents have presented a triable claim that service and parts are separate markets, and that Kodak has the "power to control prices or exclude competition" in service and parts. *Du Pont,* 351 U. S., at 391. Monopoly power under § 2 requires, of course, something greater than market power under § 1. See *Fortner*, 394 U. S., at 502. Respondents' evidence that Kodak controls nearly 100% of the parts market and 80% to 95% of the service market, with no readily available substitutes, is, however, sufficient to survive summary judgment under the more stringent monopoly standard of § 2. See *National Collegiate Athletic Assn.* v. *Board of Regents of Univ. of Okla.*, 468 U. S. 85, 112 (1984). Cf. *United States* v. *Grinnell Corp.*, 384 U. S., at 571 (87% of the market is a monopoly); *American Tobacco Co.* v. *United States,* 328 U. S. 781, 797 (1946) (over two-thirds of the market is a monopoly).

Kodak also contends that, as a matter of law, a single brand of a product or service can never be a relevant market under the Sherman Act. We disagree. The relevant mar-

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any evidence refuting respondents' theory of forced unwanted purchases at higher prices and price discrimination. While it may be, as the dissent predicts, that the equipment market will prevent any harms to consumers in the aftermarkets, the dissent never makes plain why the Court should accept that theory on faith rather than requiring the usual evidence needed to win a summary judgment motion.

ket for antitrust purposes is determined by the choices available to Kodak equipment owners. See *Jefferson Parish*, 466 U. S., at 19. Because service and parts for Kodak equipment are not interchangeable with other manufacturers' service and parts, the relevant market from the Kodak equipment owner's perspective is composed of only those companies that service Kodak machines. See *Du Pont,* 351 U. S., at 404 ("The market is composed of products that have reasonable interchangeability").[30] This Court's prior cases support the proposition that in some instances one brand of a product can constitute a separate market. See *National Collegiate Athletic Assn.*, 468 U. S., at 101–102, 111–112; *International Boxing Club of New York, Inc.* v. *United States*, 358 U. S. 242, 249–252 (1959); *International Business Machines Corp.* v. *United States*, 298 U. S. 131 (1936).[31] The proper market definition in this case can be determined only after a factual inquiry into the "commercial realities" faced by consumers. *United States* v. *Grinnell Corp.*, 384 U. S., at 572.

B

The second element of a §2 claim is the use of monopoly power "to foreclose competition, to gain a competitive advan-

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[30] Kodak erroneously contends that this Court in *Du Pont* rejected the notion that a relevant market could be limited to one brand. Brief for Petitioner 33. The Court simply held in *Du Pont* that one brand does not *necessarily* constitute a relevant market if substitutes are available. 351 U. S., at 393. See also *Boxing Club,* 358 U. S., at 249–250. Here respondents contend there are no substitutes.

[31] Other courts have limited the market to parts for a particular brand of equipment. See, *e. g., International Logistics Group, Ltd.* v. *Chrysler Corp.,* 884 F. 2d 904, 905, 908 (CA6 1989) (parts for Chrysler cars is the relevant market), cert. denied, 494 U. S. 1066 (1990); *Dimidowich* v. *Bell & Howell*, 803 F. 2d 1473, 1480–1481, n. 3 (CA9 1986), modified, 810 F. 2d 1517 (1987) (service for Bell & Howell equipment is the relevant market); *In re General Motors Corp.*, 99 F. T. C. 464, 554, 584 (1982) (crash parts for General Motors cars is the relevant market); *Heatransfer Corp.* v. *Volkswagenwerk A. G.,* 553 F. 2d 964 (CA5 1977) (air conditioners for Volkswagens is the relevant market), cert. denied, 434 U. S. 1087 (1978).

tage, or to destroy a competitor." *United States* v. *Griffith*, 334 U. S. 100, 107 (1948). If Kodak adopted its parts and service policies as part of a scheme of willful acquisition or maintenance of monopoly power, it will have violated § 2. *Grinnell Corp.*, 384 U. S., at 570–571; *United States* v. *Aluminum Co. of America*, 148 F. 2d 416, 432 (CA2 1945); *Aspen Skiing Co.* v. *Aspen Highlands Skiing Corp.*, 472 U. S. 585, 600–605 (1985).[32]

As recounted at length above, respondents have presented evidence that Kodak took exclusionary action to maintain its parts monopoly and used its control over parts to strengthen its monopoly share of the Kodak service market. Liability turns, then, on whether "valid business reasons" can explain Kodak's actions. *Id.*, at 605; *United States* v. *Aluminum Co. of America*, 148 F. 2d, at 432. Kodak contends that it has three valid business justifications for its actions: "(1) to promote interbrand equipment competition by allowing Kodak to stress the quality of its service; (2) to improve asset management by reducing Kodak's inventory costs; and (3) to prevent ISOs from free-riding on Kodak's capital investment in equipment, parts and service." Brief for Petitioner 6. Factual questions exist, however, about the validity and sufficiency of each claimed justification, making summary judgment inappropriate.

Kodak first asserts that by preventing customers from using ISO's, "it [can] best maintain high quality service for its sophisticated equipment" and avoid being "blamed for an equipment malfunction, even if the problem is the result of improper diagnosis, maintenance or repair by an ISO." *Id.*, at 6–7. Respondents have offered evidence that ISO's provide quality service and are preferred by some Kodak equipment owners. This is sufficient to raise a genuine issue of

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[32] It is true that as a general matter a firm can refuse to deal with its competitors. But such a right is not absolute; it exists only if there are legitimate competitive reasons for the refusal. See *Aspen Skiing Co.*, 472 U. S., at 602–605.

fact. See *International Business Machines Corp.* v. *United States*, 298 U. S., at 139–140 (rejecting IBM's claim that it had to control the cards used in its machines to avoid "injury to the reputation of the machines and the good will of" IBM in the absence of proof that other companies could not make quality cards); *International Salt Co.* v. *United States*, 332 U. S. 392, 397–398 (1947) (rejecting International Salt's claim that it had to control the supply of salt to protect its leased machines in the absence of proof that competitors could not supply salt of equal quality).

Moreover, there are other reasons to question Kodak's proffered motive of commitment to quality service; its quality justification appears inconsistent with its thesis that consumers are knowledgeable enough to lifecycle price, and its self-service policy. Kodak claims the exclusive-service contract is warranted because customers would otherwise blame Kodak equipment for breakdowns resulting from inferior ISO service. Thus, Kodak simultaneously claims that its customers are sophisticated enough to make complex and subtle lifecycle-pricing decisions, and yet too obtuse to distinguish which breakdowns are due to bad equipment and which are due to bad service. Kodak has failed to offer any reason why informational sophistication should be present in one circumstance and absent in the other. In addition, because self-service customers are just as likely as others to blame Kodak equipment for breakdowns resulting from (their own) inferior service, Kodak's willingness to allow self-service casts doubt on its quality claim. In sum, we agree with the Court of Appeals that respondents "have presented evidence from which a reasonable trier of fact could conclude that Kodak's first reason is pretextual." 903 F. 2d, at 618.

There is also a triable issue of fact on Kodak's second justification—controlling inventory costs. As respondents argue, Kodak's actions appear inconsistent with any need to control inventory costs. Presumably, the inventory of parts needed to repair Kodak machines turns only on breakdown rates, and those rates should be the same whether Kodak or ISO's perform the repair. More importantly, the justification fails to explain respondents' evidence that Kodak forced OEM's, equipment owners, and parts brokers not to sell parts to ISO's, actions that would have no effect on Kodak's inventory costs.

Nor does Kodak's final justification entitle it to summary judgment on respondents' § 2 claim. Kodak claims that its policies prevent ISO's from "exploit[ing] the investment Kodak has made in product development, manufacturing and equipment sales in order to take away Kodak's service revenues." Brief for Petitioner 7–8. Kodak does not dispute that respondents invest substantially in the service market, with training of repair workers and investment in parts inventory. Instead, according to Kodak, the ISO's are free-riding because they have failed to enter the equipment and parts markets. This understanding of free-riding has no support in our case law.[33] To the contrary, as the Court of Appeals noted, one of the evils proscribed by the antitrust laws is the creation of entry barriers to potential competitors by requiring them to enter two markets simultaneously. *Jefferson Parish*, 466 U. S., at 14; *Fortner*, 394 U. S., at 509.

None of Kodak's asserted business justifications, then, are sufficient to prove that Kodak is "entitled to a judgment as

[33] Kodak claims that both *Continental T. V.* and *Monsanto* support its free-rider argument. Neither is applicable. In both *Continental T. V.*, 433 U. S., at 55, and *Monsanto*, 465 U. S., at 762–763, the Court accepted free-riding as a justification because without restrictions a manufacturer would not be able to induce competent and aggressive retailers to make the kind of investment of capital and labor necessary to distribute the product. In *Continental T. V.* the relevant market level was retail sale of televisions and in *Monsanto* retail sales of herbicides. Some retailers were investing in those markets; others were not, relying, instead, on the investment of the other retailers. To be applicable to this case, the ISO's would have to be relying on Kodak's investment in the service market; that, however, is not Kodak's argument.

a matter of law" on respondents' § 2 claim. Fed. Rule Civ. Proc. 56(c).

IV

In the end, of course, Kodak's arguments may prove to be correct. It may be that its parts, service, and equipment are components of one unified market, or that the equipment market does discipline the aftermarkets so that all three are priced competitively overall, or that any anticompetitive effects of Kodak's behavior are outweighed by its competitive effects. But we cannot reach these conclusions as a matter of law on a record this sparse. Accordingly, the judgment of the Court of Appeals denying summary judgment is affirmed.

It is so ordered.

JUSTICE SCALIA, with whom JUSTICE O'CONNOR and JUSTICE THOMAS join, dissenting.

This is not, as the Court describes it, just "another case that concerns the standard for summary judgment in an antitrust controversy." *Ante,* at 454. Rather, the case presents a very narrow—but extremely important—question of substantive antitrust law: whether, for purposes of applying our *per se* rule condemning "ties," and for purposes of applying our exacting rules governing the behavior of would-be monopolists, a manufacturer's conceded lack of power in the interbrand market for its equipment is somehow consistent with its possession of "market," or even "monopoly," power in wholly derivative aftermarkets for that equipment. In my view, the Court supplies an erroneous answer to this question, and I dissent.

I

Per se rules of antitrust illegality are reserved for those situations where logic and experience show that the risk of injury to competition from the defendant's behavior is so pronounced that it is needless and wasteful to conduct the usual judicial inquiry into the balance between the behavior's procompetitive benefits and its anticompetitive costs. See, *e. g., Arizona* v. *Maricopa County Medical Society*, 457 U. S. 332, 350–351 (1982). "The character of the restraint produced by [behavior to which a *per se* rule applies] is considered a sufficient basis for presuming unreasonableness without the necessity of any analysis of the market context in which the [behavior] may be found." *Jefferson Parish Hospital Dist. No. 2* v. *Hyde*, 466 U. S. 2, 9 (1984). The *per se* rule against tying is just such a rule: Where the conditions precedent to application of the rule are met, *i. e.*, where the tying arrangement is backed up by the defendant's market power in the "tying" product, the arrangement is adjudged in violation of § 1 of the Sherman Act, 15 U. S. C. § 1 (1988 ed., Supp. II), without *any* inquiry into the practice's actual effect on competition and consumer welfare. But see *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545, 560 (ED Pa. 1960), aff'd, 365 U. S. 567 (1961) *(per curiam)* (accepting affirmative defense to *per se* tying allegation).

Despite intense criticism of the tying doctrine in academic circles, see, *e. g.*, R. Bork, The Antitrust Paradox 365–381 (1978), the stated rationale for our *per se* rule has varied little over the years. When the defendant has genuine "market power" in the tying product—the power to raise price by reducing output—the tie potentially enables him to extend that power into a second distinct market, enhancing barriers to entry in each. In addition:

> "[T]ying arrangements may be used to evade price control in the tying product through clandestine transfer of the profit to the tied product; they may be used as a counting device to effect price discrimination; and they may be used to force a full line of products on the customer so as to extract more easily from him a monopoly return on one unique product in the line." *Fortner Enterprises, Inc.* v. *United States Steel Corp.*, 394 U. S. 495, 513–514 (1969) *(Fortner I)* (WHITE, J., dissenting) (footnotes omitted).

For these reasons, as we explained in *Jefferson Parish,* "the law draws a distinction between the exploitation of market power by merely enhancing the price of the tying product, on the one hand, and by attempting to impose restraints on competition in the market for a tied product, on the other." 466 U. S., at 14.

Our § 2 monopolization doctrines are similarly directed to discrete situations in which a defendant's possession of substantial market power, combined with his exclusionary or anticompetitive behavior, threatens to defeat or forestall the corrective forces of competition and thereby sustain or extend the defendant's agglomeration of power. See *United States* v. *Grinnell Corp.,* 384 U. S. 563, 570–571 (1966). Where a defendant maintains substantial market power, his activities are examined through a special lens: Behavior that might otherwise not be of concern to the antitrust laws—or that might even be viewed as procompetitive—can take on exclusionary connotations when practiced by a monopolist. 3 P. Areeda & D. Turner, Antitrust Law ¶ 813, pp. 300–302 (1978) (hereinafter 3 Areeda & Turner).

The concerns, however, that have led the courts to heightened scrutiny both of the "exclusionary conduct" practiced by a monopolist and of tying arrangements subject to *per se* prohibition, are completely without force when the participants lack market power. As to the former, "[t]he [very] definition of exclusionary conduct," as practiced by a monopolist, is "predicated on the existence of substantial market power." *Id.,* ¶ 813, at 301; see, *e. g., Walker Process Equipment, Inc.* v. *Food Machinery & Chemical Corp.,* 382 U. S. 172, 177–178 (1965) (fraudulent patent procurement); *Standard Oil Co. of New Jersey* v. *United States,* 221 U. S. 1, 75 (1911) (acquisition of competitors); 3 Areeda & Turner ¶ 724, at 195–197 (vertical integration). And with respect to tying, we have recognized that bundling arrangements not coerced by the heavy hand of market power can serve the procompetitive functions of facilitating new entry into certain markets, see, *e. g., Brown Shoe Co.* v. *United States,* 370 U. S. 294, 330 (1962), permitting "clandestine price cutting in products which otherwise would have no price competition at all because of fear of retaliation from the few other producers dealing in the market," *Fortner I, supra,* at 514, n. 9 (WHITE, J., dissenting), assuring quality control, see, *e. g., Standard Oil Co. of Cal.* v. *United States,* 337 U. S. 293, 306 (1949), and, where "the tied and tying products are functionally related, . . . reduc[ing] costs through economies of joint production and distribution." *Fortner I, supra,* at 514, n. 9 (WHITE, J., dissenting). "Accordingly, we have [only] condemned tying arrangements [under the *per se* rule] when the seller has some special ability—usually called 'market power'—to force a purchaser to do something that he would not do in a competitive market." *Jefferson Parish, supra,* at 13–14.

The Court today finds in the typical manufacturer's inherent power over its own brand of equipment—over the sale of distinctive repair parts for that equipment, for example—the sort of "monopoly power" sufficient to bring the sledgehammer of § 2 into play. And, not surprisingly in light of that insight, it readily labels single-brand power over aftermarket products "market power" sufficient to permit an antitrust plaintiff to invoke the *per se* rule against tying. In my opinion, this makes no economic sense. The holding that market power can be found on the present record causes these venerable rules of selective proscription to extend well beyond the point where the reasoning that supports them leaves off. Moreover, because the sort of power condemned by the Court today is possessed by every manufacturer of durable goods with distinctive parts, the Court's opinion threatens to release a torrent of litigation and a flood of commercial intimidation that will do much more harm than good to enforcement of the antitrust laws and to genuine competition. I shall explain, in Parts II and III, respectively, how neither logic *nor* experience suggests, let alone compels, application of the *per se* tying prohibition and monopolization doctrine to a seller's behavior in its single-brand aftermarkets, when that seller is without power at the interbrand level.

II

On appeal in the Ninth Circuit, respondents, having waived their "rule of reason" claim, were limited to arguing that the record, construed in the light most favorable to them, *Anderson* v. *Liberty Lobby, Inc.*, 477 U. S. 242, 255 (1986), supported application of the *per se* tying prohibition to Kodak's restrictive parts and service policy. See 903 F. 2d 612, 615, n. 1 (1990). As the Court observes, in order to survive Kodak's motion for summary judgment on this claim, respondents bore the burden of proffering evidence on which a reasonable trier of fact could conclude that Kodak possesses power in the market for the alleged "tying" product. See *ante*, at 464; *Jefferson Parish*, 466 U. S., at 13–14.

A

We must assume, for purposes of deciding this case, that petitioner is without market, much less monopoly, power in the interbrand markets for its micrographic and photocopying equipment. See *ante*, at 465–466, n. 10; *Oklahoma City* v. *Tuttle*, 471 U. S. 808, 816 (1985). In the District Court, respondents did, in fact, include in their complaint an allegation which posited the interbrand equipment markets as the relevant markets; in particular, they alleged a § 1 "tie" of micrographic and photocopying equipment to the parts and service for those machines. App. 22–23. Though this allegation was apparently abandoned in pursuit of §§ 1 and 2 claims focused exclusively on the parts and service aftermarkets (about which more later), I think it helpful to analyze how that claim would have fared under the *per se* rule.

Had Kodak—from the date of its entry into the micrographic and photocopying equipment markets—included a lifetime parts and service warranty with all original equipment, or required consumers to purchase a lifetime parts and service contract with each machine, that bundling of equipment, parts, and service would no doubt constitute a tie under the tests enunciated in *Jefferson Parish, supra.* Nevertheless, it would be immune from *per se* scrutiny under the antitrust laws because the *tying* product would be *equipment,* a market in which (we assume) Kodak has no power to influence price or quantity. See *id.,* at 13–14; *United States Steel Corp.* v. *Fortner Enterprises, Inc.,* 429 U. S. 610, 620 (1977) *(Fortner II); Northern Pacific R. Co.* v. *United States,* 356 U. S. 1, 6–7 (1958). The same result would obtain, I think, had Kodak—from the date of its market entry—consistently pursued an announced policy of limiting parts sales in the manner alleged in this case, so that customers bought with the knowledge that aftermarket support could be obtained only from Kodak. The foreclosure of respondents from the business of servicing Kodak's micrographic and photocopying machines in these illustrations would be undeniably complete—as complete as the foreclosure described in respondents' complaint. Nonetheless, we would inquire no further than to ask whether Kodak's *market power* in the equipment market effectively forced consumers to purchase Kodak micrographic or photocopying machines subject to the company's restrictive aftermarket practices. If not, that would end the case insofar as the *per se* rule was concerned. See *Jefferson Parish, supra,* at 13–14; 9 P. Areeda, Antitrust Law ¶ 1709c5, pp. 101–102 (1991); Klein & Saft, The Law and Economics of Franchise Tying Contracts, 28 J. Law & Econ. 345, 356 (1985). The evils against which the tying prohibition is directed would simply not be presented. Interbrand competition would render Kodak powerless to gain economic power over an additional class of consumers, to price discriminate by charging each customer a "system" price equal to the system's economic value to that customer, or to raise barriers to entry in the interbrand equipment markets. See 3 Areeda & Turner ¶ 829d, at 331–332.

I have described these illustrations as hypothetical, but in fact they are not far removed from this case. The record below is consistent—in large part—with just this sort of bundling of equipment on the one hand, with parts and service on the other. The restrictive parts policy, with respect to micrographic equipment at least, was not even alleged to be anything but prospective. See App. 17. As respondents summarized their factual proffer below:

> "Under this policy, Kodak cut off parts on new products to Kodak micrographics [independent service organizations] ISOs. The effect of this, of course, was that as customers of Kodak micrographics ISOs obtained new equipment, the ISOs were unable to service the equipment for that customer, and, service for these customers was lost by the Kodak ISOs. Additionally, as equipment became obsolete, and the equipment population became all "new equipment" (post April 1985 models), Kodak micrographics ISOs would be able to service no equipment at all." *Id.*, at 360.

As to Kodak copiers, Kodak's restrictive parts policy had a broader foundation: Considered in the light most favorable to respondents, see *Anderson, supra,* at 255, the record suggests that, from its inception, the policy was applied to new and existing copier customers alike. But at least all post-1985 purchasers of micrographic equipment, like all post-1985 purchasers of new Kodak copiers, could have been aware of Kodak's parts practices. The only thing lacking to bring all of these purchasers (accounting for the vast bulk of the commerce at issue here) squarely within the hypotheticals we have described is concrete evidence that the restrictive parts policy was announced or generally known. Thus, under the Court's approach the existence *vel non* of such evidence is determinative of the legal standard (the *per se* rule versus the rule of reason) under which the alleged tie is examined. In my judgment, this makes no sense. It is quite simply anomalous that a manufacturer functioning in a competitive equipment market should be exempt from the *per se* rule when it bundles equipment with parts and service, but not when it bundles parts with service. This vast difference in the treatment of what will ordinarily be economically similar phenomena is alone enough to call today's decision into question.

B

In the Court of Appeals, respondents sought to sidestep the impediment posed by interbrand competition to their invocation of the *per se* tying rule by zeroing in on the parts and service "aftermarkets" for Kodak equipment. By alleging a tie of *parts* to service, rather than of *equipment* to parts and service, they identified a tying product in which Kodak unquestionably held a near-monopoly share: the parts uniquely associated with Kodak's brand of machines. See *Jefferson Parish*, 466 U. S., at 17. The Court today holds that such a facial showing of market share in a single-brand aftermarket is sufficient to invoke the *per se* rule. The existence of even vibrant interbrand competition is no defense. See *ante*, at 470–471.

I find this a curious form of market power on which to premise the application of a *per se* proscription. It is enjoyed by virtually every manufacturer of durable goods requiring aftermarket support with unique, or relatively unique, goods. See P. Areeda & H. Hovenkamp, Antitrust Law ¶ 525.1, p. 563 (Supp. 1991). "[S]uch reasoning makes every maker of unique parts for its own product a holder of market power *no matter how unimportant its product might be in the market.*" *Ibid.* (emphasis added).[1] Under

[1] That there exist innumerable parts and service firms in such industries as the automobile industry, see Brief for Automotive Warehouse Distributors Association et al. as *Amici Curiae* 2–3, does not detract from this point. The question whether power to control an aftermarket exists is quite distinct from the question whether the power has been exercised. Manufacturers in some markets have no doubt determined that exclusion-

the Court's analysis, the *per se* rule may now be applied to single-brand ties effected by the most insignificant players in fully competitive interbrand markets, as long as the arrangement forecloses aftermarket competitors from more than a *de minimis* amount of business, *Fortner I*, 394 U. S., at 501. This seems to me quite wrong. A tying arrangement "forced" through the exercise of such power no more implicates the leveraging and price discrimination concerns behind the *per se* tying prohibition than does a tie of the foremarket brand to its aftermarket derivatives, which—as I have explained—would not be subject to *per se* condemnation.[2] As implemented, the Kodak arrangement challenged

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ary intrabrand conduct works to their disadvantage at the competitive interbrand level, but this in no way refutes the self-evident reality that control over unique replacement parts for single-branded goods is ordinarily available to such manufacturers for the taking. It confounds sound analysis to suggest, as respondents do, see Brief for Respondents 5, 37, that the asserted fact that Kodak manufactures only 10% of its replacement parts, and purchases the rest from original equipment manufacturers, casts doubt on Kodak's possession of an inherent advantage in the aftermarkets. It does no such thing, any more than Kodak's contracting with others for the manufacture of all constituent parts included in its original equipment would alone suggest that Kodak lacks power in the *interbrand* micrographic and photocopying equipment markets. The suggestion implicit in respondents' analysis—that if a seller chooses to contract for the manufacture of its branded merchandise, it must permit the contractors to compete in the sale of that merchandise—is plainly unprecedented.

[2] Even *with* interbrand power, I may observe, it is unlikely that Kodak could have incrementally exploited its position through the tie of parts to service alleged here. Most of the "service" at issue is inherently associated with the parts, *i. e.*, that service involved in incorporating the parts into Kodak equipment, and the two items tend to be demanded by customers in fixed proportions (one part with one unit of service necessary to install the part). When that situation obtains, "'no revenue can be derived from setting a higher price for the tied product which could not have been made by setting the optimum price for the tying product.'" P. Areeda & L. Kaplow, Antitrust Analysis ¶ 426(a), p. 706 (4th ed. 1988) (quoting Bowman, Tying Arrangements and the Leverage Problem, 67 Yale L. J. 19 (1957)). These observations strongly suggest that Kodak

in this case may have implicated truth-in-advertising or other consumer protection concerns, but those concerns do not alone suggest an antitrust prohibition. See, *e. g., Town Sound and Custom Tops, Inc.* v. *Chrysler Motors Corp.*, 959 F. 2d 468 (CA3 1992) (en banc).

In the absence of interbrand power, a seller's predominant or monopoly share of its single-brand derivative markets does not connote the power to raise derivative market prices *generally* by reducing quantity. As Kodak and its principal *amicus,* the United States, point out, a rational consumer considering the purchase of Kodak equipment will inevitably factor into his purchasing decision the expected cost of aftermarket support. "[B]oth the price of the equipment and the price of parts and service over the life of the equipment are expenditures that are necessary to obtain copying and micrographic services." Brief for United States as *Amicus Curiae* 13. If Kodak set generally supracompetitive prices for either spare parts or repair services without making an offsetting reduction in the price of its machines, rational consumers would simply turn to Kodak's competitors for photocopying and micrographic systems. See, *e. g., Grappone, Inc.* v. *Subaru of New England, Inc.*, 858 F. 2d 792, 796–798 (CA1 1988). True, there are—as the Court notes, see *ante*, at 474–475—the occasional irrational consumers that consider only the hardware cost at the time of purchase (a category that regrettably includes the Federal Government, whose "purchasing system," we are told, assigns foremarket purchases and aftermarket purchases to different entities). But

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parts and the service involved in installing them should not be treated as distinct products for antitrust tying purposes. See *Jefferson Parish Hospital Dist. No. 2* v. *Hyde,* 466 U. S. 2, 39 (1984) (O'CONNOR, J., concurring in judgment) ("For products to be treated as distinct, the tied product must, at a minimum, be one that some consumers might wish to purchase separately *without also purchasing the tying product*") (emphasis in original) (footnote omitted); Ross, The Single Product Issue in Antitrust Tying: A Functional Approach, 23 Emory L. J. 963, 1009–1010 (1974).

we have never before premised the application of antitrust doctrine on the lowest common denominator of consumer.

The Court attempts to counter this theoretical point with a theory of its own. It says that there are "information costs"—the costs and inconvenience to the consumer of acquiring and processing life-cycle pricing data for Kodak machines—that "could create a less responsive connection between service and parts prices and equipment sales." *Ante*, at 473. But this truism about the functioning of markets for sophisticated equipment cannot create "market power" of concern to the antitrust laws where otherwise there is none. "Information costs," or, more accurately, gaps in the availability and quality of consumer information, pervade real-world markets; and because consumers generally make do with "rough cut" judgments about price in such circumstances, in virtually any market there are zones within which otherwise competitive suppliers may overprice their products without losing appreciable market share. We have never suggested that the principal players in a market with such commonplace informational deficiencies (and, thus, bands of apparent consumer pricing indifference) exercise market power in any sense relevant to the antitrust laws. "While [such] factors may generate 'market power' in some abstract sense, they do not generate the kind of market power that justifies condemnation of tying." *Jefferson Parish,* 466 U. S., at 27; see, *e. g., Town Sound and Custom Tops, Inc.* v. *Chrysler Motors Corp., supra.*

Respondents suggest that, even if the existence of interbrand competition prevents Kodak from raising prices *generally* in its single-brand aftermarkets, there remain certain consumers who are necessarily subject to abusive Kodak pricing behavior by reason of their being "locked in" to their investments in Kodak machines. The Court agrees; indeed, it goes further by suggesting that even a *general* policy of supracompetitive aftermarket prices might be profitable over the long run because of the "lock-in" phenomenon. "[A] seller profitably could maintain supracompetitive prices in the aftermarket," the Court explains, "if the switching costs were high relative to the increase in service prices, and the number of locked-in customers were high relative to the number of new purchasers." *Ante,* at 476. In speculating about this latter possibility, the Court is essentially repudiating the assumption on which we are bound to decide this case, viz., Kodak's lack of any power whatsoever in the interbrand market. If Kodak's *general* increase in aftermarket prices were to bring the total "system" price above competitive levels in the interbrand market, Kodak would be wholly unable to make further foremarket sales—and would find itself exploiting an ever-dwindling aftermarket, as those Kodak micrographic and photocopying machines already in circulation passed into disuse.

The Court's narrower point, however, is undeniably true. There will be consumers who, because of their capital investment in Kodak equipment, "will tolerate some level of service-price increases before changing equipment brands," *ibid.;* this is *necessarily* true for "every maker of unique parts for its own product." Areeda & Hovenkamp, Antitrust Law ¶ 525.1b, at 563. But this "circumstantial" leverage created by consumer investment regularly crops up in smoothly functioning, even perfectly competitive, markets, and in most—if not all—of its manifestations, it is of no concern to the antitrust laws. The leverage held by the manufacturer of a malfunctioning refrigerator (which is measured by the consumer's reluctance to walk away from his initial investment in that device) is no different in kind or degree from the leverage held by the swimming pool contractor when he discovers a 5-ton boulder in his customer's backyard and demands an additional sum of money to remove it; or the leverage held by an airplane manufacturer over an airline that has "standardized" its fleet around the manufacturer's models; or the leverage held by a drill press manufacturer whose customers have built their production lines around the manufacturer's particular style of drill press; or the leverage held by an insurance company over its independent sales force that has invested in company-specific paraphernalia; or the leverage held by a mobile home park owner over his tenants, who are unable to transfer their homes to a different park except at great expense, see generally *Yee* v. *Escondido*, 503 U. S. 519 (1992). Leverage, in the form of *circumstantial* power, plays a role in each of these relationships; but in none of them is the leverage attributable to the dominant party's *market* power in any relevant sense. Though that power can plainly work to the injury of certain consumers, it produces only "a brief perturbation in competitive conditions—not the sort of thing the antitrust laws do or should worry about." *Parts & Elec. Motors, Inc.* v. *Sterling Elec., Inc.*, 866 F. 2d 228, 236 (CA7 1988) (Posner, J., dissenting).

The Court correctly observes that the antitrust laws do not permit even a *natural* monopolist to project its monopoly power into another market, *i. e.*, to " 'exploi[t] his dominant position in one market to expand his empire into the next.' " *Ante*, at 480, n. 29 (quoting *Times-Picayune Publishing Co.* v. *United States*, 345 U. S. 594, 611 (1953)). However, when a manufacturer uses its control over single-branded parts to acquire influence in single-branded service, the monopoly "leverage" is almost invariably of no practical consequence, because of perfect identity between the consumers in each of the subject aftermarkets (those who need replacement parts for Kodak equipment and those who need servicing of Kodak equipment). When that condition exists, the tie does not permit the manufacturer to project power over a class of consumers distinct from that which it is already able to exploit (and fully) without the inconvenience of the tie. Cf., *e. g.*, Bowman, Tying Arrangements and the Leverage Problem, 67 Yale L. J. 19, 21–27 (1957).

We have never before accepted the thesis the Court today embraces: that a seller's inherent control over the unique parts for its own brand amounts to "market power" of a character sufficient to permit invocation of the *per se* rule against tying. As the Court observes, *ante,* at 479–481, n. 29, we have applied the *per se* rule to manufacturer ties of *foremarket* equipment to aftermarket derivatives—but only when the manufacturer's monopoly power in the equipment, coupled with the use of derivative sales as "counting devices" to measure the intensity of customer equipment usage, enabled the manufacturer to engage in price discrimination, and thereby more fully exploit its interbrand power. See *International Salt Co.* v. *United States,* 332 U. S. 392 (1947); *International Business Machines Corp.* v. *United States,* 298 U. S. 131 (1936); *United Shoe Machinery Corp.* v. *United States,* 258 U. S. 451 (1922). That sort of enduring opportunity to engage in price discrimination is unavailable to a manufacturer—like Kodak—that lacks power at the interbrand level. A tie between two aftermarket derivatives does next to nothing to improve a competitive manufacturer's ability to extract monopoly rents from its consumers.[3]

[3] The Court insists that the record in this case suggests otherwise, *i. e.,* that a tie between parts and service somehow *does* enable Kodak to increase overall monopoly profits. See *ante,* at 479–481, n. 29. Although the Court does not identify the record evidence on which it relies, the suggestion, apparently, is that such a tie facilitates price discrimination between sophisticated, "high-volume" users of Kodak equipment and their unsophisticated counterparts. The sophisticated users (who, the Court presumes, invariably self-service their equipment) are permitted to buy Kodak parts without also purchasing supracompetitively priced Kodak service, while the unsophisticated are—through the imposition of the tie—compelled to buy both. See *ante,* at 475–476.

While superficially appealing, at bottom this explanation lacks coherence. Whether they self-service their equipment or not, rational foremarket consumers (those consumers who are not yet "locked in" to Kodak hardware) will be driven to Kodak's competitors if the price of Kodak equipment, together with the expected cost of aftermarket support, exceeds competitive levels. This will be true no matter how Kodak distributes the total system price among equipment, parts, and service. See

Nor has any court of appeals (save for the Ninth Circuit panel below) recognized single-branded aftermarket power as a basis for invoking the *per se* tying prohibition. See *Virtual Maintenance, Inc.* v. *Prime Computer, Inc.*, 957 F. 2d 1318, 1328 (CA6 1992) ("Defining the market by customer demand *after* the customer has chosen a single supplier fails to take into account that the supplier . . . must compete with other similar suppliers to be designated the

supra, at 495. Thus, as to these consumers, Kodak's lack of interbrand power wholly prevents it from employing a tie between parts and service as a vehicle for price discrimination. Nor does a tie between parts and service offer Kodak incremental exploitative power over those consumers—sophisticated or not—who have the supposed misfortune of being "locked in" to Kodak equipment. If Kodak desired to exploit its circumstantial power over this wretched class by pressing them up to the point where the cost to each consumer of switching equipment brands barely exceeded the cost of retaining Kodak equipment and remaining subject to Kodak's abusive practices, it could plainly do so without the inconvenience of a tie, through supracompetitive parts pricing alone. Since the locked-in *sophisticated* parts purchaser is as helpless as the locked-in *unsophisticated* one, I see nothing to be gained by price discrimination in favor of the former. If such price discrimination were desired, however, it would not have to be accomplished indirectly, through a tie of parts to service. Section 2(a) of the Robinson-Patman Act, 15 U. S. C. § 13(a), would prevent giving lower parts prices to the sophisticated customers only "where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them . . . ." *Ibid.;* see, *e. g., Falls City Industries, Inc.* v. *Vanco Beverage, Inc.*, 460 U. S. 428, 434–435 (1983). That prohibited effect often occurs when price-discriminated goods are sold for resale (*i. e.,* to purchasers who are necessarily in competition with one another). *E. g., FTC* v. *Morton Salt Co.*, 334 U. S. 37, 47 (1948); see P. Areeda & L. Kaplow, Antitrust Analysis ¶ 600, p. 923 (1988) ("Secondary-line injury arises [under the Robinson-Patman Act] when a powerful firm buying supplies at favorable prices thereby gains a decisive advantage over its competitors that are forced to pay higher prices for their supplies"). It rarely occurs where, as would be the case here, the price-discriminated goods are sold to various businesses for consumption.

sole source in the first place"); *Grappone, Inc.* v. *Subaru of New England, Inc.*, 858 F. 2d, at 798 ("[W]e do not see how such dealer investment [in facilities to sell Subaru products] . . . could easily translate into Subaru market power of a kind that, through tying, could ultimately lead to higher than competitive prices for consumers"); *A. I. Root Co.* v. *Computer/Dynamics, Inc.*, 806 F. 2d 673, 675–677, and n. 3 (CA6 1986) (competition at "small business computer" level precluded assertion of computer manufacturer's power over software designed for use only with manufacturer's brand of computer); *General Business Systems* v. *North American Philips Corp.*, 699 F. 2d 965, 977 (CA9 1983) ("To have attempted to impose significant pressure to buy [aftermarket hardware] by use of the tying service only would have hastened the date on which Philips surrendered to its competitors in the small business computer market"). See also *Parts & Elec. Motors, Inc.* v. *Sterling Elec., Inc.*, 866 F. 2d, at 233 (law-of-the-case doctrine compelled finding of market power in replacement parts for single-brand engine).

We have recognized in closely related contexts that the deterrent effect of *inter*brand competition on the exploitation of *intra*brand market power should make courts exceedingly reluctant to apply rules of *per se* illegality to intrabrand restraints. For instance, we have refused to apply a rule of *per se* illegality to vertical nonprice restraints "because of their potential for a simultaneous reduction of intrabrand competition and stimulation of interbrand competition," *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 51–52 (1977), the latter of which we described as "the primary concern of antitrust law," *id.*, at 52, n. 19. We noted, for instance, that "new manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer," and that "[e]stablished manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products." *Id.*, at 55. See also *Business Electronics Corp.* v. *Sharp Electronics Corp.*, 485 U. S. 717, 726 (1988). The same assumptions, in my opinion, should govern our analysis of ties alleged to have been "forced" solely through *intra*brand market power. In the absence of interbrand power, a manufacturer's bundling of aftermarket products may serve a multitude of legitimate purposes: It may facilitate manufacturer efforts to ensure that the equipment remains operable and thus protect the seller's business reputation, see *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp., at 560; it may create the conditions for implicit consumer financing of the acquisition cost of the tying equipment through supracompetitively-priced aftermarket purchases, see, *e. g.*, A. Oxenfeldt, Industrial Pricing and Market Practices 378 (1951); and it may, through the resultant manufacturer control of aftermarket activity, "yield valuable information about component or design weaknesses that will materially contribute to product improvement," 3 Areeda & Turner ¶ 733c, at 258–259; see also *id.*, ¶ 829d, at 331–332. Because the interbrand market will generally punish intrabrand restraints that consumers do not find in their interest, we should not—under the guise of a *per se* rule—condemn such potentially procompetitive arrangements simply because of the antitrust defendant's inherent power over the unique parts for its own brand.

I would instead evaluate the aftermarket tie alleged in this case under the rule of reason, where the tie's *actual* anticompetitive effect in the tied product market, together with its potential economic benefits, can be fully captured in the analysis, see, *e. g.*, *Jefferson Parish*, 466 U. S., at 41 (O'CONNOR, J., concurring in judgment). Disposition of this case does not require such an examination, however, as respondents apparently waived any rule-of-reason claim they may have had in the District Court. I would thus reverse the Ninth Circuit's judgment on the tying claim outright.

III

These considerations apply equally to respondents' § 2 claims. An antitrust defendant lacking relevant "market power" sufficient to permit invocation of the *per se* prohibition against tying *a fortiori* lacks the monopoly power that warrants heightened scrutiny of his allegedly exclusionary behavior. Without even so much as asking whether the purposes of § 2 are implicated here, the Court points to Kodak's control of "100% of the parts market and 80% to 95% of the service market," markets with "no readily available substitutes," *ante*, at 481, and finds that the proffer of such statistics is sufficient to fend off summary judgment. But this showing could easily be made, as I have explained, with respect to virtually any manufacturer of differentiated products requiring aftermarket support. By permitting antitrust plaintiffs to invoke § 2 simply upon the unexceptional demonstration that a manufacturer controls the supplies of its single-branded merchandise, the Court transforms § 2 from a specialized mechanism for responding to extraordinary agglomerations (or threatened agglomerations) of economic power to an all-purpose remedy against run-of-the-mill business torts.

In my view, if the interbrand market is vibrant, it is simply not necessary to enlist § 2's machinery to police a seller's intrabrand restraints. In such circumstances, the interbrand market functions as an infinitely more efficient and more precise corrective to such behavior, rewarding the seller whose intrabrand restraints enhance consumer welfare while punishing the seller whose control of the aftermarkets is viewed unfavorably by interbrand consumers. See *Business Electronics Corp., supra,* at 725; *Continental T. V., Inc., supra,* at 52, n. 19, 54. Because this case comes to us on the assumption that Kodak is without such interbrand power, I believe we are compelled to reverse the judgment of the Court of Appeals. I respectfully dissent.

Mixed Bundling

FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

CASCADE HEALTH SOLUTIONS fka MCKENZIE-WILLAMETTE HOSPITAL, an Oregon nonprofit corporation, *Plaintiff-Appellant,* v. PEACEHEALTH, a Washington State nonprofit corporation, *Defendant-Appellee,* and PACIFICSOURCE HEALTH PLANS, *Defendant,* REGENCE BLUECROSS BLUESHIELD OF OREGON; PROVIDENCE HEALTH PLAN; MCKENZIE-WILLAMETTE REGIONAL MEDICAL CENTER ASSOCIATES, LLC, *Defendant-Intervenors.*	No. 05-35627 D.C. No. CV-02-06032-ALH

MCKENZIE-WILLAMETTE HOSPITAL, *Plaintiff-Appellee,* v. PEACEHEALTH, a Washington State nonprofit corporation, *Defendant-Appellant,* and PACIFICSOURCE HEALTH PLANS, *Defendant,* REGENCE BLUECROSS BLUESHIELD OF OREGON; PROVIDENCE HEALTH PLAN; MCKENZIE-WILLAMETTE REGIONAL MEDICAL CENTER ASSOCIATES, LLC, *Defendant-Intervenors.*	No. 05-35640 D.C. No. CV-02-06032-HA
MCKENZIE-WILLAMETTE HOSPITAL, *Plaintiff-Appellee,* v. PEACEHEALTH, a Washington State nonprofit corporation, *Defendant-Appellant.*	No. 05-36153 D.C. No. CV-02-06032-HA

MCKENZIE-WILLAMETTE HOSPITAL, an Oregon nonprofit corporation, *Plaintiff-Appellant*, v. PEACEHEALTH, *Defendant-Appellee.*	No. 05-36202 D.C. No. CV-02-06032-HA ORDER AMENDING OPINION AND AMENDED OPINION

Appeal from the United States District Court
for the District of Oregon
Ancer L. Haggerty, District Judge, Presiding

Argued and Submitted
March 6, 2007—Portland, Oregon

Filed September 4, 2007
Amended February 1, 2008

Before: Ronald M. Gould, Richard A. Paez, and
Johnnie B. Rawlinson, Circuit Judges.

Opinion by Judge Gould

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ORDER

In a separate order filed concurrently with this order, we certified a question on Oregon price discrimination law to the Oregon Supreme Court. Accordingly, the opinion filed on September 4, 2007 is AMENDED as follows.

First, the last paragraph before section "I," originally:

> We vacate the jury's verdict in favor of McKenzie on the attempted monopolization, price discrimination, and tortious interference claims, and we vacate the district court's summary judgment in favor of PeaceHealth on the tying claim. We also vacate the district court's award of attorneys' fees, costs, and expenses. We remand for further proceedings.

shall be replaced by the paragraph:

> We vacate the jury's verdict in favor of McKenzie on the attempted monopolization and tortious interference claims, and we vacate the district court's summary judgment in favor of PeaceHealth on the

> tying claim. We also vacate the district court's award of attorneys' fees, costs, and expenses. We certify a question to the Oregon Supreme Court on the price discrimination claim. We stay further proceedings pending resolution of the price discrimination question certified to the Oregon Supreme Court.

Second, the entire text of the section titled "II B," concerning Oregon state price discrimination law, shall be replaced with:

> After trial, the jury also returned a verdict in favor of McKenzie on its claim of primary-line price discrimination under Oregon state law. Because the validity of that jury verdict rests upon an unsettled question of Oregon antitrust law, we have certified that question to the Oregon Supreme Court.

Third, the section titled "IV," originally:

> The final issue before us is the appeal and cross-appeal of the district court's award of attorneys' fees and costs to McKenzie. Because we have vacated the district court's judgment in favor of McKenzie on the merits of McKenzie's attempted monopolization, price discrimination, and tortious interference claims, McKenzie is no longer a prevailing party for the purposes of Federal Rule of Civil Procedure 54(d)(1) and § 4(a) of the Clayton Act, 15 U.S.C. § 15(a). McKenzie is thus not entitled to attorneys' fees, costs, and expenses, and we vacate the district court's order awarding fees, costs, and expenses to McKenzie. If McKenzie prevails on remand, it may renew its request for attorneys' fees and costs. We dismiss McKenzie's cross-appeal on attorneys' fees and costs as moot.

shall be replaced with:

> The final issue before us is the appeal and cross-appeal of the district court's award of attorneys' fees and costs to McKenzie. Because we have vacated the district court's judgment in favor of McKenzie on the merits of McKenzie's attempted monopolization and tortious interference claims, McKenzie is no longer a prevailing party for the purposes of Federal Rule of Civil Procedure 54(d)(1) and § 4(a) of the Clayton Act, 15 U.S.C. § 15(a). McKenzie is thus not entitled to attorneys' fees, costs, and expenses, and we vacate the district court's order awarding fees, costs, and expenses to McKenzie for those claims. If McKenzie prevails on remand, it may renew its request for attorneys' fees and costs. We dismiss McKenzie's cross-appeal on attorneys' fees and costs as moot. We withhold a determination of attorneys' fees, costs, and expenses for McKenzie's price discrimination claim pending resolution of the question certified to the Oregon Supreme Court.

Fourth, the section titled "V," originally:

> To summarize: In No. 05-35640, we **VACATE** the judgment in favor of McKenzie and **REMAND** for further proceedings. In No. 05-35627, we **VACATE** the summary judgment in favor of PeaceHealth and **REMAND** for further proceedings. In No. 05-36153, we **VACATE** the district court's order awarding attorneys' fees and costs to McKenzie. In No. 05-36202, we **DISMISS** the appeal as moot. Each party shall bear its own costs on appeal.

shall be replaced with:

> To summarize: In No. 05-35640, we **VACATE** the judgment in favor of McKenzie on its monopolization and tortious interference claims. We certify a question to the Oregon Supreme Court on the price

> discrimination claim. In No. 05-35627, we **VACATE** the summary judgment in favor of PeaceHealth. In No. 05-36153, we **VACATE** the district court's order awarding attorneys' fees and costs to McKenzie. In No. 05-36202, we **DISMISS** the appeal as moot. Each party shall bear its own costs on appeal. We **STAY** further proceedings pending resolution of the price discrimination question certified to the Oregon Supreme Court.

and the footnote that was originally footnote 31 with the following text:

> In No. 05-35627, we also decline to address McKenzie's *Noerr-Pennington* arguments because these related to an evidentiary ruling and the issue may not arise on a retrial. Further, we hold that the district court's jury instruction on combination or conspiracy was not an abuse of discretion.

shall be placed at the conclusion of the amended sentence:

> In No. 05-35627, we **VACATE** the summary judgment in favor of PeaceHealth.

OPINION

GOULD, Circuit Judge:

McKenzie-Willamette Hospital ("McKenzie") filed a complaint in the district court against PeaceHealth asserting seven claims for relief. Five of the claims arose under the federal antitrust laws: monopolization, attempted monopolization, conspiracy to monopolize, tying, and exclusive dealing. The other two claims arose under Oregon state law: price discrimination and intentional interference with prospective economic advantage.

Before trial, the district court granted summary judgment in favor of PeaceHealth on McKenzie's tying claim. After a two-and-a-half-week trial, the jury rendered a verdict in favor of PeaceHealth on McKenzie's claims of monopolization, conspiracy to monopolize, and exclusive dealing. However, the jury found in favor of McKenzie on McKenzie's claims of attempted monopolization, price discrimination, and tortious interference. The jury awarded McKenzie $5.4 million in damages, which the district court trebled for a final award of $16.2 million. The district court also awarded McKenzie $1,583,185.57 in attorneys' fees, costs, and expenses.

We vacate the jury's verdict in favor of McKenzie on the attempted monopolization and tortious interference claims, and we vacate the district court's summary judgment in favor of PeaceHealth on the tying claim. We also vacate the district court's award of attorneys' fees, costs, and expenses. We certify a question to the Oregon Supreme Court on the price discrimination claim. We stay further proceedings pending resolution of the price discrimination question certified to the Oregon Supreme Court.

I

A

McKenzie and PeaceHealth are the only two providers of hospital care in Lane County, Oregon. The jury found and, for the purposes of this appeal, the parties do not dispute, that the relevant market in this case is the market for primary and secondary acute care hospital services in Lane County. Primary and secondary acute care hospital services are common medical services like setting a broken bone and performing a tonsillectomy. Some hospitals also provide what the parties call "tertiary care," which includes more complex services like invasive cardiovascular surgery and intensive neonatal care.

In Lane County, PeaceHealth operates three hospitals while McKenzie operates one. McKenzie's sole endeavor is McKenzie-Willamette Hospital, a 114-bed hospital that offers primary and secondary acute care in Springfield, Oregon. McKenzie does not provide tertiary care. In the time period leading up to and including this litigation, McKenzie had been suffering financial losses, and, as a result, merged with Triad Hospitals, Inc.[1] so that it could add tertiary services to its menu of care.

The largest of PeaceHealth's three facilities is Sacred Heart Hospital, a 432-bed operation that offers primary, secondary, and tertiary care in Eugene, Oregon. PeaceHealth also operates Peace Harbor Hospital, a 21-bed hospital in Florence, Oregon and Cottage Grove Hospital, an 11-bed hospital in Cottage Grove, Oregon. In Lane County, PeaceHealth has a 90% market share of tertiary neonatal services, a 93% market share of tertiary cardiovascular services, and a roughly 75% market share of primary and secondary care services.

To understand the antitrust issues in this case, it is necessary to appreciate the structure of the market in which this case arises. The market for hospital services and medical care is complex. However, based on the record, there appear to be three major participants in the market for hospital services: hospitals, insurers, and patients. Hospitals, like those operated by PeaceHealth and McKenzie, provide services to patients and sell services to insurers. Insurers are usually commercial health insurance companies that seek to buy medical services from hospitals on the best terms possible. The insurers in turn sell insurance services to patients and employers. Patients buy health insurance from insurers (often through their employers) and sometimes buy services from hospitals.

[1]As a result of the merger, McKenzie's name changed to Cascade Health Solutions. For the purposes of this opinion, we, like the parties, continue to refer to Cascade Health Solutions as McKenzie.

In the transaction between a hospital that sells care services and an insurer that buys care services, the price agreed upon is often referred to as a "reimbursement rate." For example, in a hospital-insurer contract, the agreed upon price might be "a 90% reimbursement rate." A 90% reimbursement rate price means that, when the insurer must purchase services from the hospital, the insurer gets a 10% discount off the hospital's regular price, also called the charge master or list price. It follows that hospitals prefer high reimbursement rates and insurers prefer low reimbursement rates, as each group pursues its own economic interest.

B

Before trial, the district court granted summary judgment to PeaceHealth on McKenzie's tying claim, concluding that McKenzie had not presented any evidence that PeaceHealth "coerced" insurers into purchasing primary and secondary services from it in order for the insurers to obtain tertiary services. The district court let the remainder of McKenzie's claims proceed to trial before a jury. On McKenzie's monopolization and attempted monopolization claims, McKenzie's primary theory was that PeaceHealth engaged in anticompetitive conduct by offering insurers "bundled" or "package" discounts. McKenzie asserted that PeaceHealth offered insurers discounts of 35% to 40% on tertiary services if the insurers made PeaceHealth their sole preferred provider for *all* services—primary, secondary, and tertiary. McKenzie introduced evidence of a few specific instances of PeaceHealth's bundled discounting practices.

For example, in 2001, PeaceHealth was the only preferred provider of hospital care under the preferred provider plan ("PPP") of Regence BlueCross BlueShield of Oregon ("Regence").[2] At that time, Regence was paying PeaceHealth

[2]In a preferred provider plan, health care providers contract with an insurer to provide health care to the insurer's customers. The insurer's customers pay much higher prices if they obtain services from providers other than those with whom their insurer has contracted.

a 76% reimbursement rate for all of PeaceHealth's medical services, including primary, secondary, and tertiary services. Around that time, pursuant to McKenzie's request, Regence considered adding McKenzie to the PPP as a preferred provider of primary and secondary services. When Regence's contract with PeaceHealth came up for its annual renewal, Regence solicited two proposals from PeaceHealth. Under one proposal, PeaceHealth would remain the only preferred provider. Under the other proposal, McKenzie would be added as a preferred provider. PeaceHealth offered an 85% reimbursement rate for all services if it remained Regence's sole preferred provider of primary, secondary, and tertiary services, and a 90% reimbursement rate if McKenzie was added as a preferred provider of primary and secondary services. Regence thereafter declined to include McKenzie as a preferred provider.

That same year, McKenzie sought and received admission as a preferred provider of primary and secondary services under the preferred plan offered by Providence Health Plan ("Providence"). Until then, PeaceHealth was the only preferred provider of primary, secondary, and tertiary services in the Providence preferred plan. Upon McKenzie's admission as a preferred provider, PeaceHealth increased its reimbursement rate with Providence from 90% to 93%. The evidence showed that insurers who made PeaceHealth their exclusive preferred provider across all services, thus purchasing from PeaceHealth a full complement of primary, secondary, and tertiary services, paid lower reimbursement rates than insurers who purchased tertiary services from PeaceHealth, but at least some primary and secondary services from McKenzie.

The jury rejected McKenzie's claims of monopolization, conspiracy to monopolize, and exclusive dealing in its verdict for PeaceHealth on those issues. However, the jury found in favor of McKenzie on its claims of attempted monopolization, price discrimination, and tortious interference. The jury awarded damages of $5.4 million on each claim. McKenzie elected to pursue its remedy under federal law on the attempted monopolization claim, so the district court, pursuant to § 4(a) of the Clayton Act, 15 U.S.C. § 15(a), trebled the jury's $5.4 million award on the attempted monopolization claim for a final damage award of $16.2 million. The district court denied PeaceHealth's motion for judgment as a matter of law on the claims the jury decided in McKenzie's favor, and also awarded McKenzie $1,583,185.57 in attorneys' fees and costs.

PeaceHealth appeals the judgment entered pursuant to the jury verdict in McKenzie's favor. McKenzie cross-appeals the district court's grant of summary judgment to PeaceHealth on McKenzie's tying claim. Both parties appeal the district court's award of attorneys' fees and costs.

II

We first address PeaceHealth's appeal of the jury verdict in McKenzie's favor on McKenzie's claims of attempted monopolization, price discrimination, and tortious interference.

A

We address initially the attempted monopolization claim. Section 2 of the Sherman Act makes it illegal to "attempt to monopolize . . . any part of the trade or commerce among the several States, or with foreign nations." 15 U.S.C. § 2. "[T]o demonstrate attempted monopolization a plaintiff must prove (1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power." *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456 (1993); *Amarel v. Connell*, 102 F.3d 1494, 1521 (9th Cir. 1996).[3]

[3]The focus in attempted monopolization cases on a defendant's "specific intent" to monopolize and on the "dangerous probability" that

PeaceHealth's appeal centers on the first element of the *Spectrum Sports* test, the conduct element. Anticompetitive conduct is behavior that tends to impair the opportunities of rivals and either does not further competition on the merits or does so in an unnecessarily restrictive way. *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 605 n.32 (1985). PeaceHealth contends that we should vacate the jury's verdict because the district court incorrectly instructed the

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monopoly will result traces its roots to the Supreme Court's earliest pronouncements on the Sherman Act. Over one hundred years ago, Justice Holmes explained that the Sherman Act permits claims

> against combinations in restraint of commerce among the states and against attempts to monopolize the same. Intent is almost essential to such a combination, and is essential to such an attempt. Where acts are not sufficient in themselves to produce a result which the law seeks to prevent—for instance, the monopoly,—but require further acts in addition to the mere forces of nature to bring that result to pass, an intent to bring it to pass is necessary in order to produce a dangerous probability that it will happen. But when that intent and the consequent dangerous probability exist, this statute, like many others, and like the common law in some cases, directs itself against that dangerous probability as well as against the completed result.

Swift & Co. v. United States, 196 U.S. 375, 396 (1905) (citation omitted). By contrast, in monopolization cases, monopolistic intent can be inferred from the exclusionary conduct of a firm with monopoly power. *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 432 (2d Cir. 1945) (Hand, J.) (noting that, in a monopolization case, "no intent is relevant except that which is relevant to any liability, criminal or civil: i.e. an intent to bring about the forbidden act"); *United States v. United Shoe Mach. Corp.*, 110 F. Supp. 295, 346 (D. Mass. 1953) ("Defendant intended to engage in the leasing practices and pricing policies which maintained its market power. That is all the intent which the law requires when both the complaint and the judgment rest on a charge of 'monopolizing', not merely 'attempting to monopolize'. Defendant having willed the means, has willed the end."), *aff'd*, 347 U.S. 521 (1954). In attempted monopolization cases, though, the defendant firm "has not yet achieved a position of power in the market but is trying to build up such a position. Being without power to exploit or exclude, such a firm must be shown to have a specific intent to achieve these results." A.D. Neale & D.G. Goyder, *The Antitrust Laws of the United States of America* 93 (3d ed. 1980).

jury about when bundled discounting can amount to anticompetitive conduct. This leads us to consider at some length the phenomena of bundles and bundled discounts.

1

[1] Bundling is the practice of offering, for a single price, two or more goods or services that could be sold separately. A bundled discount occurs when a firm sells a bundle of goods or services for a lower price than the seller charges for the goods or services purchased individually. *See* Daniel A. Crane, *Mixed Bundling, Profit Sacrifice, and Consumer Welfare*, 55 Emory L.J. 423, 425 (2006); David S. Evans & Michael Salinger, *Why Do Firms Bundle and Tie?*, 22 Yale J. on Reg. 37, 41 (2005); Thomas A. Lambert, *Evaluating Bundled Discounts*, 89 Minn. L. Rev. 1688, 1693 (2005). As discussed above, PeaceHealth offered bundled discounts to Regence and other insurers in this case. Specifically, PeaceHealth offered insurers discounts if the insurers made PeaceHealth their exclusive preferred provider for primary, secondary, and tertiary care.

Bundled discounts are pervasive, and examples abound. Season tickets, fast food value meals, all-in-one home theater systems—all are bundled discounts. Like individual consumers, institutional purchasers seek and obtain bundled discounts, too. *See, e.g.*, *LePage's Inc. v. 3M*, 324 F.3d 141, 154 (3d Cir. 2003) (en banc) (involving rebates offered by 3M to retailers who purchased 3M's full line of health care, home care, home improvement, stationary, retail auto, and "Leisure Time" products); *Invacare Corp. v. Respironics, Inc.*, No. 1:04-CV-1580, 2006 WL 3022968, at *1 (N.D. Ohio Oct. 23, 2006) (involving a medical device manufacturer who bundled the masks worn by persons with obstructive sleep apena with the devices that blow air into the masks); *Masimo Corp. v. Tyco Health Care Group, L.P.*, No. CV 02-4770, 2006 WL 1236666, at *9 (C.D. Cal. Mar. 22, 2006) (involving rebates offered by Tyco to hospitals that purchased both Tyco's oximetry and non-oximetry products together); *J.B.D.L. Corp. v. Wyeth-Ayerst Labs., Inc.*, No. 1:01-CV-704, 2005 WL 1396940, at *3 (S.D. Ohio June 13, 2005) (involving rebates offered by Wyeth to pharmacy benefit managers based on combined purchases of estrogen-replacement drugs, oral contraceptives, an antidepressant, an antibiotic, a calcium channel blocker, and a beta blocker), *aff'd*, 485 F.3d 880 (6th Cir. 2007). The varied and pervasive nature of bundled discounts illustrates that such discounts transcend market boundaries. On the one hand, the world's largest corporations offer bundled discounts as their product lines expand with the convergence of industries.[4] On the other hand, a street-corner vendor with a food cart—a merchant with limited capital—might offer a discount to a customer who buys a drink and potato chips to complement a hot dog. The fact that such diverse sellers offer bundled discounts shows that such discounts are a fundamental option for both buyers and sellers.[5]

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[4]For example, in the telecommunications field, it is common for companies to offer not only phone service, but also Internet access and television service, and many of these companies offer bundled discounts to customers who purchase their entire package. *See* Ken Belson, *Dial M for Merger*, N.Y. Times, Jan. 28, 2005, at C1; Ken Belson, *Cable's Rivals Lure Customers with Packages*, N.Y. Times, Nov. 22, 2004, at C1.

[5]That bundled discounts are a common feature of our current economic system is relevant to our analysis of allegedly anticompetitive conduct under § 2 of the Sherman Act. The Supreme Court, in assessing the *stare decisis* effect of its prior precedents under § 1 of the Sherman Act, recently noted that "[f]rom the beginning the Court has treated the Sherman Act as a common-law statute," and that "[j]ust as the common law adapts to modern understanding and greater experience, so too does the Sherman Act's prohibition on 'restraint[s] of trade' evolve to meet the dynamics of present economic conditions." *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 127 S. Ct. 2705, 2720 (2007) (third alteration in original). The frequency with which we see bundled discounts in varied contexts does not insulate such discounts from antitrust review, but it heightens the need to ensure that the rule adopted does not expose inventive and legitimate forms of price competition to an overbroad liability standard.

Bundled discounts generally benefit buyers because the discounts allow the buyer to get more for less.[6] Lambert, *supra*, 89 Minn. L. Rev. at 1726 (suggesting that bundled discounts always provide some immediate consumer benefit in the form of lower prices); 3 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 749b at 324 (Supp. 2006) (explaining that "[t]he great majority of discounting practices are procompetitive" and "reflect hard bargaining"). Bundling can also result in savings to the seller because it usually costs a firm less to sell multiple products to one customer at the same time than it does to sell the products individually. *United States v. Microsoft Corp.*, 253 F.3d 34, 87 (D.C. Cir. 2001) (per curiam) (noting that "[b]undling obviously saves distribution and consumer transaction costs" and allows firms to "capitalize on certain economies of scope"); Crane, *supra*, 55 Emory L.J. at 430-33 (discussing how package discounts can create economies of scope and transaction costs savings).[7]

Not surprisingly, the Supreme Court has instructed that, because of the benefits that flow to consumers from discounted prices, price cutting is a practice the antitrust laws aim to promote. *See Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 594 (1986) ("[C]utting prices in order to increase business often is the very essence of compe-

[6]The Supreme Court has recognized the principle that package pricing is usually procompetitive, noting that "[b]uyers often find package sales attractive; a seller's decision to offer such packages can merely be an attempt to compete effectively—conduct that is entirely consistent with the Sherman Act." *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 12 (1984).

[7]The academic literature provides other examples of ways in which sellers benefit from bundling. *See, e.g.*, Crane, *supra*, 55 Emory L.J. at 430-43 (suggesting sellers can use bundles to instill customer loyalty, lower net prices to consumers by eliminating multiple monopoly-price markups on complementary goods, and price discrimination); *see also* Antitrust Modernization Comm'n, *Report and Recommendations* 95 (2007) (suggesting sellers can use bundled discounts to increase demand in lieu of advertising, encourage use of a new product, or enter a new market).

tition."). Consistent with that principle, we should not be too quick to condemn price-reducing bundled discounts as anti-competitive, lest we end up with a rule that discourages legitimate price competition. *See Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 234 (1st Cir. 1983) (Breyer, J.).

However, it is possible, at least in theory, for a firm to use a bundled discount to exclude an equally or more efficient competitor and thereby reduce consumer welfare in the long run. *See* Richard A. Posner, *Antitrust Law* 236 (2d ed. 2001); Barry Nalebuff, *Exclusionary Bundling*, 50 Antitrust Bull. 321, 321 (2005). For example, a competitor who sells only a single product in the bundle (and who produces that single product at a lower cost than the defendant) might not be able to match profitably the price created by the multi-product bundled discount. *See Ortho Diagnostic Sys., Inc. v. Abbott Labs., Inc.*, 920 F. Supp. 455, 467 (S.D.N.Y. 1996). This is true even if the post-discount prices for both the entire bundle and each product in the bundle are above the seller's cost. *See Ortho*, 920 F. Supp. at 467 (noting that "a firm that enjoys a monopoly on one or more of a group of complementary products, but which faces competition on others, can price all of its products above average variable cost and yet still drive an equally efficient competitor out of the market"). Judge Kaplan's opinion in *Ortho* provides an example of such a situation:

> Assume for the sake of simplicity that the case involved the sale of two hair products, shampoo and conditioner, the latter made only by A and the former by both A and B. Assume as well that both must be used to wash one's hair. Assume further that A's average variable cost for conditioner is $2.50, that its average variable cost for shampoo is $1.50, and that B's average variable cost for shampoo is $1.25. B therefore is the more efficient producer of shampoo. Finally, assume that A prices conditioner and shampoo at $5 and $3, respectively, if bought separately

> but at $3 and $2.25 if bought as part of a package. Absent the package pricing, A's price for both products is $8. B therefore must price its shampoo at or below $3 in order to compete effectively with A, given that the customer will be paying A $5 for conditioner irrespective of which shampoo supplier it chooses. With the package pricing, the customer can purchase both products from A for $5.25, a price above the sum of A's average variable cost for both products. In order for B to compete, however, it must persuade the customer to buy B's shampoo while purchasing its conditioner from A for $5. In order to do that, B cannot charge more than $0.25 for shampoo, as the customer otherwise will find A's package cheaper than buying conditioner from A and shampoo from B. On these assumptions, A would force B out of the shampoo market, notwithstanding that B is the more efficient producer of shampoo, without pricing either of A's products below average variable cost.

Id.; *see also* 3 Areeda & Hovenkamp, *supra*, ¶ 749a at 318-19 (Supp. 2006) (providing a similar example). It is worth reiterating that, as the example above shows, a bundled discounter can exclude rivals who do not sell as great a number of product lines without pricing its products below its cost to produce them. Thus, a bundled discounter can achieve exclusion without sacrificing any short-run profits. *See* Nalebuff, *supra*, 50 Antitrust Bull. at 339 (providing an example of exclusion accomplished with an *increase* in profits).

[2] In this case, McKenzie asserts it could provide primary and secondary services at a lower cost than PeaceHealth. Thus, the principal anticompetitive danger of the bundled discounts offered by PeaceHealth is that the discounts could freeze McKenzie out of the market for primary and secondary services because McKenzie, like seller B in Judge Kaplan's example, does not provide the same array of services as

PeaceHealth and therefore could possibly not be able to match the discount PeaceHealth offers insurers.

[3] From our discussion above, it is evident that bundled discounts, while potentially procompetitive by offering bargains to consumers, can also pose the threat of anticompetitive impact by excluding less diversified but more efficient producers. These considerations put into focus this problem: How are we to discern where antitrust law draws the line between bundled discounts that are procompetitive and part of the normal rough-and-tumble of our competitive economy and bundled discounts, offered by firms holding or on the verge of gaining monopoly power in the relevant market, that harm competition and are thus proscribed by § 2 of the Sherman Act?

2

In this case, the district court based its jury instruction regarding the anticompetitive effect of bundled discounting on the Third Circuit's en banc decision in *LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003) (en banc). In that case, the plaintiff, LePage's, was the market leader in sales of "private label" (i.e., store brand) transparent tape. *See id.* at 144. As LePage's market share fell and its profitability declined, it brought suit asserting that 3M, who manufactured Scotch tape, some private label tape, and many other products that LePage's did not produce (like healthcare products and retail automotive products), leveraged its monopoly over Scotch brand tape to monopolize the private label tape market. *Id.* at 145, 154. Specifically, LePage's alleged that 3M's multi-tiered bundled rebate structure was anticompetitive. *Id.* at 145. The bundled rebate structure offered progressively higher rebates when customers increased purchases across 3M's different product lines—discounts LePage's could not offer because it did not sell the same diverse array of products as 3M. *See id.* A jury found that 3M's conduct violated § 2 of the Sherman Act and 3M appealed. *Id.*

The primary issue before the Third Circuit was whether 3M unlawfully maintained its monopoly power through the bundled discount program. *See id.* at 146-47. 3M argued that its bundled rebate structure was legal as a matter of law because it never priced below cost. *Id.* at 147. 3M relied heavily on the United States Supreme Court's decision in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993). In *Brooke Group*, a primary-line price discrimination case brought under the Robinson-Patman Act, the Supreme Court held that, in a single product predatory pricing case, a plaintiff must prove (1) that its rival's low prices were below an appropriate measure of its rival's costs and (2) that its rival "had a reasonable prospect, or, under § 2 of the Sherman Act, a dangerous probability, of recouping its investment in below-cost prices." *Id.* at 222, 224. In *LePage's*, the Third Circuit, in a 7-3 en banc decision, refused to apply *Brooke Group*'s below-cost pricing requirement to bundled discounting.

The Third Circuit first distinguished *Brooke Group* by noting that the defendant in that case was an oligopolist while 3M was a monopolist. *LePage's*, 324 F.3d at 151-52. The court reasoned that while *Brooke Group*'s requirement of below-cost pricing with a probability of recoupment is appropriate when the defendant is an oligopolist who still faces competition when it tries to recoup the losses it suffered during the predation period, below-cost pricing and a probability of recoupment should not be required when the defendant is a monopolist whose behavior will be unconstrained by the market after it eliminates its lone rival. *See id.* The court in *LePage's* also noted that the plaintiff in *Brooke Group* simply challenged the defendant's pricing practices, not bundling accomplished through discounting. *See id.* at 151. The court reasoned that *Brooke Group* did not require below-cost pricing for *any* pricing practice to be deemed exclusionary. *See id.*

The court noted that "[t]he principal anticompetitive effect of bundled rebates as offered by 3M is that when offered by a monopolist they may foreclose portions of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer." *Id.* at 155. The Third Circuit concluded that the jury could reasonably have found that 3M used its monopoly in transparent tape along with its extensive catalog of other products to exclude LePage's from the market and that 3M did not present any adequate business justification for its bundled discounting program. *Id.* at 164, 169. The court thus affirmed the jury verdict in LePage's favor, *id.* at 169, even though LePage's economist testified that LePage's was not as efficient a tape producer as 3M, *see id.* at 177 (Greenburg, J., dissenting).[8]

In this case, the district court used *LePage's* to formulate its jury instruction. Specifically, the district court instructed the jury that

> plaintiff . . . contends that defendant has bundled price discounts for its primary, secondary, and tertiary acute care products and that doing so is anti-competitive. Bundled pricing occurs when price discounts are offered for purchasing an entire line of services exclusively from one supplier. Bundled price discounts may be anti-competitive if they are offered by a monopolist and substantially foreclose portions of the market to a competitor who does not provide an equally diverse group of services and who therefore cannot make a comparable offer.

As 3M did in *LePage's*, PeaceHealth argues that the jury instruction incorrectly stated the law because it allowed the jury to find that a defendant with monopoly power (or, in the case of an attempted monopolization claim, a dangerous prob-

[8]Judge Scirica and then-Judge Alito joined Judge Greenburg's dissent from the majority opinion. The Third Circuit reaffirmed the rule of *LePage's* in *United States v. Dentsply Int'l, Inc.*, 399 F.3d 181, 187 (3d Cir. 2005).

ability of achieving monopoly power) engaged in exclusionary conduct by simply offering a bundled discount that its competitor could not match. The instruction did not require the jury to consider whether the defendant priced below cost. *LePage's*, PeaceHealth asserts, was wrongly decided because it allows the jury to conclude, from the structure of the market alone, that a competitor has been anticompetitively excluded from the market.[9] We generally review jury instructions for abuse of discretion, but we review de novo whether jury instructions correctly stated the law. *Voohries-Larson v. Cessna Aircraft Co.*, 241 F.3d 707, 713 (9th Cir. 2001).

[4] As the bipartisan Antitrust Modernization Commission ("AMC")[10] recently noted, the fundamental problem with the *LePage's* standard is that it does not consider whether the bundled discounts constitute competition on the merits, but simply concludes that all bundled discounts offered by a

[9]After oral argument, we issued an order inviting amicus briefing on the issue of whether a plaintiff seeking to establish the anticompetitive conduct element of an attempted monopolization claim by showing that the defendant offered bundled discounts must prove that the defendant's prices were below the defendant's costs. *Cascade Health Solutions v. PeaceHealth*, 479 F.3d 726, 727 (9th Cir. 2007). We also sought input on the appropriate measure of costs if a plaintiff must prove below-cost pricing. *Id.* Finally, we asked amici who were arguing that a plaintiff should not be required to prove below-cost pricing to suggest alternative standards for the trier of fact to use in determining whether bundled discounts are anticompetitive. *Id.* We thank the many amici who accepted our invitation for their thoughtful briefs.

[10]Congress created the AMC in the Antitrust Modernization Commission Act of 2002, Pub. L. No. 107-273, §§ 11051-60, 116 Stat. 1758, 1856-59. The Act entrusted the AMC with four tasks: (1) soliciting the views of all parties concerned with the federal antitrust laws; (2) examining whether the antitrust laws needed modernization; (3) evaluating proposals to modernize the antitrust laws; and (4) submitting a report to the President and Congress containing a statement of the AMC's findings and conclusions and recommending any legislative or administrative action the AMC considered appropriate. *See id.* §§ 11053, 11058. The procedure for appointing the twelve commissioners ensured that both major political parties were equally represented on the AMC. *See id.* § 11054.

monopolist are anticompetitive with respect to its competitors who do not manufacture an equally diverse product line. Antitrust Modernization Comm'n, *Report and Recommendations* 97 (2007) [hereinafter AMC Report]. The *LePage's* standard, the AMC noted, asks the jury to consider whether the plaintiff has been excluded from the market, but does not require the jury to consider whether the plaintiff was at least as efficient of a producer as the defendant. *Id.*; *see also LePage's*, 324 F.3d at 175 (Greenberg, J., dissenting) (noting that "LePage's did not even attempt to show that it could not compete by calculating the discount that it would have had to provide in order to match the discounts offered by 3M through its bundled rebates"). Thus, the *LePage's* standard could protect a less efficient competitor at the expense of consumer welfare. As Judge Greenberg explained in his *LePage's* dissent, the Third Circuit's standard "risks curtailing price competition and a method of pricing beneficial to customers because the bundled rebates effectively lowered [the seller's] costs." *LePage's*, 324 F.3d at 179 (Greenberg, J., dissenting).

The AMC also lamented that *LePage's* "offers no clear standards by which firms can assess whether their bundled rebates are likely to pass antitrust muster." AMC Report, *supra*, at 94. The Commission noted that efficiencies, and not schemes to acquire or maintain monopoly power, likely explain the use of bundled discounts because many firms without market power offer them. *Id.* at 95. The AMC thus proposed a three-part test that it believed would protect procompetitive bundled discounts from antitrust scrutiny. The AMC proposed that:

> Courts should adopt a three-part test to determine whether bundled discounts or rebates violate Section 2 of the Sherman Act. To prove a violation of Section 2, a plaintiff should be required to show each one of the following elements (as well as other elements of a Section 2 claim): (1) after allocating all discounts and rebates attributable to the entire bun-

> dle of products to the competitive product, the defendant sold the competitive product below its incremental cost for the competitive product; (2) the defendant is likely to recoup these short-term losses; and (3) the bundled discount or rebate program has had or is likely to have an adverse effect on competition.

Id. at 99. The AMC reasoned that the first element would (1) subject bundled discounts to antitrust scrutiny only if they could exclude a hypothetical equally efficient competitor and (2) provide sufficient clarity for businesses to determine whether their bundled discounting practices run afoul of § 2. *Id.* at 100. The AMC concluded that the three-part test would, as a whole, bring the law on bundled discounting in line with the Supreme Court's reasoning in *Brooke Group*. *Id.*

3

We must decide whether we should follow *LePage's* or whether we should part ways with the Third Circuit by adopting a cost-based standard to apply in bundled discounting cases.

Observers have commented that, in some respects, bundled discounts are similar to both predatory pricing and tying. *See* Nalebuff, *supra*, 50 Antitrust Bull. at 365; Daniel L. Rubinfeld, *3M's Bundled Rebates: An Economic Perspective*, 72 U. Chi. L. Rev. 243, 252-56 (2005). As the Supreme Court explained in *Brooke Group*, a plaintiff in a single product predatory pricing case must establish that the defendant priced below cost and that there was a probability the defendant could recoup the losses it suffered during the predation period. *See Brooke Group*, 509 U.S. at 222. In a normal tying case, however, while a plaintiff must prove that it was "coerced" into buying the tied products from the defendant, a plaintiff does not need to prove that the defendant priced the products below cost, and therefore the plaintiff also does not need to prove any recoupment of losses. *See Datagate, Inc. v. Hewlett-Packard Co.*, 60 F.3d 1421, 1423-24 (9th Cir. 1995).

However, "[o]ne difference between traditional tying by contract and tying via package discounts is that the traditional tying contract typically forces the buyer to accept both products, as well as the cost savings." 3 Areeda & Hovenkamp, *supra*, ¶ 749b2 at 332 (Supp. 2006). Conversely, "the package discount gives the buyer the choice of accepting the cost savings by purchasing the package, or foregoing the savings by purchasing the products separately." *Id.* The package discount thus does not constrain the buyer's choice as much as the traditional tie. For that reason, the late-Professor Areeda and Professor Hovenkamp suggest that "[a] variation of the requirement that prices be 'below cost' is essential for the plaintiff to establish one particular element of unlawful bundled discounting—namely, that there was actually 'tying'—that is, that the purchaser was actually 'coerced' (in this case, by lower prices) into taking the tied-up package." *Id.* at 331.

In addition, the Supreme Court has forcefully suggested that we should not condemn prices that are above some measure of incremental cost. *See id.* ¶ 737a at 393 (2d ed. 2002) (quoting *Brooke Group*, 509 U.S. at 223). In *Brooke Group*, the Court held that "a plaintiff seeking to establish competitive injury resulting from a rival's low prices must prove that the prices complained of are below an appropriate measure of its rival's costs." *Brooke Group*, 509 U.S. at 222. In the course of rejecting the plaintiff's argument that a predatory pricing plaintiff need not prove below-cost pricing, the Court wrote that it has "rejected . . . the notion that above-cost prices that are below general market levels or the costs of a firm's competitors inflict injury to competition cognizable under the antitrust laws." *Id.* at 223 (citing *Atl. Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 340 (1990)). The Court went on to emphasize that "[l]ow prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition." *Id.*

(internal quotation omitted). The Court also noted the broad application of the principle that only below-cost prices are anticompetitive, stating that "[w]e have adhered to this principle regardless of the type of antitrust claim involved." *Id.* (internal quotation omitted). "As a general rule," the Court concluded, "the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting." *Id.*; *accord Matsushita*, 475 U.S. at 594.

The Court recently reemphasized these principles in *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 1078 (2007), a case in which the Court held that *Brooke Group*'s below-cost pricing requirement applies in cases in which the plaintiff alleges that the defendant engaged in predatory bidding—the practice of bidding up input costs to drive rivals out of business. Specifically, the Court held that a predatory bidding "plaintiff must prove that the alleged predatory bidding led to below-cost pricing of the predator's outputs. That is, the predator's bidding on the [input] side must have caused the cost of the relevant output to rise above the revenues generated in the sale of those outputs." *Weyerhaeuser*, 127 S. Ct. at 1078.

Of course, in neither *Brooke Group* nor *Weyerhaeuser* did the Court go so far as to hold that in every case in which a plaintiff challenges low prices as exclusionary conduct the plaintiff must prove that those prices were below cost. But the Court's opinions strongly suggest that, in the normal case, above-cost pricing will not be considered exclusionary conduct for antitrust purposes, and the Court's reasoning poses a strong caution against condemning bundled discounts that result in prices above a relevant measure of costs.

The Supreme Court's long and consistent adherence to the principle that the antitrust laws protect the process of competition, and not the pursuits of any particular competitor, reinforce our conclusion of caution concerning bundled discounts that result in prices above an appropriate measure of costs. The Court voiced this principle most notably in *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477 (1977). In that case, the plaintiffs challenged, under § 7 of the Clayton Act,[11] Brunswick's acquisition of unprofitable bowling centers. *Id.* at 479-80. The plaintiffs, like McKenzie, sought treble damages under § 4 of the Clayton Act. The Court considered the "narrow" issue of "whether antitrust damages are available where the sole injury alleged is that competitors were continued in business, thereby denying [the plaintiffs] an anticipated increase in market shares." *Id.* at 484. The Court observed that the damages the plaintiffs sought were "designed to provide them with the profits they would have realized had competition been reduced." *Id.* at 488. Noting that "[t]he antitrust laws, however, were enacted for 'the protection of competition not competitors,' " the Court reasoned that "[i]t is inimical to the purposes of these laws to award damages for the type of injury claimed here." *Id.* (quoting *Brown Shoe Co. v. United States*, 370 U.S., 294, 320 (1962)). The Court concluded:

> We therefore hold that for plaintiffs to recover treble damages on account of § 7 violations, they must prove more than injury causally linked to an illegal presence in the market. Plaintiffs must prove *antitrust* injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation.

[11]Section 7 of the Clayton Act forbids acquisitions that "substantially . . . lessen competition[ ] or tend to create a monopoly." 15 U.S.C. § 18.

Id. at 489.

Subsequent to *Brunswick*, the Court has often reinforced the principle that the antitrust laws' prohibitions focus on protecting the competitive process and not on the success or failure of individual competitors. *See, e.g.*, *Volvo Trucks N. Am., Inc. v. Reeder-Simco GMC, Inc.*, 546 U.S. 164, ___ 126 S. Ct. 860, 872 (2006) ("Interbrand competition, our opinions affirm, is the primary concern of antitrust law." (internal quotation omitted)); *Spectrum Sports*, 506 U.S. at 458 ("The purpose of the [Sherman] Act is not to protect businesses from the working of the market; it is to protect the public from the failure of the market. The law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself."); *Atl. Richfield*, 495 U.S. at 331 (holding that a firm does not incur an antitrust injury when it loses sales to a competitor charging nonpredatory prices pursuant to a vertical, maximum-price-fixing scheme); *Cargill, Inc. v. Monfort of Colo., Inc.*, 479 U.S. 104, 113 (1986) (extending antitrust injury requirement to suits for injunctive relief under § 16 of the Clayton Act, 15 U.S.C. § 26); *J. Truett Payne Co. v. Chrysler Motors Corp.*, 451 U.S. 557, 562 (1981) (extending antitrust injury requirement to price discrimination suits arising under § 2 of the Clayton Act). The Court's reasoning and conclusions in *Brooke Group*, as reaffirmed recently in *Weyerhauser*, accordingly show a measured concern to leave unhampered pricing practices that might benefit consumers, absent the clearest showing that an injury to the competitive process will result. *Microsoft*, 253 F.3d at 58; *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039, 1060-61 (8th Cir. 2000).

One of the challenges of interpreting and enforcing the amorphous prohibitions of §§ 1 and 2 of the Sherman Act is ensuring that the antitrust laws do not punish economic behavior that benefits consumers and will not cause long-run injury to the competitive process. A bundled discount, however else it might be viewed, is a price discount on a collection of goods. The Supreme Court has undoubtedly shown a solicitude for price competition. In *Weyerhaeuser*, Justice Thomas, writing for the Court, reminded us that, in *Brooke Group*, the Court had cautioned that "the costs of erroneous findings of predatory-pricing liability were quite high because [t]he mechanism by which a firm engages in predatory pricing —lowering prices—is the same mechanism by which a firm stimulates competition, and therefore, mistaken findings of liability would chill the very conduct the antitrust laws are designed to protect." *Weyerhaeuser*, 127 S. Ct. at 1075 (internal quotations omitted, alteration in original).

[5] Given the endemic nature of bundled discounts in many spheres of normal economic activity, we decline to endorse the Third Circuit's definition of when bundled discounts constitute the exclusionary conduct proscribed by § 2 of the Sherman Act. Instead, we think the course safer for consumers and our competitive economy to hold that bundled discounts may not be considered exclusionary conduct within the meaning of § 2 of the Sherman Act unless the discounts resemble the behavior that the Supreme Court in *Brooke Group* identified as predatory.[12] Accordingly, we hold that the exclusionary

[12]McKenzie contends that *Brooke Group* is not persuasive in this case because *Brooke Group* dealt with liability for primary-line price discrimination in violation of § 2(a) of the Robinson-Patman Act, whereas this case arises under § 2 of the Sherman Act. However, the Court made clear in *Brooke Group* that, whether a predatory pricing claim arises under § 2(a) of the Robinson-Patman Act or § 2 of the Sherman Act, the concerns are essentially the same, noting that:

> There are, to be sure, differences between the two statutes. For example, we interpret § 2 of the Sherman Act to condemn predatory pricing when it poses "a dangerous probability of actual monopolization," whereas the Robinson-Patman Act requires only that there be "a reasonable possibility" of substantial injury to competition before its protections are triggered. But whatever additional flexibility the Robinson-Patman Act standard may imply, the essence of the claim under either statute is the same: A business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market.

Brooke Group, 509 U.S. at 222 (citations omitted).

conduct element of a claim arising under § 2 of the Sherman Act cannot be satisfied by reference to bundled discounts unless the discounts result in prices that are below an appropriate measure of the defendant's costs.[13]

4

The next question we must address is how we define the appropriate measure of the defendant's costs in bundled discounting cases and how we determine whether discounted prices fall below that mark. Defining the appropriate measure of costs in a bundled discounting case is more complex than in a single product case. In a single product case, we may simply ask whether the defendant has priced its product below its incremental cost of producing that product because a rival that produces the same product as efficiently as the defendant should be able to match any price at or above the defendant's cost. However, as we discussed above, a defendant offering a bundled discount, without pricing below cost either the individual products in the bundle or the bundle as a whole, can, in some cases, exclude a rival who produces one of the products in the bundle equally or more efficiently than the defendant. Thus, simply asking whether the defendant's prices are below its incremental costs might fail to alert us to bundled discounts that threaten the exclusion of equally efficient rivals. Nonetheless, we are mindful that, in single product pricing cases, the Supreme Court has not adopted rules condemning prices above a seller's incremental costs. With these considerations in mind, we assess the rules the parties and amici propose for us to use in bundled discounting cases to determine the appropriate measure of a defendant's costs and whether a defendant has priced below that level.

[13]Of course, even if the exclusionary conduct element is satisfied by bundled discounts at price levels that yield a conclusion of below-cost sales, under the appropriate measure, there cannot be Sherman Act § 2 liability for attempted monopolization unless the other elements of a specific intent to monopolize and dangerous probability of success are satisfied.

PeaceHealth and some amici urge us to adopt a rule they term the "aggregate discount" rule. This rule condemns bundled discounts as anticompetitive only in the narrow cases in which the discounted price of the entire bundle does not exceed the bundling firm's incremental cost to produce the entire bundle. PeaceHealth and amici argue that support for such a rule can be found in the Supreme Court's single product predation cases—*Brooke Group* and *Weyerhaeuser*.

We are not persuaded that those cases require us to adopt an aggregate discount rule in multi-product discounting cases. As we discussed above, bundled discounts present one potential threat to consumer welfare that single product discounts do not: A competitor who produces fewer products than the defendant but produces the competitive product at or below the defendant's cost to produce that product may nevertheless be excluded from the market because the competitor cannot match the discount the defendant offers over its numerous product lines. This possibility exists even when the defendant's prices are above cost for each individual product and for the bundle as a whole. *See Ortho*, 920 F. Supp. at 467; Nalebuff, *supra*, 50 Antitrust Bull. at 359 ("Whether or not a collection of goods is sold at a profit does not reveal whether one-good rivals were foreclosed."). Under a discount aggregation rule, anticompetitive bundled discounting schemes that harm competition may too easily escape liability.

[6] Additionally, as commentators have pointed out, *Brooke Group*'s safe harbor for above-cost discounting in the single product discount context is not based on a theory that above-cost pricing strategies can never be anticompetitive, but rather on a cost-benefit rejection of a more nuanced rule. 3 Areeda & Hovenkamp, *supra*, ¶ 749b at 324 (Supp. 2006); Lambert, *supra*, 89 Minn. L. Rev. at 1704; *see also Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 414 (2004) (explaining that while above-cost predatory pricing schemes may exist, they are " 'beyond the practical ability of a judicial tribunal to control' " (quoting *Brooke*

Group, 509 U.S. at 223)). That is, the safe harbor rests on the premise that "any consumer benefit created by a rule that permits inquiry into above-cost, single-product discounts, but allows judicial condemnation of those deemed legitimately exclusionary, would likely be outweighed by the consumer harm occasioned by overdeterring nonexclusionary discounts." Lambert, *supra*, 89 Minn. L. Rev. at 1705; *see Weyerhaeuser*, 127 S. Ct. at 1075 (noting the high costs of erroneous findings of predatory-pricing liability because "[t]he mechanism by which a firm engages in predatory pricing—lowering prices—is the same mechanism by which a firm stimulates competition" (alteration in original, internal quotations omitted)); 3 Areeda & Hovenkamp, *supra*, ¶ 749b at 324 (Supp. 2006) (noting that "our measurement tools are too imprecise to evaluate [above-cost discounting] strategies without creating an intolerable risk of chilling competitive behavior"). So, in adopting an appropriate cost-based test for bundled discounting cases, we should not adopt an aggregate discount rule without inquiring whether a rule exists that is more likely to identify anticompetitive bundled discounting practices while at the same time resulting in little harm to competition.

The first potential alternative cost-based standard we consider derives from the district court's opinion in *Ortho*. This standard deems a bundled discount exclusionary if the plaintiff can show that it was an equally efficient producer of the competitive product, but the defendant's bundled discount made it impossible for the plaintiff to continue to produce profitably the competitive product. As the district court in *Ortho* phrased the standard: a plaintiff basing a § 2 claim on an anticompetitive bundled discount "must allege and prove either that (a) the monopolist has priced below its average variable cost or (b) the plaintiff is at least as efficient a producer of the competitive product as the defendant, but that the defendant's pricing makes it unprofitable for the plaintiff to continue to produce." *Ortho*, 920 F. Supp. at 469. Under this standard, above-cost prices are not per se legal. *Cf. Brooke*

Group, 509 U.S. at 222. Instead, this standard treats below-cost prices as simply one beacon for identifying discounts that create the risk of excluding firms that are as efficient as the defendant—the unique anticompetitive risk posed by bundled discounts. *See Ortho*, 920 F. Supp. at 466-67. Under *Ortho*'s standard, an above-cost discount can still be anticompetitive if a plaintiff proves it is as efficient a producer as the defendant, but is excluded because the defendant sells in more product markets than the plaintiff and can "spread the total discount over all those product lines and . . . force competitors to provide the entire dollar amount of the discount on a smaller collection of products." Lambert, *supra*, 89 Minn. L. Rev. at 1728. As compared to the discount aggregation rule, *Ortho*'s approach does a better job of identifying bundled discounts that threaten harm to competition.

However, one downside of *Ortho*'s standard is that it does not provide adequate guidance to sellers who wish to offer procompetitive bundled discounts because the standard looks to the costs of the actual plaintiff. A potential defendant who is considering offering a bundled discount will likely not have access to information about its competitors' costs, thus making it hard for that potential discounter, under the *Ortho* standard, to determine whether the discount it wishes to offer complies with the antitrust laws. Also, the *Ortho* standard, which asks whether the actual plaintiff is as efficient a producer as the defendant, could require multiple suits to determine the legality of a single bundled discount. While it might turn out that the plaintiff in one particular case is not as efficient a producer of the competitive product as the defendant, another rival might be. This second rival would have to bring another suit under the *Ortho* approach. We decline to adopt a rule that might encourage more antitrust litigation than is reasonably necessary to ferret out anticompetitive practices. *See Bell Atl. Corp. v. Twombly*, 127 S. Ct. 1955, 1966-67 (2007); *see also* Manual for Complex Litigation (Fourth) § 30 (2004) ("Antitrust litigation can . . . involve voluminous documentary and testimonial evidence, extensive discovery, complicated legal, factual, and technical (particularly economic) questions, numerous parties and attorneys, and substantial sums of money . . . . Antitrust trials usually are long, and there often are controversies over settlements and attorney fees."). Accordingly, we do not adopt *Ortho*'s approach, which we believe would be unduly cumbersome for sellers to assess and thus might chill procompetitive bundled discounting.

[7] Instead, as our cost-based rule, we adopt what amici refer to as a "discount attribution" standard.[14] Under this standard, the full amount of the discounts given by the defendant on the bundle are allocated to the competitive product or products. If the resulting price of the competitive product or products is below the defendant's incremental cost to produce them, the trier of fact may find that the bundled discount is exclusionary for the purpose of § 2. This standard makes the defendant's bundled discounts legal unless the discounts have the potential to exclude a *hypothetical* equally efficient producer of the competitive product.[15] *Cf. Ortho*, 920 F. Supp. at

[14]In the academic literature, this standard is sometimes referred to as a "discount allocation" or "discount reallocation" standard. *See e.g.*, Daniel A. Crane, *Multiproduct Discounting: A Myth of Nonprice Predation*, 72 U. Chi. L. Rev. 27, 28 (2005).

[15]A variation of the example from *Ortho* illustrates how the discount attribution standard condemns discounts that could not be matched by an equally or more efficient producer of the competitive product. Recall that the example involves A, a firm that makes both shampoo and conditioner. A's incremental cost of shampoo is $1.50 and A's incremental cost of conditioner is $2.50. A prices shampoo at $3 and conditioner at $5, if purchased separately. However, if purchased as a bundle, A prices shampoo at $2.25 and conditioner at $3. Purchased separately from A, the total price of one unit of shampoo and one unit of conditioner is $8. However, with the bundled discount, a customer can purchase both products from A for $5.25, a discount of $2.75 off the separate prices, but at a price that is still above A's variable cost of producing the bundle. Applying the discount attribution rule to the example, we subtract the entire discount on the package of products, $2.75, from the separate per unit price of the competitive product, shampoo, $3. The resulting effective price of shampoo is thus $0.25, meaning that, if a customer must purchase conditioner

469 (deeming bundled discounts anticompetitive if the *actual plaintiff* is excluded but equally efficient).

In their leading treatise on antitrust law, Professors Areeda and Hovenkamp support an approach that focuses on whether a bundled discount excludes a hypothetical equally efficient rival. Rejecting *Ortho*'s "actual plaintiff" standard, they explain:

> [W]e would not require a showing that the actual plaintiff be equally efficient. The relevant question is not necessarily whether a particular plaintiff was equally efficient, but whether the challenged bundling practices would have excluded an equally efficient rival, without reasonable justification. This rule is preferable on grounds of both administrability and principle. On the first, proving whether a hypothetical equally efficient rival is excluded by a multiproduct discount is typically quite manageable. By contrast, proof that the plaintiff is equally efficient can be quite difficult, particularly in cases where the defendant produces a larger product line than the plaintiff and there are joint costs.
>
> A requirement that the bundling practice be sufficiently severe so as to exclude an equally efficient

from A at the separate price of $5, a rival who produces only shampoo must sell the shampoo for $0.25 to make customers indifferent between A's bundle and the separate purchase of conditioner from A and shampoo from the hypothetical rival. A's pricing scheme thus has the effect of excluding any potential rival who would produce only shampoo, and would produce it at an incremental cost above $0.25. However, as we noted above, A's incremental cost of producing shampoo is $1.50. Thus, A's pricing practices exclude potential competitors that could produce shampoo more efficiently than A (i.e., at an incremental cost of less than $1.50). A's discount could thus be considered exclusionary under our rule, supporting Sherman Act § 2 liability if the other elements were proved.

> single-product rival, and without an adequate business justification, seems to strike about the right balance between permitting aggressive pricing while prohibiting conduct that can only be characterized as anticompetitive. Requiring the defendant's pricing policies to protect the trade of higher cost rivals is overly solicitous of small firms and denies customers the benefits of the defendant's lower costs. Further, if the practice will exclude an equally efficient rival, then it will exclude whether or not the rival is equally efficient in fact.

3 Areeda & Hovenkamp, *supra*, ¶ 749a at 322-23 (Supp. 2006) (footnotes omitted); *accord* Nalebuff, *supra*, 50 Antitrust Bull. at 328-29. Judge Posner's work on antitrust law also supports an approach that asks whether a bundled discount excludes a hypothetical equally efficient rival, stating that the acts of a monopolist should be deemed exclusionary if "the challenged practice is likely in the circumstances to exclude from the defendant's market an equally or more efficient competitor." Posner, *supra*, at 194-95.

Areeda and Hovenkamp also support using a discount attribution approach to determine if a bundled discount is exclusionary. They state:

> To see whether a package price is "exclusionary" . . . one simply attributes the entire discount on all products in the package to the product for which exclusion is claimed. If the resulting price is less than the defendant's cost, then the package discount is exclusionary as against a rival who makes only one of the two goods in the package.

3 Areeda & Hovenkamp, *supra*, ¶ 749b2 at 335-36 (Supp. 2006) (footnotes omitted); *accord* Nalebuff, *supra*, 50 Antitrust Bull. at 328. The discount attribution standard has also been used by two of the district courts in the small number of

published opinions dealing with allegedly exclusionary bundled discounts. *See Info. Res., Inc. v. Dun & Bradstreet Corp.*, 359 F. Supp. 2d 307, 307 (S.D.N.Y. 2004) ("When price discounts in one market are bundled with the price charged in a second market, the discounts must be applied to the price in the second market in determining whether that price is below that product's average variable cost."); *Virgin Atl. Airways Ltd. v. British Airways PLC*, 69 F. Supp. 2d 571, 580 n.8 (S.D.N.Y. 1999) (holding that a bundled discount is exclusionary "if the competitive product in the bundle [was] sold for a price below average variable cost after the discounts on the monopoly items in the bundle were subtracted from the price of that competitive product"), *aff'd*, 257 F.3d 256 (2d Cir. 2001). The discount attribution standard is also the standard endorsed by the AMC. AMC Report, *supra*, at 99 (requiring plaintiff to prove that "after allocating all discounts and rebates attributable to the entire bundle of products to the competitive product, the defendant sold the competitive product below its incremental cost for the competitive product").

The discount attribution standard provides clear guidance for sellers that engage in bundled discounting practices. A seller can easily ascertain its own prices and costs of production and calculate whether its discounting practices run afoul of the rule we have outlined. *See* Nalebuff, *supra*, 50 Antitrust Bull. at 330. Unlike under the *Ortho* standard, under the discount attribution standard a bundled discounter need not fret over and predict or determine its rivals' cost structure.[16]

[16]Professor Nalebuff identifies the practical problem of calculating a rival firm's costs as a compelling argument in favor of a standard that focuses on whether bundled discounts would exclude a hypothetical equally efficient competitor:

> There is . . . a practical problem in determining if a rival firm is equally efficient or not. The problem is compounded for the monopolist who is looking for a bright line test to know whether its bundled pricing might be exclusionary or not. The solution to both these problems is to pick the monopolist itself as the equally efficient rival.

Nalebuff, *supra*, 50 Antitrust Bull. at 330.

We are aware that liability under the discount attribution standard has the potential to sweep more broadly than under the aggregate discount rule or the *Ortho* standard. However, there is limited judicial experience with bundled discounts, and academic inquiry into the competitive effects of bundled discounts is only beginning.[17] By comparison, the Supreme Court's decision in *Brooke Group* (prefaced by the Court's discussion of predatory pricing in *Matsushita*, 475 U.S. at 588-91) marked the culmination of nearly twenty years of scholarly and judicial analysis of the feasibility and competitive effects of single product predatory pricing schemes.[18] *Cf.* 3 Areeda & Hovenkamp, *supra*, ¶ 749b at 323 (Supp. 2006) ("[T]he theory of anticompetitive discounting is in much the same position as the theory of predatory pricing was in the 1970s: no shortage of theories, but a frightening inability of courts to assess them."). The cost-based standard we adopt will allow courts the experience they need to divine the prevalence and competitive effects of bundled discounts and will

[17]Although the volume of case law dealing with bundled discounting is small, one thirty-year-old case shows that antitrust claims based on bundled discounting practices are nothing new under the sun. *See SmithKline Corp. v. Eli Lilly & Co.*, 427 F. Supp. 1089, 1124 (E.D. Pa. 1976), *aff'd*, 575 F.2d 1056 (3d Cir. 1978).

[18]A 1975 article by Professors Areeda and Turner ignited the modern debate about predatory pricing, *see* Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 Harv. L. Rev. 697 (1975), and many prominent antitrust scholars weighed in on the topic in the following decade-and-a-half. *See, e.g.*, Robert H. Bork, *The Antitrust Paradox* 154-55 (1978); George A. Hay, *Predatory Pricing*, 58 Antitrust L.J. 913 (1989); Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. Chi. L. Rev. 263 (1981); Paul L. Joskow & Alvin K. Klevorick, *A Framework for Analyzing Predatory Pricing Policy*, 89 Yale L.J. 213 (1979); William J. Baumol, *Quasi-Permanence of Price Reductions: A Policy for Prevention of Predatory Pricing*, 89 Yale L.J. 1 (1979); Oliver E. Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 Yale L.J. 284 (1977); *see also* Wesley J. Leibeler, *Whither Predatory Pricing? From Areeda and Turner to Matsushita*, 61 Notre Dame L. Rev. 1052 (1986) (discussing the history of predatory pricing theory in the courts and academic literature).

allow these difficult issues to further percolate in the lower courts. As the Solicitor General noted in his amicus brief urging the denial of certiorari in *LePage's*:

> There is insufficient experience with bundled discounts to this point to make a firm judgment about the relative prevalence of exclusionary versus pro-competitive bundled discounts. Relative to the practice of predatory pricing analyzed in *Brooke Group*, there is less knowledge on which to assess whether, or to what extent, the legal approach to a monopolist's allegedly exclusionary bundled discounts should be driven by a strong concern for false positives and low risk of false negatives. Further empirical development may shed light on that question.

Brief for United States as Amicus Curiae at 14, *3M Co. v. LePage's Inc.*, 124 S. Ct. 2932 (2004) (No. 02-1865), 2004 WL 1205191 (citation omitted). Pending further judicial and academic inquiry into the prevalence of anticompetitive bundled discounts, we think it preferable to allow plaintiffs to challenge bundled discounts if those plaintiffs can prove a defendant's bundled discounts would have excluded an equally efficient competitor.

To summarize, the primary anticompetitive danger posed by a multi-product bundled discount is that such a discount can exclude a rival is who is equally efficient at producing the competitive product simply because the rival does not sell as many products as the bundled discounter. Thus, a plaintiff who challenges a package discount as anticompetitive must prove that, when the full amount of the discounts given by the defendant is allocated to the competitive product or products, the resulting price of the competitive product or products is below the defendant's incremental cost to produce them. This requirement ensures that the only bundled discounts condemned as exclusionary are those that would exclude an equally efficient producer of the competitive product or products.

5

[8] The next issue before us is the appropriate measure of incremental costs in a bundled discounting case. In single product predatory pricing cases, the appropriate measure of incremental costs is an open question in this circuit. *See Rebel Oil Co. v. Atl. Richfield Co.*, 146 F.3d 1088, 1092 (9th Cir. 1998). The Supreme Court has likewise refused to decide the matter. *See Brooke Group*, 509 U.S. at 222 n.1; *Cargill*, 479 U.S. at 118 n.12.

As our cases and the relevant academic literature thoroughly discuss, firms face both fixed costs—costs that a firm must bear regardless of the amount of output—and variable costs—costs that change with the amount of output. The sum of fixed and variable costs is a firm's total cost. Marginal cost is the increase to total cost that occurs as a result of producing one additional unit of output. Average cost is the sum of fixed costs and total variable costs, divided by the amount of output. In their oft-cited 1975 law review article, Professors Areeda and Turner concluded that the optimal measure of a firm's cost in a predatory pricing case is marginal cost—the cost to produce one additional unit and the price that would obtain in the market under conditions of perfect competition. *See* Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 Harv. L. Rev. 697, 712, 716 (1975). However, Professors Areeda and Turner also recognized that "[t]he incremental cost of making and selling the last unit cannot readily be inferred from conventional business accounts, which typically go no further than showing observed average variable cost." *Id.* at 716. Thus, the professors adopted average variable cost as a surrogate for marginal cost. *Id.* A number of circuits have adopted the Areeda-Turner formulation and concluded that prices below average variable cost can indicate predation. *See*, *e.g.*, *Stearns Airport Equip. Co. v. FMC Corp.*, 170 F.3d 518, 532 (5th Cir. 1999); *Morgan v. Ponder*, 892 F.2d 1355, 1360 (8th Cir. 1989); *Barry Wright*, 724 F.2d at 236; *Ne. Tel. Co. v. AT&T Co.*, 651 F.2d 76, 87-88 (2d Cir. 1981).[19]

[9] Likewise, "we have approved the use of marginal or average variable cost statistics in proving predation." *See William Inglis & Sons Baking Co. v. ITT Cont'l Baking Co.*, 668 F.2d 1014, 1033 (9th Cir. 1981).[20] We have also held that a plaintiff can establish a prima facie case of predatory pricing

[19]At least one circuit has held that average total cost, not average variable cost, is the appropriate baseline for determining predation. *See McGahee v. N. Propane Gas Co.*, 858 F.2d 1487, 1500 (11th Cir. 1988). However, such an approach is inconsistent with the Supreme Court's instruction in *Brooke Group* that predatory prices are those below " 'some measure of *incremental* cost.' " *Brooke Group*, 509 U.S. at 223 (quoting *Cargill*, 479 U.S. at 117-18 n.12) (emphasis added). As the *Antitrust Law* treatise explains:

> In the ordinary case a predator increases output out of existing facilities, cutting the price to predatory levels. For this reason the Supreme Court has emphasized that predators must have excess capacity from which to produce the increased output. But in that case, the only "incremental" cost of the predation is variable costs.

3 Areeda & Hovenkamp, *supra*, ¶ 741c at 444 (2d ed. 2002) (footnote omitted).

[20]In a number of cases decided before *Brooke Group*, we held that pricing below marginal cost or average variable cost provided evidence that a pricing scheme was predatory, but also held that that mode of proof was not exclusive. *See Transamerica Computer Co. v. IBM Corp.*, 698 F.2d 1377, 1385 (9th Cir. 1983); *Inglis*, 668 F.2d at 1033. We suggested that an above-cost pricing policy could be predatory if accompanied by evidence of predatory intent, market power, or "long-run behavior." *See Transamerica*, 698 F.2d at 1387. Other circuits rejected the notion that predation could be proved through evidence of intent alone, *see, e.g.*, *Barry Wright*, 724 F.2d at 232, and *Brooke Group*'s holding that "a plaintiff seeking to establish competitive injury resulting from a rival's low prices must prove that the prices complained of are below an appropriate measure of its rival's costs" put to rest any notion that predation can be proven through evidence of intent alone, *Brooke Group*, 509 U.S. at 222.

by proving that the defendant's prices were below average variable cost. *Id.* at 1036. We see no reason to depart from these principles in the bundled discounting context, and we hold that the appropriate measure of costs for our cost-based standard is average variable cost.

6

[10] In summary, we hold the following: To prove that a bundled discount was exclusionary or predatory for the purposes of a monopolization or attempted monopolization claim under § 2 of the Sherman Act, the plaintiff must establish that, after allocating the discount given by the defendant on the entire bundle of products to the competitive product or products, the defendant sold the competitive product or products below its average variable cost of producing them. The district court's jury instruction on the attempted monopolization claim, which built on the holding of *LePage's* that we have rejected, thus contained an error of law.[21]

[21]As we noted above, the AMC's proposed standard in bundled discounting cases, in addition to requiring below-cost pricing, also contains two further proposed elements.

The second element proposed by the AMC is that there is a dangerous probability that the defendant will recoup its investment in the bundled discounting program. AMC Report, *supra*, at 99. This requirement, adopted from *Brooke Group*, is imported from the single product predatory pricing context, but we think imported incorrectly. We do not believe that the recoupment requirement from single product cases translates to multi-product discounting cases. Single-product predatory pricing, unlike bundling, necessarily involves a loss for the defendant. For a period of time, the defendant must sell below its cost, with the intent to eliminate its competitors so that, when its competition is eliminated, the defendant can charge supracompetitive prices, recouping its losses and potentially more. By contrast, as discussed above, exclusionary bundling does not necessarily involve any loss of profits for the bundled discounter. *See* Nalebuff, *supra*, 50 Antitrust Bull. at 327. As the example from *Ortho* illustrates, a bundled discounter can exclude its rivals who do not sell as many product lines even when the bundle as a whole, and the individual products within it, are priced above the discounter's incremental cost to

[11] McKenzie argues that we may nevertheless affirm the jury's verdict on the principle that flawed jury instructions are a harmless error when the facts which needed to be proven are strongly supported by the evidence presented at trial. *See Harmsen v. Smith*, 693 F.2d 932, 945 (9th Cir. 1982); *Cancellier v. Federated Dep't Stores*, 672 F.2d 1312, 1316 (9th Cir. 1982). In support of this argument, McKenzie points out that there was "undisputed evidence of [PeaceHealth's] higher prices and the need for [McKenzie] to sell beneath variable cost to hold Regence harmless from [PeaceHealth's] threatened price increases." However, as we have held, the relevant inquiry is not whether PeaceHealth's pricing practices forced McKenzie to price below cost, but whether PeaceHealth

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produce them. The trier of fact can identify cases that present this possibility for anticompetitive exclusion by applying the discount attribution standard outlined above. Under that standard, the ultimate question is whether the bundled discount would exclude an equally efficient rival. But because discounts on all products in the bundle have been allocated to the competitive product in issue, a conclusion of below-cost sales under the discount attribution standard may occur in some cases even where there is not an actual loss because the bundle is sold at a price exceeding incremental cost. In such a case, we do not think it is analytically helpful to think in terms of recoupment of a loss that did not occur.

The third element proposed by the AMC is that "the bundled discount or rebate program has had or is likely to have an adverse effect on competition." AMC Report, *supra*, at 99. We view this final element as redundant because it is no different than the general requirement of "antitrust injury" that a plaintiff must prove in any private antitrust action. *See Brunswick*, 429 U.S. at 489 (defining antitrust injury as "injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful" and noting that "[t]he injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation").

For these reasons, while adopting the AMC's proposal to require below-cost sales to prove exclusionary conduct, we do not adopt the element of recoupment, which we think may be inapplicable in some cases, and we do not adopt the element of "adverse effect on competition" as we think that is superfluous in light of the general and pre-existing requirement of antitrust injury under *Brunswick*.

priced its own services below an appropriate measure of its cost, as we have defined that concept using the discount attribution rule. In this case, we cannot conclude that the error in the jury instructions was harmless. We vacate the judgment entered in McKenzie's favor and remand for further proceedings consistent with our opinion.[22]

B

[12] After trial, the jury also returned a verdict in favor of McKenzie on its claim of primary-line price discrimination under Oregon state law. Because the validity of that jury verdict rests upon an unsettled question of Oregon antitrust law, we have certified that question to the Oregon Supreme Court.

C

[13] Finally, the jury found in favor of McKenzie on its Oregon tort law claim of intentional interference with prospective economic advantage. The parties agree that a claim of tortious interference under Oregon law requires a complementary finding of a violation of the antitrust laws. *See Kovac v. Crooked River Ranch Club & Maint. Ass'n*, 63 P.3d 1197, 1201 (Or. Ct. App. 2003); *Willamette Dental Group, P.C. v. Or. Dental Serv. Corp.*, 882 P.2d 637, 644 (Or. Ct. App. 1994). Because we have vacated the jury's verdict in favor of

[22]PeaceHealth also argues that because the jury found in its favor on McKenzie's claim of exclusive dealing under § 1 of the Sherman Act, it is entitled to judgment as a matter of law on McKenzie's claim of attempted monopolization under § 2 of the Sherman Act. Our vacatur of the jury's verdict on the attempted monopolization claim makes it unnecessary for us to fully address that argument. However, we previously have held that "[t]he 'predatory or anticompetitive conduct' element of § 2 attempt, like the conduct element of monopolization, encompasses more than violations of § 1." *Cal. Computer Prods., Inc. v. IBM Corp.*, 613 F.2d 727, 737 (9th Cir. 1979). Specifically, § 1 is limited to concerted activity, while § 2 reaches unilateral exclusive conduct. *See id.*; *Microsoft*, 253 F.3d at 70.

McKenzie on McKenzie's antitrust claims, we also vacate the jury's verdict in favor of McKenzie on McKenzie's claim of intentional interference with prospective economic advantage.

III

We next address McKenzie's cross-appeal.

A

Before trial, the district court granted PeaceHealth summary judgment on McKenzie's claim that PeaceHealth illegally tied primary and secondary services to its provision of tertiary services in violation of § 1 of the Sherman Act, 15 U.S.C. § 1. The district court granted summary judgment because McKenzie presented no evidence that the insurers were coerced into taking the tied product.

We review de novo the district court's grant of summary judgment. *Welles v. Turner Entm't Co.*, 488 F.3d 1178, 1183 (9th Cir. 2007). Federal Rule of Civil Procedure 56(c) entitles a party to summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." In deciding a motion for summary judgment, we view the evidence in the light most favorable to the non-moving party, and draw all justifiable inferences in favor of the non-moving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986); *Betz v. Trainer Wortham & Co.*, 486 F.3d 590, 591 (9th Cir. 2007).

A tying arrangement is a device used by a seller with market power in one product market to extend its market power to a distinct product market. *Paladin Assocs., Inc. v. Mont. Power Co.*, 328 F.3d 1145, 1159 (9th Cir. 2003). To accomplish this objective, the seller conditions the sale of one product (the tying product) on the buyer's purchase of a second product (the tied product).[23] *See Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 461 (1992); Posner, *supra*, at 197. Tying arrangements are forbidden on the theory that, if the seller has market power over the tying product, the seller can leverage this market power through tying arrangements to exclude other sellers of the tied product.[24] *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 14 (1984); *Fortner Enters., Inc. v. U.S. Steel Corp.*, 394 U.S. 495, 517-18 (1969) [hereinafter *Fortner I*] (White, J., dissenting).

The Supreme Court has developed a unique per se rule for illegal tying arrangements. For a tying claim to suffer per se condemnation, a plaintiff must prove: (1) that the defendant tied together the sale of two distinct products or services; (2) that the defendant possesses enough economic power in the tying product market to coerce its customers into purchasing the tied product; and (3) that the tying arrangement affects a "not insubstantial volume of commerce" in the tied product market. *See Paladin Assocs., Inc.*, 328 F.3d at 1159 (citing *Eastman Kodak*, 504 U.S. at 461-62).

As to the first element, McKenzie alleged two distinct products: tertiary services (the tying or desired product) and primary and secondary services (the tied or forced product). As to the third element, PeaceHealth does not dispute that the tying arrangement affected a substantial volume of commerce in the market for primary and secondary services. *See Fortner I*, 394 U.S. at 501. Thus, the only issue we must decide is

[23]A § 1 violation can also occur when the customer promises not to take the tied product from the defendant's competitor, but courts "rarely encounter[ ]" such a situation. 10 Areeda & Hovenkamp, *supra*, ¶ 1752c n.8 at 263 (2d ed. 2004).

[24]For criticism of the leverage theory, see Bork, *supra*, at 372. *See also* Christopher R. Leslie, *Cutting Through Tying Theory With Occam's Razor: A Simple Explanation of Tying Arrangements*, 78 Tul. L. Rev. 727, 731-41 (2004) (summarizing the conflict between leverage theorists and the Chicago School).

whether PeaceHealth coerced purchases of primary and secondary services.

McKenzie first argues that, in this particular case, it need not demonstrate coercion because it was a third party to the tying arrangements between PeaceHealth and the insurers, or, at the very least, that the standard for coercion is lower in cases brought by a third-party plaintiff. For the premise that the standard of coercion is lower or nonexistent for plaintiffs who are not parties to the tying arrangement, McKenzie relies heavily on the Fifth Circuit's opinion in *Heatransfer Corp. v. Volkswagenwerk, A.G.*, 553 F.2d 964 (5th Cir. 1977). In that case, the Fifth Circuit suggested that, in cases brought by third parties, "[t]he fact of coercion appears less important . . . [than] the fact of foreclosure." *Id.* at 978. But the Fifth Circuit did not abandon the coercion requirement in third-party suits. Instead, the court concluded that if the purchaser under the tying arrangement is "coerced or 'persuaded' to buy goods which they otherwise would not buy, with the result being tremendous lessening of the market in which a competitor sells his product, such a showing is sufficient to submit the question of a Section 1 antitrust violation to the jury." *Id.*

[14] Additionally, the suggestion that a lower (or no) coercion standard must be satisfied in third party suits, and in particular the dictum in *Heatransfer*, has been criticized by commentators:

> A few dicta have suggested that standards for proving a tying condition—often expressed as "coercion"—should be lower for defendant's rival than for its customers. This distinction was rightly rejected by the Eleventh Circuit, which correctly pointed out that every plaintiff must prove the tying condition, although of course the competitor need not show that it was itself was subjected to any such condition. Moreover, Supreme Court discussions about the

> existence of a tie have not varied according to the status of the plaintiff.

10 Areeda & Hovenkamp, *supra*, ¶ 1752d at 264 (2d ed. 2004) (footnotes omitted) (citing *Tic-X-Press v. Omni Promotions Co.*, 815 F.2d 1407, 1415 n.15 (11th Cir. 1987); *Heatransfer*, 553 F.2d at 978)). Indeed, the Supreme Court has emphasized that the coerced purchase of the tied product is the key aspect of an illegal tie:

> [T]he essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to *force* the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms.

Jefferson Parish, 466 U.S. at 12 (emphasis added). Thus, because coercion is often the touchstone issue in assessing a claim of illegal tying, we reject McKenzie's argument that, because it was not a party to the tying arrangement, it does not need to demonstrate coercion as part of its tying claim.

[15] McKenzie next argues that, even if coercion must be shown in tying cases brought by third parties, there was at least a disputed factual issue regarding coercion in this case. As evidence that no coercion was present in this case, the district court, in granting summary judgment to PeaceHealth, relied heavily on the deposition testimony of Farzenah Whyte, Regence's contract negotiator, who testified that Regence voluntarily entered into its contracts with PeaceHealth. PeaceHealth also points out that some insurers contracted to purchase PeaceHealth's services without exclusivity, indicating that PeaceHealth did not force those who wanted tertiary services to purchase primary and secondary services from PeaceHealth also.[25] *Cf. Moore v. Jas. H. Matthews & Co.*, 550

[25]McKenzie has filed a motion to strike portions of PeaceHealth's brief citing to evidence that insurers had alternatives to taking all services from

F.2d 1207, 1217 (9th Cir. 1977) (noting that "coercion may be implied from a showing that an appreciable number of buyers have accepted burdensome terms, such as a tie-in"). However, when all justifiable factual inferences are drawn in McKenzie's favor, there is no doubt that PeaceHealth's practice of giving a larger discount to insurers who dealt with it as an exclusive preferred provider may have coerced some insurers to purchase primary and secondary services from PeaceHealth rather than from McKenzie. We conclude that, as a whole, the evidence shows genuine factual disputes about whether PeaceHealth forced insurers either as an implied condition of dealing or as a matter of economic imperative through its bundled discounting, to take its primary and secondary services if the insurers wanted tertiary services.

First, while Whyte testified that Regence was not explicitly forced to deal exclusively with PeaceHealth, Whyte also testified that the higher prices PeaceHealth would have charged

PeaceHealth because the evidence PeaceHealth cites was not in the portion of the record designated to the district court on summary judgment. Specifically, McKenzie argues that we should not permit PeaceHealth on appeal to refer to portions of exhibits that, while submitted to the district court in support of PeaceHealth's motion for summary judgment, did not have their relevant portions highlighted for the district court.

Under the district court's Local Rule 56.1(c)(3), the moving party is required to highlight relevant portions of documents presented to the court, and under Local Rule 56.1(e), "the Court has no independent duty to search and consider any part of the court record not otherwise referenced in the separate concise statements of the parties." D. Or. R. 56.1. However, all of the documents cited by PeaceHealth on appeal were before the district court, even if not highlighted. Moreover, the principal policy underlying local rules like Rule 56.1 is to obviate the need for the district court to search the record for facts relevant to summary judgment. *Delange v. Dutra Constr., Co.*, 183 F.3d 916, 919 n.2 (9th Cir. 1999) (per curiam). Such a policy has no impact on the scope of our *appellate* review. *See* Fed. R. App. P. 10(a) (stating that the record on appeal consists of all papers and exhibits filed in the district court). We therefore deny McKenzie's motion to strike portions of PeaceHealth's combined brief.

Regence had McKenzie been admitted to Regence's PPP would have had a "large impact" on Regence. Also, Whyte stated that she had been "held hostage" by PeaceHealth's pricing practices.

Standing alone, the fact that a customer would end up paying higher prices to purchase the tied products separately does not necessarily create a fact issue on coercion. *Paladin*, 328 F.3d at 1162; *Robert's Waikiki U-Drive, Inc. v. Budget Rent-a-Car Sys., Inc.*, 732 F.2d 1403, 1407 (9th Cir. 1984). However, the record contains additional evidence of economic coercion. For example, while PeaceHealth emphasizes that four insurers in Lane County purchased PeaceHealth's services separately, "a trivial proportion of separate sales shows that the package discount is as effective as an outright refusal to sell [the tying product] separately." 10 Areeda & Hovenkamp, *supra*, ¶ 1758b at 327 (2d ed. 2004). In this case, there are twenty-eight insurers operating in Lane County. The fact that only four of them, or about 14% percent, made a separate purchase may indicate some degree of coercion, placing this issue in the realm of disputed facts that must be tendered to a jury. *See id.* at 328 (suggesting that a less than 10% proportion of separate sales indicates an illegal tie). Additionally, McKenzie provided some evidence that its prices on primary and secondary services were lower than PeaceHealth's prices on those services. Again, while not dispositive evidence of an illegal tie, it is a permissible inference that a rational customer would not purchase PeaceHealth's allegedly overpriced product in the absence of a tie. *See Data Gen. Corp. v. Grumman Sys. Support Corp.*, 36 F.3d 1147, 1181 (1st Cir. 1994); 10 Areeda & Hovenkamp, *supra*, ¶ 1756b3 at 301 (2d ed. 2004); *cf. Amerinet, Inc. v. Xerox Corp.*, 972 F.2d 1483, 1501 (8th Cir. 1992) (refusing to find an illegal tie in part because the plaintiff did not demonstrate that defendant used its market power in the tying product market "to shelter an inferior or overpriced product from competition"). McKenzie also offered expert testimony that Regence's exclusive relationship with PeaceHealth made no economic sense, evidencing coercion.

[16] Finally, the Supreme Court has condemned tying arrangements when the seller has the market power to force a purchaser to do something that he would not do in a competitive market. *Jefferson Parish*, 466 U.S. at 17. PeaceHealth was the only provider of tertiary services in the relevant geographic market. The substantial market power PeaceHealth possessed as a result of being the exclusive provider of tertiary services in Lane County creates a possibility that PeaceHealth was able to force unwanted purchases of primary and secondary services. In light of the evidence adduced by McKenzie at summary judgment, whether PeaceHealth in fact used its market power to effectively coerce purchases of primary and secondary services is a question that can be answered only through further factual development. The need for further factual development renders summary judgment on McKenzie's tying claim inappropriate.[26] Because a trier of fact might reasonably determine McKenzie established a claim of illegal tying based on the evidence in the record, we vacate the district court's order granting summary judgment to PeaceHealth and remand for further proceedings.[27]

[26]The Supreme Court has also held that the unique character of the tying product can provide a basis for holding that a defendant has sufficient economic power in the tying product market to coerce acceptance of the tied product. *See U.S. Steel Corp. v. Fortner Enters., Inc.*, 429 U.S. 610, 619 (1977) [hereinafter *Fortner II*] (citing *N. Pac. Ry. Co. v. United States*, 356 U.S. 1 (1958); *Int'l Salt Co. v. United States*, 332 U.S. 392 (1947)). The Court in *Fortner II* recognized that the key question in establishing sufficient market power is whether the seller has some cost advantage not shared by its competitors which makes its competitors *unable* to provide the tying product and that a mere showing that its competitors did not *want* to provide the tying product is insufficient to establish an illegal tie. *Id.* at 621-22. At the summary judgment stage, the evidence presented by McKenzie was sufficient to create a factual issue about whether McKenzie could not provide tertiary services or whether it was simply unwilling, as a matter of business strategy, to provide tertiary services.

[27]If, on remand, McKenzie stakes its tying claim not on a theory that PeaceHealth explicitly (e.g., by contract) or implicitly coerced insurers to

B

McKenzie raises two other issues on its cross-appeal related to rulings made by the district court during the course of the trial.

First, McKenzie contends that the district court erred by not admitting into evidence what McKenzie considered to be anti-competitive conduct of PeaceHealth in petitioning the Oregon attorney general to stop the McKenzie-Triad merger or condition approval of the merger on McKenzie taking certain actions. McKenzie maintains that the district court erred in holding that PeaceHealth's activity was protected from antitrust scrutiny under the *Noerr-Pennington* doctrine, which protects an antitrust defendant's right to petition the government. *See United Mine Workers v. Pennington*, 381 U.S. 657,

purchase primary and secondary services from PeaceHealth as a condition to obtaining tertiary services, but on a theory that PeaceHealth's bundled discounts effectively left insurers with no rational economic choice other than purchasing tertiary services from PeaceHealth, such a claim might raise the question of whether, to establish the coercion element of a tying claim through a bundled discount, McKenzie must prove that PeaceHealth priced below a relevant measure of its costs. Some commentators would require a plaintiff alleging that a bundled discount amounts to an illegal tie to prove below-cost prices. *See, e.g.*, 3 Areeda & Hovenkamp, *supra*, ¶ 749b2 at 334 (Supp. 2006). It is unclear whether the AMC intended its three-part test to apply when a plaintiff alleging an illegal tying arrangement asserts that the defendant's pricing practices coerced unwanted purchases of the tied product. *See* AMC Report, *supra*, at 114 n.157 ("The recommended three-part test is proposed here for challenges to bundled *pricing* practices, and its purpose, as the text explains, is to avoid deterring procompetitive price reductions. The Commission is not recommending application of this test outside the bundled pricing context, for example in tying or exclusive dealing cases. The Commission did not undertake to study tying and exclusive dealing issues more generally."). The parties have not briefed this issue to us, and the parties did not raise the issue before the district court. We therefore leave it to the district court, if necessary, to decide the issue in the first instance on remand. *Singleton v. Wulff*, 428 U.S. 106, 121 (1976).

670 (1965); *E. R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 143-44 (1961). Because we vacate the jury's verdict in Part II of our opinion, McKenzie's argument, which challenges evidentiary rulings the district court made at trial, is moot, and we decline to address it.

The second issue McKenzie raises on its cross-appeal is whether the jury instruction on "combination or conspiracy" to monopolize was correct. As we discussed above, the jury found for PeaceHealth on McKenzie's conspiracy to monopolize claim. The district court refused to give the following instruction proposed by McKenzie: "The involuntary nature of one's participation in a conspiracy to monopolize is no defense. An antitrust conspirator can be liable for damages even though he participates only under duress." McKenzie culled this language from our opinion in *Calnetics Corp. v. Volkswagen of America, Inc.*, 532 F.2d 674, 682 (9th Cir. 1976) (per curiam), in which we wrote, "[t]he involuntary nature of one's participation in a conspiracy to monopolize is no defense. An antitrust conspirator can be liable for damages even though he participates only under coercion." McKenzie argues that, because this instruction was not given, the jury may have found in PeaceHealth's favor because it viewed Regence's participation in PeaceHealth's alleged conspiracy to monopolize as involuntary.

As we noted above, the general rule is that we " 'review[ ] jury instructions to determine whether, taken as a whole, they mislead the jury or state the law incorrectly to the prejudice of the objecting party. So long as they do not, we review the formulation of the instructions and the choice of language for abuse of discretion.' " *City of Long Beach v. Standard Oil Co. of Cal.*, 46 F.3d 929, 933 (9th Cir. 1995) (quoting *Reed v. Hoy*, 909 F.2d 324, 326 (9th Cir. 1989)).

[17] While McKenzie's proposed instruction is a correct statement of the law of conspiracy as we explained it in *Calnetic Corp.*, it was within the district court's discretion to refuse to give the requested instruction because the instruction could have confused the jury. It is true that an antitrust conspirator “can be liable for damages” even though he participates in the conspiracy only under coercion. *See Flintkote Co. v. Lysfjord*, 246 F.2d 368, 375 (9th Cir. 1957). But the only conspirator who could have been “liable for damages” in this case was PeaceHealth, the sole defendant. Conversely, if anyone participated in the conspiracy under coercion, it was *Regence*. “A district court has substantial latitude in tailoring jury instructions . . . .” *Kendall-Jackson Winery, Ltd. v. E. & J. Gallo Winery*, 150 F.3d 1042, 1051 (9th Cir. 1998). We conclude that the district court was within its discretion in refusing to give McKenzie’s proposed conspiracy instruction.

IV

The final issue before us is the appeal and cross-appeal of the district court’s award of attorneys’ fees and costs to McKenzie. Because we have vacated the district court’s judgment in favor of McKenzie on the merits of McKenzie’s attempted monopolization and tortious interference claims, McKenzie is no longer a prevailing party for the purposes of Federal Rule of Civil Procedure 54(d)(1) and § 4(a) of the Clayton Act, 15 U.S.C. § 15(a). McKenzie is thus not entitled to attorneys’ fees, costs, and expenses, and we vacate the district court’s order awarding fees, costs, and expenses to McKenzie for those claims. If McKenzie prevails on remand, it may renew its request for attorneys’ fees and costs. We dismiss McKenzie’s cross-appeal on attorneys’ fees and costs as moot. We withhold a determination of attorneys’ fees, costs, and expenses for McKenzie’s price discrimination claim pending resolution of the question certified to the Oregon Supreme Court.

V

To summarize: In No. 05-35640, we **VACATE** the judgment in favor of McKenzie on its monopolization and tortious interference claims. We certify a question to the Oregon Supreme Court on the price discrimination claim. In No. 05-35627, we **VACATE** the summary judgment in favor of PeaceHealth.[28] In No. 05-36153, we **VACATE** the district court's order awarding attorneys' fees and costs to McKenzie. In No. 05-36202, we **DISMISS** the appeal as moot. Each party shall bear its own costs on appeal. We **STAY** further proceedings pending resolution of the price discrimination question certified to the Oregon Supreme Court.

[28]In No. 05-35627, we also decline to address McKenzie's *Noerr-Pennington* arguments because these related to an evidentiary ruling and the issue may not arise on a retrial. Further, we hold that the district court's jury instruction on combination or conspiracy was not an abuse of discretion.

Resale Price Maintenance

Syllabus

SUPREME COURT OF THE UNITED STATES

Syllabus

LEEGIN CREATIVE LEATHER PRODUCTS, INC. *v.* PSKS, INC., DBA KAY'S KLOSET . . . KAY'S SHOES

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 06–480. Argued March 26, 2007—Decided June 28, 2007

Given its policy of refusing to sell to retailers that discount its goods below suggested prices, petitioner (Leegin) stopped selling to respondent's (PSKS) store. PSKS filed suit, alleging, *inter alia,* that Leegin violated the antitrust laws by entering into vertical agreements with its retailers to set minimum resale prices. The District Court excluded expert testimony about Leegin's pricing policy's procompetitive effects on the ground that *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U. S. 373, makes it *per se* illegal under §1 of the Sherman Act for a manufacturer and its distributor to agree on the minimum price the distributor can charge for the manufacturer's goods. At trial, PSKS alleged that Leegin and its retailers had agreed to fix prices, but Leegin argued that its pricing policy was lawful under §1. The jury found for PSKS. On appeal, the Fifth Circuit declined to apply the rule of reason to Leegin's vertical price-fixing agreements and affirmed, finding that *Dr. Miles*' *per se* rule rendered irrelevant any procompetitive justifications for Leegin's policy.

Held: Dr. Miles is overruled and vertical price restraints are to be judged by the rule of reason. Pp. 5–28.

(a) The accepted standard for testing whether a practice restrains trade in violation of §1 is the rule of reason, which requires the factfinder to weigh "all of the circumstances," *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 49, including "specific information about the relevant business" and "the restraint's history, nature, and effect," *State Oil Co. v. Khan,* 522 U. S. 3, 10. The rule distinguishes between restraints with anticompetitive effect that are harmful to the consumer and those with procompetitive effect that are in the consumer's best interest. However, when a restraint is deemed "unlawful *per se,*" *ibid.,* the need to study an individual restraint's reasonableness in light of real market forces is eliminated, *Business Electronics Corp.* v. *Sharp Electronics Corp.*, 485 U. S. 717, 723. Resort to *per se* rules is confined to restraints "that would always or almost always tend to restrict competition and decrease output." *Ibid.* Thus, a *per se* rule is appropriate only after courts have had considerable experience with the type of restraint at issue, see *Broadcast Music, Inc.* v. *Columbia Broadcasting System, Inc.*, 441 U. S. 1, 9, and only if they can predict with confidence that the restraint would be invalidated in all or almost all instances under the rule of reason, see *Arizona* v. *Maricopa County Medical Soc.*, 457 U. S. 332, 344. Pp. 5–7.

(b) Because the reasons upon which *Dr. Miles* relied do not justify a *per se* rule, it is necessary to examine, in the first instance, the economic effects of vertical agreements to fix minimum resale prices and to determine whether the *per se* rule is nonetheless appropriate. Were this Court considering the issue as an original matter, the rule of reason, not a *per se* rule of unlawfulness, would be the appropriate standard to judge vertical price restraints. Pp. 7–19.

(1) Economics literature is replete with procompetitive justifications for a manufacturer's use of resale price maintenance, and the few recent studies on the subject also cast doubt on the conclusion that the practice meets the criteria for a *per se* rule. The justifications for vertical price restraints are similar to those for other vertical restraints. Minimum resale price maintenance can stimulate interbrand competition among manufacturers selling different brands of the same type of product by reducing intrabrand competition among retailers selling the same brand. This is important because the antitrust laws' "primary purpose . . . is to protect interbrand competition," *Khan*, *supra*, at 15. A single manufacturer's use of vertical price restraints tends to eliminate intrabrand price competition; this in turn encourages retailers to invest in services or promotional efforts that aid the manufacturer's position as against rival manufacturers. Resale price maintenance may also give consumers more options to choose among low-price, low-service brands; high-price, high-service brands; and brands falling in between. Absent vertical price restraints, retail services that enhance interbrand competition might be underprovided because discounting retailers can free ride on retailers who furnish services and then capture some of the demand those services generate. Retail price maintenance can also increase interbrand competition by facilitating market entry for new firms and brands and by encouraging retailer services that would not be provided even absent free riding. Pp. 9–12.

(2) Setting minimum resale prices may also have anticompetitive

effects; and unlawful price fixing, designed solely to obtain monopoly profits, is an ever present temptation. Resale price maintenance may, for example, facilitate a manufacturer cartel or be used to organize retail cartels. It can also be abused by a powerful manufacturer or retailer. Thus, the potential anticompetitive consequences of vertical price restraints must not be ignored or underestimated. Pp. 12–14.

(3) Notwithstanding the risks of unlawful conduct, it cannot be stated with any degree of confidence that retail price maintenance "always or almost always tend[s] to restrict competition and decrease output," *Business Electronics, supra,* at 723. Vertical retail-price agreements have either procompetitive or anticompetitive effects, depending on the circumstances in which they were formed; and the limited empirical evidence available does not suggest efficient uses of the agreements are infrequent or hypothetical. A *per se* rule should not be adopted for administrative convenience alone. Such rules can be counterproductive, increasing the antitrust system's total cost by prohibiting procompetitive conduct the antitrust laws should encourage. And a *per se* rule cannot be justified by the possibility of higher prices absent a further showing of anticompetitive conduct. The antitrust laws primarily are designed to protect interbrand competition from which lower prices can later result. Respondent's argument overlooks that, in general, the interests of manufacturers and consumers are aligned with respect to retailer profit margins. Resale price maintenance has economic dangers. If the rule of reason were to apply, courts would have to be diligent in eliminating their anticompetitive uses from the market. Factors relevant to the inquiry are the number of manufacturers using the practice, the restraint's source, and a manufacturer's market power. The rule of reason is designed and used to ascertain whether transactions are anticompetitive or procompetitive. This standard principle applies to vertical price restraints. As courts gain experience with these restraints by applying the rule of reason over the course of decisions, they can establish the litigation structure to ensure the rule operates to eliminate anticompetitive restraints from the market and to provide more guidance to businesses. Pp. 14–19.

(c) *Stare decisis* does not compel continued adherence to the *per se* rule here. Because the Sherman Act is treated as a common-law statute, its prohibition on "restraint[s] of trade" evolves to meet the dynamics of present economic conditions. The rule of reason's case-by-case adjudication implements this common-law approach. Here, respected economics authorities suggest that the *per se* rule is inappropriate. And both the Department of Justice and the Federal Trade Commission recommend replacing the *per se* rule with the rule of reason. In addition, this Court has "overruled [its] precedents when subsequent cases have undermined their doctrinal underpinnings." *Dickerson* v. *United States*, 530 U. S. 428, 443. It is not surprising that the Court has distanced itself from *Dr. Miles'* rationales, for the case was decided not long after the Sherman Act was enacted, when the Court had little experience with antitrust analysis. Only eight years after *Dr. Miles*, the Court reined in the decision, holding that a manufacturer can suggest resale prices and refuse to deal with distributors who do not follow them, *United States v. Colgate & Co.,* 250 U. S. 300, 307–308; and more recently the Court has tempered, limited, or overruled once strict vertical restraint prohibitions, see, *e.g., GTE Sylvania*, *supra,* at 57–59. The *Dr. Miles* rule is also inconsistent with a principled framework, for it makes little economic sense when analyzed with the Court's other vertical restraint cases. Deciding that procompetitive effects of resale price maintenance are insufficient to overrule *Dr. Miles* would call into question cases such as *Colgate* and *GTE Sylvania*. Respondent's arguments for reaffirming *Dr. Miles* based on *stare decisis* do not require a different result. Pp. 19–28.

171 Fed. Appx. 464, reversed and remanded.

KENNEDY, J., delivered the opinion of the Court, in which ROBERTS, C. J., and SCALIA, THOMAS, and ALITO, JJ., joined. BREYER, J., filed a dissenting opinion, in which STEVENS, SOUTER, and GINSBURG, JJ., joined.

SUPREME COURT OF THE UNITED STATES

No. 06–480

LEEGIN CREATIVE LEATHER PRODUCTS, INC., PETITIONER *v.* PSKS, INC., DBA KAY'S KLOSET . . . KAY'S SHOES

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

[June 28, 2007]

JUSTICE KENNEDY delivered the opinion of the Court.

In *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U. S. 373 (1911), the Court established the rule that it is *per se* illegal under §1 of the Sherman Act, 15 U. S. C. §1, for a manufacturer to agree with its distributor to set the minimum price the distributor can charge for the manufacturer's goods. The question presented by the instant case is whether the Court should overrule the *per se* rule and allow resale price maintenance agreements to be judged by the rule of reason, the usual standard applied to determine if there is a violation of §1. The Court has abandoned the rule of *per se* illegality for other vertical restraints a manufacturer imposes on its distributors. Respected economic analysts, furthermore, conclude that vertical price restraints can have procompetitive effects. We now hold that *Dr. Miles* should be overruled and that vertical price restraints are to be judged by the rule of reason.

I

Petitioner, Leegin Creative Leather Products, Inc.

(Leegin), designs, manufactures, and distributes leather goods and accessories. In 1991, Leegin began to sell belts under the brand name "Brighton." The Brighton brand has now expanded into a variety of women's fashion accessories. It is sold across the United States in over 5,000 retail establishments, for the most part independent, small boutiques and specialty stores. Leegin's president, Jerry Kohl, also has an interest in about 70 stores that sell Brighton products. Leegin asserts that, at least for its products, small retailers treat customers better, provide customers more services, and make their shopping experience more satisfactory than do larger, often impersonal retailers. Kohl explained: "[W]e want the consumers to get a different experience than they get in Sam's Club or in Wal-Mart. And you can't get that kind of experience or support or customer service from a store like Wal-Mart." 5 Record 127.

Respondent, PSKS, Inc. (PSKS), operates Kay's Kloset, a women's apparel store in Lewisville, Texas. Kay's Kloset buys from about 75 different manufacturers and at one time sold the Brighton brand. It first started purchasing Brighton goods from Leegin in 1995. Once it began selling the brand, the store promoted Brighton. For example, it ran Brighton advertisements and had Brighton days in the store. Kay's Kloset became the destination retailer in the area to buy Brighton products. Brighton was the store's most important brand and once accounted for 40 to 50 percent of its profits.

In 1997, Leegin instituted the "Brighton Retail Pricing and Promotion Policy." 4 *id.,* at 939. Following the policy, Leegin refused to sell to retailers that discounted Brighton goods below suggested prices. The policy contained an exception for products not selling well that the retailer did not plan on reordering. In the letter to retailers establishing the policy, Leegin stated:

> "In this age of mega stores like Macy's, Bloomingdales, May Co. and others, consumers are perplexed by promises of product quality and support of product which we believe is lacking in these large stores. Consumers are further confused by the ever popular sale, sale, sale, etc.
>
> "We, at Leegin, choose to break away from the pack by selling [at] specialty stores; specialty stores that can offer the customer great quality merchandise, superb service, and support the Brighton product 365 days a year on a consistent basis.
>
> "We realize that half the equation is Leegin producing great Brighton product and the other half is you, our retailer, creating great looking stores selling our products in a quality manner." *Ibid.*

Leegin adopted the policy to give its retailers sufficient margins to provide customers the service central to its distribution strategy. It also expressed concern that discounting harmed Brighton's brand image and reputation.

A year after instituting the pricing policy Leegin introduced a marketing strategy known as the "Heart Store Program." See *id.,* at 962–972. It offered retailers incentives to become Heart Stores, and, in exchange, retailers pledged, among other things, to sell at Leegin's suggested prices. Kay's Kloset became a Heart Store soon after Leegin created the program. After a Leegin employee visited the store and found it unattractive, the parties appear to have agreed that Kay's Kloset would not be a Heart Store beyond 1998. Despite losing this status, Kay's Kloset continued to increase its Brighton sales.

In December 2002, Leegin discovered Kay's Kloset had been marking down Brighton's entire line by 20 percent. Kay's Kloset contended it placed Brighton products on sale to compete with nearby retailers who also were undercutting Leegin's suggested prices. Leegin, nonetheless, requested that Kay's Kloset cease discounting. Its request refused, Leegin stopped selling to the store. The loss of the Brighton brand had a considerable negative impact on the store's revenue from sales.

PSKS sued Leegin in the United States District Court for the Eastern District of Texas. It alleged, among other claims, that Leegin had violated the antitrust laws by "enter[ing] into agreements with retailers to charge only those prices fixed by Leegin." *Id.,* at 1236. Leegin planned to introduce expert testimony describing the procompetitive effects of its pricing policy. The District Court excluded the testimony, relying on the *per se* rule established by *Dr. Miles*. At trial PSKS argued that the Heart Store program, among other things, demonstrated Leegin and its retailers had agreed to fix prices. Leegin responded that it had established a unilateral pricing policy lawful under §1, which applies only to concerted action. See *United States* v. *Colgate & Co.*, 250 U. S. 300, 307 (1919). The jury agreed with PSKS and awarded it $1.2 million. Pursuant to 15 U. S. C. §15(a), the District Court trebled the damages and reimbursed PSKS for its attorney's fees and costs. It entered judgment against Leegin in the amount of $3,975,000.80.

The Court of Appeals for the Fifth Circuit affirmed. 171 Fed. Appx. 464 (2006) *(per curiam)*. On appeal Leegin did not dispute that it had entered into vertical price-fixing agreements with its retailers. Rather, it contended that the rule of reason should have applied to those agreements. The Court of Appeals rejected this argument. *Id.,* at 466–467. It was correct to explain that it remained bound by *Dr. Miles* "[b]ecause [the Supreme] Court has consistently applied the *per se* rule to [vertical minimum price-fixing] agreements." 171 Fed. Appx., at 466. On this premise the Court of Appeals held that the District Court did not abuse its discretion in excluding the testimony of Leegin's economic expert, for the *per se* rule rendered irrelevant any procompetitive justifications for Leegin's pricing policy. *Id.,* at 467. We granted certiorari to determine whether vertical minimum resale price maintenance agreements should continue to be treated as *per se* unlawful. 549 U. S. ___ (2006).

II

Section 1 of the Sherman Act prohibits "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States." Ch. 647, 26 Stat. 209, as amended, 15 U. S. C. §1. While §1 could be interpreted to proscribe all contracts, see, *e.g., Board of Trade of Chicago* v. *United States*, 246 U. S. 231, 238 (1918), the Court has never "taken a literal approach to [its] language," *Texaco Inc.* v. *Dagher*, 547 U. S. 1, 5 (2006). Rather, the Court has repeated time and again that §1 "outlaw[s] only unreasonable restraints." *State Oil Co.* v. *Khan*, 522 U. S. 3, 10 (1997).

The rule of reason is the accepted standard for testing whether a practice restrains trade in violation of §1. See *Texaco, supra,* at 5. "Under this rule, the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 49 (1977). Appropriate factors to take into account include "specific information about the relevant business" and "the restraint's history, nature, and effect." *Khan*, *supra,* at 10. Whether the businesses involved have market power is a further, significant consideration. See, *e.g., Copperweld Corp.* v. *Independence Tube Corp.*, 467 U. S. 752, 768 (1984) (equating the rule of reason with "an inquiry into market power and market structure designed to assess [a restraint's] actual effect"); see also *Illinois Tool Works Inc.* v. *Independent Ink, Inc.*, 547 U. S. 28, 45–46 (2006). In its design and function the rule distinguishes between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest.

The rule of reason does not govern all restraints. Some types "are deemed unlawful *per se*." *Khan*, *supra,* at 10. The *per se* rule, treating categories of restraints as necessarily illegal, eliminates the need to study the reasonableness of an individual restraint in light of the real market forces at work, *Business Electronics Corp.* v. *Sharp Electronics Corp.*, 485 U. S. 717, 723 (1988); and, it must be acknowledged, the *per se* rule can give clear guidance for certain conduct. Restraints that are *per se* unlawful include horizontal agreements among competitors to fix prices, see *Texaco*, *supra,* at 5, or to divide markets, see *Palmer* v. *BRG of Ga., Inc.*, 498 U. S. 46, 49–50 (1990) *(per curiam)*.

Resort to *per se* rules is confined to restraints, like those mentioned, "that would always or almost always tend to restrict competition and decrease output." *Business Electronics*, *supra,* at 723 (internal quotation marks omitted). To justify a *per se* prohibition a restraint must have "manifestly anticompetitive" effects, *GTE Sylvania*, *supra,* at 50, and "lack . . . any redeeming virtue," *Northwest Wholesale Stationers, Inc.* v. *Pacific Stationery & Printing Co.*, 472 U. S. 284, 289 (1985) (internal quotation marks omitted).

As a consequence, the *per se* rule is appropriate only after courts have had considerable experience with the type of restraint at issue, see *Broadcast Music, Inc.* v. *Columbia Broadcasting System, Inc.*, 441 U. S. 1, 9 (1979), and only if courts can predict with confidence that it would be invalidated in all or almost all instances under the rule of reason, see *Arizona* v. *Maricopa County Medical Soc.*, 457 U. S. 332, 344 (1982). It should come as no surprise, then, that "we have expressed reluctance to adopt *per se* rules with regard to restraints imposed in the context of business relationships where the economic impact of certain practices is not immediately obvious." *Khan*, *supra,* at 10 (internal quotation marks omitted); see also *White Motor Co.* v. *United States*, 372 U. S. 253, 263 (1963) (refusing to adopt a *per se* rule for a vertical nonprice restraint because of the uncertainty concerning whether this type of restraint satisfied the demanding standards necessary to apply a *per se* rule). And, as we have stated, a "departure from the rule-of-reason standard must be based upon demonstrable economic effect rather than . . . upon formalistic line drawing." *GTE Sylvania*, *supra,* at 58–59.

III

The Court has interpreted *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U. S. 373 (1911), as establishing a *per se* rule against a vertical agreement between a manufacturer and its distributor to set minimum resale prices. See, *e.g., Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U. S. 752, 761 (1984). In *Dr. Miles* the plaintiff, a manufacturer of medicines, sold its products only to distributors who agreed to resell them at set prices. The Court found the manufacturer's control of resale prices to be unlawful. It relied on the common-law rule that "a general restraint upon alienation is ordinarily invalid." 220 U. S., at 404–405. The Court then explained that the agreements would advantage the distributors, not the manufacturer, and were analogous to a combination among competing distributors, which the law treated as void. *Id.,* at 407–408.

The reasoning of the Court's more recent jurisprudence has rejected the rationales on which *Dr. Miles* was based. By relying on the common-law rule against restraints on alienation, *id.,* at 404–405, the Court justified its decision based on "formalistic" legal doctrine rather than "demonstrable economic effect," *GTE Sylvania*, *supra,* at 58–59. The Court in *Dr. Miles* relied on a treatise published in

1628, but failed to discuss in detail the business reasons that would motivate a manufacturer situated in 1911 to make use of vertical price restraints. Yet the Sherman Act's use of "restraint of trade" "invokes the common law itself, . . . not merely the static content that the common law had assigned to the term in 1890." *Business Electronics*, *supra,* at 732. The general restraint on alienation, especially in the age when then-Justice Hughes used the term, tended to evoke policy concerns extraneous to the question that controls here. Usually associated with land, not chattels, the rule arose from restrictions removing real property from the stream of commerce for generations. The Court should be cautious about putting dispositive weight on doctrines from antiquity but of slight relevance. We reaffirm that "the state of the common law 400 or even 100 years ago is irrelevant to the issue before us: the effect of the antitrust laws upon vertical distributional restraints in the American economy today." *GTE Sylvania*, 433 U. S., at 53, n. 21 (internal quotation marks omitted).

Dr. Miles, furthermore, treated vertical agreements a manufacturer makes with its distributors as analogous to a horizontal combination among competing distributors. See 220 U. S., at 407–408. In later cases, however, the Court rejected the approach of reliance on rules governing horizontal restraints when defining rules applicable to vertical ones. See, *e.g., Business Electronics*, *supra,* at 734 (disclaiming the "notion of equivalence between the scope of horizontal *per se* illegality and that of vertical *per se* illegality"); *Maricopa County*, *supra,* at 348, n. 18 (noting that "horizontal restraints are generally less defensible than vertical restraints"). Our recent cases formulate antitrust principles in accordance with the appreciated differences in economic effect between vertical and horizontal agreements, differences the *Dr. Miles* Court failed to consider.

The reasons upon which *Dr. Miles* relied do not justify a *per se* rule. As a consequence, it is necessary to examine, in the first instance, the economic effects of vertical agreements to fix minimum resale prices, and to determine whether the *per se* rule is nonetheless appropriate. See *Business Electronics*, 485 U. S., at 726.

A

Though each side of the debate can find sources to support its position, it suffices to say here that economics literature is replete with procompetitive justifications for a manufacturer's use of resale price maintenance. See, *e.g.,* Brief for Economists as *Amici Curiae* 16 ("In the theoretical literature, it is essentially undisputed that minimum [resale price maintenance] can have procompetitive effects and that under a variety of market conditions it is unlikely to have anticompetitive effects"); Brief for United States as *Amicus Curiae* 9 ("[T]here is a widespread consensus that permitting a manufacturer to control the price at which its goods are sold may promote *inter*brand competition and consumer welfare in a variety of ways"); ABA Section of Antitrust Law, Antitrust Law and Economics of Product Distribution 76 (2006) ("[T]he bulk of the economic literature on [resale price maintenance] suggests that [it] is more likely to be used to enhance efficiency than for anticompetitive purposes"); see also H. Hovenkamp, The Antitrust Enterprise: Principle and Execution 184–191 (2005) (hereinafter Hovenkamp); R. Bork, The Antitrust Paradox 288–291 (1978) (hereinafter Bork). Even those more skeptical of resale price maintenance acknowledge it can have procompetitive effects. See, *e.g.,* Brief for William S. Comanor et al. as *Amici Curiae* 3 ("[G]iven [the] diversity of effects [of resale price maintenance], one could reasonably take the position that a *rule of reason* rather than a *per se* approach is warranted"); F.M. Scherer & D. Ross, Industrial Market Structure and Economic Performance 558 (3d ed. 1990) (hereinafter

Scherer & Ross) ("The overall balance between benefits and costs [of resale price maintenance] is probably close").

The few recent studies documenting the competitive effects of resale price maintenance also cast doubt on the conclusion that the practice meets the criteria for a *per se* rule. See T. Overstreet, Resale Price Maintenance: Economic Theories and Empirical Evidence 170 (1983) (hereinafter Overstreet) (noting that "[e]fficient uses of [resale price maintenance] are evidently not unusual or rare"); see also Ippolito, Resale Price Maintenance: Empirical Evidence From Litigation, 34 J. Law & Econ. 263, 292–293 (1991) (hereinafter Ippolito).

The justifications for vertical price restraints are similar to those for other vertical restraints. See *GTE Sylvania*, 433 U. S., at 54–57. Minimum resale price maintenance can stimulate interbrand competition—the competition among manufacturers selling different brands of the same type of product—by reducing intrabrand competition—the competition among retailers selling the same brand. See *id.,* at 51–52. The promotion of interbrand competition is important because "the primary purpose of the antitrust laws is to protect [this type of] competition." *Khan*, 522 U. S., at 15. A single manufacturer's use of vertical price restraints tends to eliminate intrabrand price competition; this in turn encourages retailers to invest in tangible or intangible services or promotional efforts that aid the manufacturer's position as against rival manufacturers. Resale price maintenance also has the potential to give consumers more options so that they can choose among low-price, low-service brands; high-price, high-service brands; and brands that fall in between.

Absent vertical price restraints, the retail services that enhance interbrand competition might be underprovided. This is because discounting retailers can free ride on retailers who furnish services and then capture some of the increased demand those services generate. *GTE Syl-*

vania, *supra,* at 55. Consumers might learn, for example, about the benefits of a manufacturer's product from a retailer that invests in fine showrooms, offers product demonstrations, or hires and trains knowledgeable employees. R. Posner, Antitrust Law 172–173 (2d ed. 2001) (hereinafter Posner). Or consumers might decide to buy the product because they see it in a retail establishment that has a reputation for selling high-quality merchandise. Marvel & McCafferty, Resale Price Maintenance and Quality Certification, 15 Rand J. Econ. 346, 347–349 (1984) (hereinafter Marvel & McCafferty). If the consumer can then buy the product from a retailer that discounts because it has not spent capital providing services or developing a quality reputation, the high-service retailer will lose sales to the discounter, forcing it to cut back its services to a level lower than consumers would otherwise prefer. Minimum resale price maintenance alleviates the problem because it prevents the discounter from undercutting the service provider. With price competition decreased, the manufacturer's retailers compete among themselves over services.

Resale price maintenance, in addition, can increase interbrand competition by facilitating market entry for new firms and brands. "[N]ew manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and aggressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer." *GTE Sylvania*, *supra,* at 55; see Marvel & McCafferty 349 (noting that reliance on a retailer's reputation "will decline as the manufacturer's brand becomes better known, so that [resale price maintenance] may be particularly important as a competitive device for new entrants"). New products and new brands are essential to a dynamic economy, and if markets can be penetrated by using resale price maintenance there is a procompetitive effect.

Resale price maintenance can also increase interbrand competition by encouraging retailer services that would not be provided even absent free riding. It may be difficult and inefficient for a manufacturer to make and enforce a contract with a retailer specifying the different services the retailer must perform. Offering the retailer a guaranteed margin and threatening termination if it does not live up to expectations may be the most efficient way to expand the manufacturer's market share by inducing the retailer's performance and allowing it to use its own initiative and experience in providing valuable services. See Mathewson & Winter, The Law and Economics of Resale Price Maintenance, 13 Rev. Indus. Org. 57, 74–75 (1998) (hereinafter Mathewson & Winter); Klein & Murphy, Vertical Restraints as Contract Enforcement Mechanisms, 31 J. Law & Econ. 265, 295 (1988); see also Deneckere, Marvel, & Peck, Demand Uncertainty, Inventories, and Resale Price Maintenance, 111 Q. J. Econ. 885, 911 (1996) (noting that resale price maintenance may be beneficial to motivate retailers to stock adequate inventories of a manufacturer's goods in the face of uncertain consumer demand).

B

While vertical agreements setting minimum resale prices can have procompetitive justifications, they may have anticompetitive effects in other cases; and unlawful price fixing, designed solely to obtain monopoly profits, is an ever present temptation. Resale price maintenance may, for example, facilitate a manufacturer cartel. See *Business Electronics*, 485 U. S., at 725. An unlawful cartel will seek to discover if some manufacturers are undercutting the cartel's fixed prices. Resale price maintenance could assist the cartel in identifying price-cutting manufacturers who benefit from the lower prices they offer.

Resale price maintenance, furthermore, could discourage a manufacturer from cutting prices to retailers with the concomitant benefit of cheaper prices to consumers. See *ibid.;* see also Posner 172; Overstreet 19–23.

Vertical price restraints also "might be used to organize cartels at the retailer level." *Business Electronics*, *supra,* at 725–726. A group of retailers might collude to fix prices to consumers and then compel a manufacturer to aid the unlawful arrangement with resale price maintenance. In that instance the manufacturer does not establish the practice to stimulate services or to promote its brand but to give inefficient retailers higher profits. Retailers with better distribution systems and lower cost structures would be prevented from charging lower prices by the agreement. See Posner 172; Overstreet 13–19. Historical examples suggest this possibility is a legitimate concern. See, *e.g.,* Marvel & McCafferty, The Welfare Effects of Resale Price Maintenance, 28 J. Law & Econ. 363, 373 (1985) (hereinafter Marvel) (providing an example of the power of the National Association of Retail Druggists to compel manufacturers to use resale price maintenance); Hovenkamp 186 (suggesting that the retail druggists in *Dr. Miles* formed a cartel and used manufacturers to enforce it).

A horizontal cartel among competing manufacturers or competing retailers that decreases output or reduces competition in order to increase price is, and ought to be, *per se* unlawful. See *Texaco*, 547 U. S., at 5; *GTE Sylvania*, 433 U. S., at 58, n. 28. To the extent a vertical agreement setting minimum resale prices is entered upon to facilitate either type of cartel, it, too, would need to be held unlawful under the rule of reason. This type of agreement may also be useful evidence for a plaintiff attempting to prove the existence of a horizontal cartel.

Resale price maintenance, furthermore, can be abused by a powerful manufacturer or retailer. A dominant retailer, for example, might request resale price maintenance to forestall innovation in distribution that decreases costs. A manufacturer might consider it has little choice but to accommodate the retailer's demands for vertical price restraints if the manufacturer believes it needs access to the retailer's distribution network. See Overstreet 31; 8 P. Areeda & H. Hovenkamp, Antitrust Law 47 (2d ed. 2004) (hereinafter Areeda & Hovenkamp); cf. *Toys "R" Us, Inc.* v. *FTC*, 221 F. 3d 928, 937–938 (CA7 2000). A manufacturer with market power, by comparison, might use resale price maintenance to give retailers an incentive not to sell the products of smaller rivals or new entrants. See, *e.g.,* Marvel 366–368. As should be evident, the potential anticompetitive consequences of vertical price restraints must not be ignored or underestimated.

C

Notwithstanding the risks of unlawful conduct, it cannot be stated with any degree of confidence that resale price maintenance "always or almost always tend[s] to restrict competition and decrease output." *Business Electronics*, *supra,* at 723 (internal quotation marks omitted). Vertical agreements establishing minimum resale prices can have either procompetitive or anticompetitive effects, depending upon the circumstances in which they are formed. And although the empirical evidence on the topic is limited, it does not suggest efficient uses of the agreements are infrequent or hypothetical. See Overstreet 170; see also *id.,* at 80 (noting that for the majority of enforcement actions brought by the Federal Trade Commission between 1965 and 1982, "the use of [resale price maintenance] was not likely motivated by collusive dealers who had successfully coerced their suppliers"); Ippolito 292 (reaching a similar conclusion). As the rule would proscribe a significant amount of procompetitive conduct, these agreements appear ill suited for *per se* condemnation.

Respondent contends, nonetheless, that vertical price restraints should be *per se* unlawful because of the administrative convenience of *per se* rules. See, *e.g., GTE Sylvania*, *supra,* at 50, n. 16 (noting "*per se* rules tend to provide guidance to the business community and to minimize the burdens on litigants and the judicial system"). That argument suggests *per se* illegality is the rule rather than the exception. This misinterprets our antitrust law. *Per se* rules may decrease administrative costs, but that is only part of the equation. Those rules can be counterproductive. They can increase the total cost of the antitrust system by prohibiting procompetitive conduct the antitrust laws should encourage. See Easterbrook, Vertical Arrangements and the Rule of Reason, 53 Antitrust L. J. 135, 158 (1984) (hereinafter Easterbrook). They also may increase litigation costs by promoting frivolous suits against legitimate practices. The Court has thus explained that administrative "advantages are not sufficient in themselves to justify the creation of *per se* rules," *GTE Sylvania*, 433 U. S., at 50, n. 16, and has relegated their use to restraints that are "manifestly anticompetitive," *id.,* at 49–50. Were the Court now to conclude that vertical price restraints should be *per se* illegal based on administrative costs, we would undermine, if not overrule, the traditional "demanding standards" for adopting *per se* rules. *Id.,* at 50. Any possible reduction in administrative costs cannot alone justify the *Dr. Miles* rule.

Respondent also argues the *per se* rule is justified because a vertical price restraint can lead to higher prices for the manufacturer's goods. See also Overstreet 160 (noting that "price surveys indicate that [resale price maintenance] in most cases increased the prices of products sold"). Respondent is mistaken in relying on pricing effects absent a further showing of anticompetitive conduct. Cf. *id.,* at 106 (explaining that price surveys "do not necessarily tell us anything conclusive about the welfare effects of [resale price maintenance] because the results are generally consistent with both procompetitive and anticompetitive theories"). For, as has been indicated already, the antitrust laws are designed primarily to protect interbrand competition, from which lower prices can later result. See *Khan*, 522 U. S., at 15. The Court, moreover, has evaluated other vertical restraints under the rule of reason even though prices can be increased in the course of promoting procompetitive effects. See, *e.g., Business Electronics*, 485 U. S., at 728. And resale price maintenance may reduce prices if manufacturers have resorted to costlier alternatives of controlling resale prices that are not *per se* unlawful. See *infra*, at 22–25; see also Marvel 371.

Respondent's argument, furthermore, overlooks that, in general, the interests of manufacturers and consumers are aligned with respect to retailer profit margins. The difference between the price a manufacturer charges retailers and the price retailers charge consumers represents part of the manufacturer's cost of distribution, which, like any other cost, the manufacturer usually desires to minimize. See *GTE Sylvania*, 433 U. S., at 56, n. 24; see also *id.,* at 56 ("Economists . . . have argued that manufacturers have an economic interest in maintaining as much intrabrand competition as is consistent with the efficient distribution of their products"). A manufacturer has no incentive to overcompensate retailers with unjustified margins. The retailers, not the manufacturer, gain from higher retail prices. The manufacturer often loses; interbrand competition reduces its competitiveness and market share because consumers will "substitute a different brand of the same product." *Id.,* at 52, n. 19; see *Business Electronics*, *supra,* at 725. As a general matter, therefore, a single manufacturer will desire to set minimum resale prices only if the "increase in demand resulting from enhanced service . . . will more than offset a negative impact on demand of a higher retail price." Mathewson & Winter 67.

The implications of respondent's position are far reaching. Many decisions a manufacturer makes and carries out through concerted action can lead to higher prices. A manufacturer might, for example, contract with different suppliers to obtain better inputs that improve product quality. Or it might hire an advertising agency to promote awareness of its goods. Yet no one would think these actions violate the Sherman Act because they lead to higher prices. The antitrust laws do not require manufacturers to produce generic goods that consumers do not know about or want. The manufacturer strives to improve its product quality or to promote its brand because it believes this conduct will lead to increased demand despite higher prices. The same can hold true for resale price maintenance.

Resale price maintenance, it is true, does have economic dangers. If the rule of reason were to apply to vertical price restraints, courts would have to be diligent in eliminating their anticompetitive uses from the market. This is a realistic objective, and certain factors are relevant to the inquiry. For example, the number of manufacturers that make use of the practice in a given industry can provide important instruction. When only a few manufacturers lacking market power adopt the practice, there is little likelihood it is facilitating a manufacturer cartel, for a cartel then can be undercut by rival manufacturers. See Overstreet 22; Bork 294. Likewise, a retailer cartel is unlikely when only a single manufacturer in a competitive market uses resale price maintenance. Interbrand competition would divert consumers to lower priced substitutes and eliminate any gains to retailers from their price-fixing agreement over a single brand. See Posner 172; Bork 292. Resale price maintenance should be subject to more careful scrutiny, by contrast, if many competing manufacturers adopt the practice. Cf. Scherer & Ross 558 (noting that "except when [resale price maintenance] spreads to cover the bulk of an industry's output, depriving consumers of a meaningful choice between high-service and low-price outlets, most [resale price maintenance arrangements] are probably innocuous"); Easterbrook 162 (suggesting that "every one of the potentially-anticompetitive outcomes of vertical arrangements depends on the uniformity of the practice").

The source of the restraint may also be an important consideration. If there is evidence retailers were the impetus for a vertical price restraint, there is a greater likelihood that the restraint facilitates a retailer cartel or supports a dominant, inefficient retailer. See Brief for William S. Comanor et al. as *Amici Curiae* 7–8. If, by contrast, a manufacturer adopted the policy independent of retailer pressure, the restraint is less likely to promote anticompetitive conduct. Cf. Posner 177 ("It makes all the difference whether minimum retail prices are imposed by the manufacturer in order to evoke point-of-sale services or by the dealers in order to obtain monopoly profits"). A manufacturer also has an incentive to protest inefficient retailer-induced price restraints because they can harm its competitive position.

As a final matter, that a dominant manufacturer or retailer can abuse resale price maintenance for anticompetitive purposes may not be a serious concern unless the relevant entity has market power. If a retailer lacks market power, manufacturers likely can sell their goods through rival retailers. See also *Business Electronics*, *supra,* at 727, n. 2 (noting "[r]etail market power is rare, because of the usual presence of interbrand competition and other dealers"). And if a manufacturer lacks market power, there is less likelihood it can use the practice to keep competitors away from distribution outlets.

The rule of reason is designed and used to eliminate anticompetitive transactions from the market. This standard principle applies to vertical price restraints. A party alleging injury from a vertical agreement setting minimum resale prices will have, as a general matter, the information and resources available to show the existence of the agreement and its scope of operation. As courts gain experience considering the effects of these restraints by applying the rule of reason over the course of decisions, they can establish the litigation structure to ensure the rule operates to eliminate anticompetitive restraints from the market and to provide more guidance to businesses. Courts can, for example, devise rules over time for offering proof, or even presumptions where justified, to make the rule of reason a fair and efficient way to prohibit anticompetitive restraints and to promote procompetitive ones.

For all of the foregoing reasons, we think that were the Court considering the issue as an original matter, the rule of reason, not a *per se* rule of unlawfulness, would be the appropriate standard to judge vertical price restraints.

IV

We do not write on a clean slate, for the decision in *Dr. Miles* is almost a century old. So there is an argument for its retention on the basis of *stare decisis* alone. Even if *Dr. Miles* established an erroneous rule, "*[s]tare decisis* reflects a policy judgment that in most matters it is more important that the applicable rule of law be settled than that it be settled right." *Khan*, 522 U. S., at 20 (internal quotation marks omitted). And concerns about maintaining settled law are strong when the question is one of statutory interpretation. See, *e.g., Hohn* v. *United States*, 524 U. S. 236, 251 (1998).

Stare decisis is not as significant in this case, however, because the issue before us is the scope of the Sherman Act. *Khan*, *supra,* at 20 ("[T]he general presumption that legislative changes should be left to Congress has less force with respect to the Sherman Act"). From the beginning the Court has treated the Sherman Act as a common-law statute. See *National Soc. of Professional Engineers* v. *United States*, 435 U. S. 679, 688 (1978); see also *Northwest Airlines, Inc.* v. *Transport Workers*, 451 U. S. 77, 98, n. 42 (1981) ("In antitrust, the federal courts . . . act more as common-law courts than in other areas governed by federal statute"). Just as the common law adapts to modern understanding and greater experience, so too does the Sherman Act's prohibition on "restraint[s] of trade" evolve to meet the dynamics of present economic conditions. The case-by-case adjudication contemplated by the rule of reason has implemented this common-law approach. See *National Soc. of Professional Engineers*, *supra,* at 688. Likewise, the boundaries of the doctrine of *per se* illegality should not be immovable. For "[i]t would make no sense to create out of the single term 'restraint of trade' a chronologically schizoid statute, in which a 'rule of reason' evolves with new circumstance and new wisdom, but a line of *per se* illegality remains forever fixed where it was." *Business Electronics*, 485 U. S., at 732.

A

Stare decisis, we conclude, does not compel our continued adherence to the *per se* rule against vertical price restraints. As discussed earlier, respected authorities in the economics literature suggest the *per se* rule is inappropriate, and there is now widespread agreement that resale price maintenance can have procompetitive effects. See, *e.g.,* Brief for Economists as *Amici Curiae* 16. It is also significant that both the Department of Justice and the Federal Trade Commission—the antitrust enforcement agencies with the ability to assess the long-term impacts of resale price maintenance—have recommended that this Court replace the *per se* rule with the traditional rule of reason. See Brief for United States as *Amicus Curiae* 6. In the antitrust context the fact that a decision has been "called into serious question" justifies our reevaluation of it. *Khan*, *supra,* at 21.

Other considerations reinforce the conclusion that *Dr. Miles* should be overturned. Of most relevance, "we have overruled our precedents when subsequent cases have undermined their doctrinal underpinnings." *Dickerson* v. *United States*, 530 U. S. 428, 443 (2000). The Court's treatment of vertical restraints has progressed away from *Dr. Miles*' strict approach. We have distanced ourselves from the opinion's rationales. See *supra,* at 7–8; see also *Khan*, *supra,* at 21 (overruling a case when "the views underlying [it had been] eroded by this Court's precedent"); *Rodriguez de Quijas* v. *Shearson/American Express, Inc.*, 490 U. S. 477, 480–481 (1989) (same). This is unsurprising, for the case was decided not long after enactment of the Sherman Act when the Court had little experience with antitrust analysis. Only eight years after *Dr. Miles*, moreover, the Court reined in the decision by holding that a manufacturer can announce suggested resale prices and refuse to deal with distributors who do not follow them. *Colgate*, 250 U. S., at 307–308.

In more recent cases the Court, following a common-law approach, has continued to temper, limit, or overrule once strict prohibitions on vertical restraints. In 1977, the Court overturned the *per se* rule for vertical nonprice restraints, adopting the rule of reason in its stead. *GTE Sylvania*, 433 U. S., at 57–59 (overruling *United States* v. *Arnold, Schwinn & Co.*, 388 U. S. 365 (1967)); see also 433 U. S., at 58, n. 29 (noting "that the advantages of vertical restrictions should not be limited to the categories of new entrants and failing firms"). While the Court in a footnote in *GTE Sylvania* suggested that differences between vertical price and nonprice restraints could support different legal treatment, see 433 U. S., at 51, n. 18, the central part of the opinion relied on authorities and arguments that find unequal treatment "difficult to justify," *id.,* at 69–70 (White, J., concurring in judgment).

Continuing in this direction, in two cases in the 1980's the Court defined legal rules to limit the reach of *Dr. Miles* and to accommodate the doctrines enunciated in *GTE Sylvania* and *Colgate*. See *Business Electronics*, *supra,* at 726–728; *Monsanto*, 465 U. S., at 763–764. In *Monsanto*, the Court required that antitrust plaintiffs alleging a §1 price-fixing conspiracy must present evidence tending to exclude the possibility a manufacturer and its distributors acted in an independent manner. *Id.,* at 764. Unlike Justice Brennan's concurrence, which rejected arguments that *Dr. Miles* should be overruled, see 465 U. S., at 769, the Court "decline[d] to reach the question" whether vertical agreements fixing resale prices always should be unlawful because neither party suggested otherwise, *id.,* at 761–762, n. 7. In *Business Electronics* the Court further narrowed the scope of *Dr. Miles*. It held that the *per se* rule applied only to specific agreements over price levels and not to an agreement between a manufacturer and a distributor to terminate a price-cutting distributor. 485 U. S., at 726–727, 735–736.

Most recently, in 1997, after examining the issue of vertical maximum price-fixing agreements in light of commentary and real experience, the Court overruled a 29-year-old precedent treating those agreements as *per se* illegal. *Khan*, 522 U. S., at 22 (overruling *Albrecht* v. *Herald Co.*, 390 U. S. 145 (1968)). It held instead that they should be evaluated under the traditional rule of reason. 522 U. S., at 22. Our continued limiting of the reach of the decision in *Dr. Miles* and our recent treatment of other vertical restraints justify the conclusion that *Dr. Miles* should not be retained.

The *Dr. Miles* rule is also inconsistent with a principled framework, for it makes little economic sense when analyzed with our other cases on vertical restraints. If we were to decide the procompetitive effects of resale price maintenance were insufficient to overrule *Dr. Miles*, then cases such as *Colgate* and *GTE Sylvania* themselves would be called into question. These later decisions, while they may result in less intrabrand competition, can be justified because they permit manufacturers to secure the procompetitive benefits associated with vertical price restraints through other methods. The other methods, however, could be less efficient for a particular manufacturer to establish and sustain. The end result hinders competition and consumer welfare because manufacturers are forced to engage in second-best alternatives and because consumers are required to shoulder the increased expense of the inferior practices.

The manufacturer has a number of legitimate options to achieve benefits similar to those provided by vertical price restraints. A manufacturer can exercise its *Colgate* right to refuse to deal with retailers that do not follow its suggested prices. See 250 U. S., at 307. The economic effects of unilateral and concerted price setting are in general the same. See, *e.g., Monsanto*, 465 U. S., at 762–764. The problem for the manufacturer is that a jury might conclude its unilateral policy was really a vertical agreement, subjecting it to treble damages and potential criminal liability. *Ibid.; Business Electronics*, *supra,* at 728. Even with the stringent standards in *Monsanto* and *Business Electronics*, this danger can lead, and has led, rational manufacturers to take wasteful measures. See, *e.g.,* Brief for PING, Inc., as *Amicus Curiae* 9–18. A manufacturer might refuse to discuss its pricing policy with its distributors except through counsel knowledgeable of the subtle intricacies of the law. Or it might terminate longstanding distributors for minor violations without seeking an explanation. See *ibid*. The increased costs these burdensome measures generate flow to consumers in the form of higher prices.

Furthermore, depending on the type of product it sells, a manufacturer might be able to achieve the procompetitive benefits of resale price maintenance by integrating downstream and selling its products directly to consumers. *Dr. Miles* tilts the relative costs of vertical integration and vertical agreement by making the former more attractive based on the *per se* rule, not on real market conditions. See *Business Electronics*, *supra,* at 725; see generally Coase, The Nature of the Firm, 4 Economica, New Series 386 (1937). This distortion might lead to inefficient integration that would not otherwise take place, so that consumers must again suffer the consequences of the suboptimal distribution strategy. And integration, unlike vertical price restraints, eliminates all intrabrand competition. See, *e.g., GTE Sylvania*, 433 U. S., at 57, n. 26.

There is yet another consideration. A manufacturer can impose territorial restrictions on distributors and allow only one distributor to sell its goods in a given region. Our cases have recognized, and the economics literature confirms, that these vertical nonprice restraints have impacts similar to those of vertical price restraints; both reduce intrabrand competition and can stimulate retailer services. See, *e.g., Business Electronics*, *supra,* at 728; *Monsanto*, *supra,* at 762–763; see also Brief for Economists as *Amici Curiae* 17–18. Cf. Scherer & Ross 560 (noting that vertical nonprice restraints "can engender inefficiencies at least as serious as those imposed upon the consumer by resale price maintenance"); Steiner, How Manufacturers Deal with the Price-Cutting Retailer: When Are Vertical Restraints Efficient?, 65 Antitrust L. J. 407, 446–447 (1997) (indicating that "antitrust law should recognize that the consumer interest is often better served by [resale price maintenance]—contrary to its per se illegality and the rule-of-reason status of vertical nonprice restraints"). The same legal standard (*per se* unlawfulness) applies to horizontal market division and horizontal price fixing because both have similar economic effect. There is likewise little economic justification for the current differential treatment of vertical price and nonprice restraints. Furthermore, vertical nonprice restraints may prove less efficient for inducing desired services, and they reduce intrabrand competition more than vertical price restraints by eliminating both price and service competition. See Brief for Economists as *Amici Curiae* 17–18.

In sum, it is a flawed antitrust doctrine that serves the interests of lawyers—by creating legal distinctions that operate as traps for the unwary—more than the interests of consumers—by requiring manufacturers to choose second-best options to achieve sound business objectives.

B

Respondent's arguments for reaffirming *Dr. Miles* on the basis of *stare decisis* do not require a different result. Respondent looks to congressional action concerning vertical price restraints. In 1937, Congress passed the Miller-Tydings Fair Trade Act, 50 Stat. 693, which made vertical price restraints legal if authorized by a fair trade law enacted by a State. Fifteen years later, Congress expanded the exemption to permit vertical price-setting agreements between a manufacturer and a distributor to be enforced against other distributors not involved in the agreement. McGuire Act, 66 Stat. 632. In 1975, however, Congress repealed both Acts. Consumer Goods Pricing Act, 89 Stat. 801. That the *Dr. Miles* rule applied to vertical price restraints in 1975, according to respondent, shows Congress ratified the rule.

This is not so. The text of the Consumer Goods Pricing Act did not codify the rule of *per se* illegality for vertical price restraints. It rescinded statutory provisions that made them *per se* legal. Congress once again placed these restraints within the ambit of §1 of the Sherman Act.

And, as has been discussed, Congress intended §1 to give courts the ability "to develop governing principles of law" in the common-law tradition. *Texas Industries, Inc.* v. *Radcliff Materials, Inc.*, 451 U. S. 630, 643 (1981); see *Business Electronics*, 485 U. S., at 731 ("The changing content of the term 'restraint of trade' was well recognized at the time the Sherman Act was enacted"). Congress could have set the *Dr. Miles* rule in stone, but it chose a more flexible option. We respect its decision by analyzing vertical price restraints, like all restraints, in conformance with traditional §1 principles, including the principle that our antitrust doctrines "evolv[e] with new circumstances and new wisdom." *Business Electronics, supra,* at 732; see also Easterbrook 139.

The rule of reason, furthermore, is not inconsistent with the Consumer Goods Pricing Act. Unlike the earlier congressional exemption, it does not treat vertical price restraints as *per se* legal. In this respect, the justifications for the prior exemption are illuminating. Its goal "was to allow the States to protect small retail establishments that Congress thought might otherwise be driven from the marketplace by large-volume discounters." *California Retail Liquor Dealers Assn.* v. *Midcal Aluminum, Inc.*, 445 U. S. 97, 102 (1980). The state fair trade laws also appear to have been justified on similar grounds. See Areeda & Hovenkamp 298. The rationales for these provisions are foreign to the Sherman Act. Divorced from competition and consumer welfare, they were designed to save inefficient small retailers from their inability to compete. The purpose of the antitrust laws, by contrast, is "the protection of *competition*, not *competitors*." *Atlantic Richfield Co.* v. *USA Petroleum Co.*, 495 U. S. 328, 338 (1990) (internal quotation marks omitted). To the extent Congress repealed the exemption for some vertical price restraints to end its prior practice of encouraging anticompetitive conduct, the rule of reason promotes the same objective.

Respondent also relies on several congressional appropriations in the mid-1980's in which Congress did not permit the Department of Justice or the Federal Trade Commission to use funds to advocate overturning *Dr. Miles*. See, *e.g.,* 97 Stat. 1071. We need not pause long in addressing this argument. The conditions on funding are no longer in place, see, *e.g.,* Brief for United States as *Amicus Curiae* 21, and they were ambiguous at best. As much as they might show congressional approval for *Dr. Miles*, they might demonstrate a different proposition: that Congress could not pass legislation codifying the rule and reached a short-term compromise instead.

Reliance interests do not require us to reaffirm *Dr. Miles*. To be sure, reliance on a judicial opinion is a significant reason to adhere to it, *Payne* v. *Tennessee*, 501 U. S. 808, 828 (1991), especially "in cases involving property and contract rights," *Khan*, 522 U. S., at 20. The reliance interests here, however, like the reliance interests in *Khan*, cannot justify an inefficient rule, especially because the narrowness of the rule has allowed manufacturers to set minimum resale prices in other ways. And while the *Dr. Miles* rule is longstanding, resale price maintenance was legal under fair trade laws in a majority of States for a large part of the past century up until 1975.

It is also of note that during this time "when the legal environment in the [United States] was most favorable for [resale price maintenance], no more than a tiny fraction of manufacturers ever employed [resale price maintenance] contracts." Overstreet 6; see also *id.,* at 169 (noting that "no more than one percent of manufacturers, accounting for no more than ten percent of consumer goods purchases, ever employed [resale price maintenance] in any single year in the [United States]"); Scherer & Ross 549 (noting that "[t]he fraction of U.S. retail sales covered by [resale price maintenance] in its heyday has been variously estimated at from 4 to 10 percent"). To the extent consumers demand cheap goods, judging vertical price restraints under the rule of reason will not prevent the market from providing them. Cf. Easterbrook 152–153 (noting that "S.S. Kresge (the old K-Mart) flourished during the days of manufacturers' greatest freedom" because "discount stores offer a combination of price and service that many customers value" and that "[n]othing in restricted dealing threatens the ability of consumers to find low prices"); Scherer & Ross 557 (noting that "for the most part, the effects of the [Consumer Goods Pricing Act] were imperceptible because the forces of competition had already repealed the [previous antitrust exemption] in their own quiet way").

For these reasons the Court's decision in *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U. S. 373 (1911), is now overruled. Vertical price restraints are to be judged according to the rule of reason.

V

Noting that Leegin's president has an ownership interest in retail stores that sell Brighton, respondent claims Leegin participated in an unlawful horizontal cartel with competing retailers. Respondent did not make this allegation in the lower courts, and we do not consider it here.

The judgment of the Court of Appeals is reversed, and the case is remanded for proceedings consistent with this opinion.

It is so ordered.

SUPREME COURT OF THE UNITED STATES

No. 06–480

LEEGIN CREATIVE LEATHER PRODUCTS, INC., PETITIONER *v.* PSKS, INC., DBA KAY'S KLOSET . . . KAY'S SHOES

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

[June 28, 2007]

JUSTICE BREYER, with whom JUSTICE STEVENS, JUSTICE SOUTER, and JUSTICE GINSBURG join, dissenting.

In *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U. S. 373, 394, 408–409 (1911), this Court held that an agreement between a manufacturer of proprietary medicines and its dealers to fix the minimum price at which its medicines could be sold was "invalid . . . under the [Sherman Act, 15 U. S. C. §1]." This Court has consistently read *Dr. Miles* as establishing a bright-line rule that agreements fixing minimum resale prices are *per se* illegal. See, *e.g.*, *United States* v. *Trenton Potteries Co.*, 273 U. S. 392, 399–401 (1927); *NYNEX Corp.* v. *Discon, Inc.*, 525 U. S. 128, 133 (1998). That *per se* rule is one upon which the legal profession, business, and the public have relied for close to a century. Today the Court holds that courts must determine the lawfulness of minimum resale price maintenance by applying, not a bright-line *per se* rule, but a circumstance-specific "rule of reason." *Ante*, at 28. And in doing so it overturns *Dr. Miles*.

The Court justifies its departure from ordinary considerations of *stare decisis* by pointing to a set of arguments well known in the antitrust literature for close to half a century. See *ante*, at 10–12. Congress has repeatedly found in these arguments insufficient grounds for overturning the *per se* rule. See, *e.g.*, Hearings on H. R. 10527 et al. before the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce, 85th Cong., 2d Sess., 74–76, 89, 99, 101–102, 192–195, 261–262 (1958). And, in my view, they do not warrant the Court's now overturning so well-established a legal precedent.

I

The Sherman Act seeks to maintain a marketplace free of anticompetitive practices, in particular those enforced by agreement among private firms. The law assumes that such a marketplace, free of private restrictions, will tend to bring about the lower prices, better products, and more efficient production processes that consumers typically desire. In determining the lawfulness of particular practices, courts often apply a "rule of reason." They examine both a practice's likely anticompetitive effects and its beneficial business justifications. See, *e.g.*, *National Collegiate Athletic Assn.* v. *Board of Regents of Univ. of Okla.*, 468 U. S. 85, 109–110, and n. 39 (1984); *National Soc. of Professional Engineers* v. *United States*, 435 U. S. 679, 688–691 (1978); *Board of Trade of Chicago* v. *United States*, 246 U. S. 231, 238 (1918).

Nonetheless, sometimes the likely anticompetitive consequences of a particular practice are so serious and the potential justifications so few (or, *e.g.*, so difficult to prove) that courts have departed from a pure "rule of reason" approach. And sometimes this Court has imposed a rule of *per se* unlawfulness—a rule that instructs courts to find the practice unlawful all (or nearly all) the time. See, *e.g.*, *NYNEX*, *supra*, at 133; *Arizona* v. *Maricopa County Medical Soc.*, 457 U. S. 332, 343–344, and n. 16 (1982); *Continental T. V., Inc.* v. *GTE Sylvania Inc.*, 433 U. S. 36, 50, n. 16 (1977); *United States* v. *Topco Associ-*

ates, Inc., 405 U. S. 596, 609–611 (1972); *United States* v. *Socony-Vacuum Oil Co.*, 310 U. S. 150, 213–214 (1940) (citing and quoting *Trenton Potteries*, *supra*, at 397–398).

The case before us asks which kind of approach the courts should follow where minimum resale price maintenance is at issue. Should they apply a *per se* rule (or a variation) that would make minimum resale price maintenance always (or *almost* always) unlawful? Should they apply a "rule of reason"? Were the Court writing on a blank slate, I would find these questions difficult. But, of course, the Court is not writing on a blank slate, and that fact makes a considerable legal difference.

To best explain why the question would be difficult were we deciding it afresh, I briefly summarize several classical arguments for and against the use of a *per se* rule. The arguments focus on three sets of considerations, those involving: (1) potential anticompetitive effects, (2) potential benefits, and (3) administration. The difficulty arises out of the fact that the different sets of considerations point in different directions. See, *e.g.*, 8 P. Areeda, Antitrust Law ¶¶1628–1633, pp. 330–392 (1st ed. 1989) (hereinafter Areeda); 8 P. Areeda & H. Hovenkamp, Antitrust Law ¶¶1628–1633, pp. 288–339 (2d ed. 2004) (hereinafter Areeda & Hovenkamp); Easterbrook, Vertical Arrangements and the Rule of Reason, 53 Antitrust L. J. 135, 146–152 (1984) (hereinafter Easterbrook); Pitofsky, In Defense of Discounters: The No-Frills Case for a *Per Se* Rule Against Vertical Price Fixing, 71 Geo. L. J. 1487 (1983) (hereinafter Pitofsky); Scherer, The Economics of Vertical Restraints, 52 Antitrust L. J. 687, 706–707 (1983) (hereinafter Scherer); Posner, The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality, 48 U. Chi. L. Rev. 6, 22–26 (1981); Brief for William S. Comanor and Frederic M. Scherer as *Amici Curiae* 7–10.

On the one hand, agreements setting minimum resale prices may have serious anticompetitive consequences. *In* *respect to dealers:* Resale price maintenance agreements, rather like horizontal price agreements, can diminish or eliminate price competition among dealers of a single brand or (if practiced generally by manufacturers) among multibrand dealers. In doing so, they can prevent dealers from offering customers the lower prices that many customers prefer; they can prevent dealers from responding to changes in demand, say falling demand, by cutting prices; they can encourage dealers to substitute service, for price, competition, thereby threatening wastefully to attract too many resources into that portion of the industry; they can inhibit expansion by more efficient dealers whose lower prices might otherwise attract more customers, stifling the development of new, more efficient modes of retailing; and so forth. See, *e.g.*, 8 Areeda & Hovenkamp ¶1632c, at 319–321; Steiner, The Evolution and Applications of Dual-Stage Thinking, 49 The Antitrust Bulletin 877, 899–900 (2004); Comanor, Vertical Price-Fixing, Vertical Market Restrictions, and the New Antitrust Policy, 98 Harv. L. Rev. 983, 990–1000 (1985).

In respect to producers: Resale price maintenance agreements can help to reinforce the competition-inhibiting behavior of firms in concentrated industries. In such industries firms may tacitly collude, *i.e.*, observe each other's pricing behavior, each understanding that price cutting by one firm is likely to trigger price competition by all. See 8 Areeda & Hovenkamp ¶1632d, at 321–323; P. Areeda & L. Kaplow, Antitrust Analysis ¶¶231–233, pp. 276–283 (4th ed. 1988) (hereinafter Areeda & Kaplow). Cf. *United States* v. *Container Corp. of America*, 393 U. S. 333 (1969); Areeda & Kaplow ¶¶247–253, at 327–348. Where that is so, resale price maintenance can make it easier for each producer to identify (by observing retail markets) when a competitor has begun to cut prices. And a producer who cuts wholesale prices *without* lowering the minimum resale price will stand to gain little, if anything, in increased profits, because the dealer will be unable to stimulate increased consumer demand by passing along the producer's price cut to consumers. In either case, resale price maintenance agreements will tend to prevent price competition from "breaking out"; and they will thereby tend to stabilize producer prices. See Pitofsky 1490–1491. Cf., *e.g.*, *Container Corp.*, *supra*, at 336–337.

Those who express concern about the potential anticompetitive effects find empirical support in the behavior of prices before, and then after, Congress in 1975 repealed the Miller-Tydings Fair Trade Act, 50 Stat. 693, and the McGuire Act, 66 Stat. 631. Those Acts had permitted (but not required) individual States to enact "fair trade" laws authorizing minimum resale price maintenance. At the time of repeal minimum resale price maintenance was lawful in 36 States; it was unlawful in 14 States. See Hearings on S. 408 before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 94th Cong., 1st Sess., 173 (1975) (hereinafter Hearings on S. 408) (statement of Thomas E. Kauper, Assistant Attorney General, Antitrust Division). Comparing prices in the former States with prices in the latter States, the Department of Justice argued that minimum resale price maintenance had raised prices by 19% to 27%. See Hearings on H. R. 2384 before the Subcommittee on Monopolies and Commercial Law of the House Committee on the Judiciary, 94th Cong., 1st Sess., 122 (1975) (hereinafter Hearings on H. R. 2384) (statement of Keith I. Clearwaters, Deputy Assistant Attorney General, Antitrust Division).

After repeal, minimum resale price maintenance agreements were unlawful *per se* in every State. The Federal Trade Commission (FTC) staff, after studying numerous price surveys, wrote that collectively the surveys "indicate[d] that [resale price maintenance] in most cases increased the prices of products sold with [resale price maintenance]." Bureau of Economics Staff Report to the

FTC, T. Overstreet, Resale Price Maintenance: Economic Theories and Empirical Evidence, 160 (1983) (hereinafter Overstreet). Most economists today agree that, in the words of a prominent antitrust treatise, "resale price maintenance tends to produce higher consumer prices than would otherwise be the case." 8 Areeda & Hovenkamp ¶1604b, at 40 (finding "[t]he evidence . . . persuasive on this point"). See also Brief for William S. Comanor and Frederic M. Scherer as *Amici Curiae* 4 ("It is uniformly acknowledged that [resale price maintenance] and other vertical restraints lead to higher consumer prices").

On the other hand, those favoring resale price maintenance have long argued that resale price maintenance agreements can provide important consumer benefits. The majority lists two: First, such agreements can facilitate new entry. *Ante*, at 11–12. For example, a newly entering producer wishing to build a product name might be able to convince dealers to help it do so—if, but only if, the producer can assure those dealers that they will later recoup their investment. Without resale price maintenance, late-entering dealers might take advantage of the earlier investment and, through price competition, drive prices down to the point where the early dealers cannot recover what they spent. By assuring the initial dealers that such later price competition will not occur, resale price maintenance can encourage them to carry the new product, thereby helping the new producer succeed. See 8 Areeda & Hovenkamp ¶¶1617a, 1631b, at 193–196, 308. The result might be increased competition at the producer level, *i.e.*, greater *inter*-brand competition, that brings with it net consumer benefits.

Second, without resale price maintenance a producer might find its efforts to sell a product undermined by what resale price maintenance advocates call "free riding." *Ante*, at 10–11. Suppose a producer concludes that it can succeed only if dealers provide certain services, say, product demonstrations, high quality shops, advertising that creates a certain product image, and so forth. Without resale price maintenance, some dealers might take a "free ride" on the investment that others make in providing those services. Such a dealer would save money by not paying for those services and could consequently cut its own price and increase its own sales. Under these circumstances, dealers might prove unwilling to invest in the provision of necessary services. See, *e.g.*, 8 Areeda & Hovenkamp ¶¶1611–1613, 1631c, at 126–165, 309–313; R. Posner, Antitrust Law 172–173 (2d ed. 2001); R. Bork, The Antitrust Paradox 290–291 (1978) (hereinafter Bork); Easterbrook 146–149.

Moreover, where a producer and not a group of dealers seeks a resale price maintenance agreement, there is a special reason to believe some such benefits exist. That is because, other things being equal, producers should want to encourage price competition among their dealers. By doing so they will often increase profits by selling more of their product. See *Sylvania*, 433 U. S., at 56, n. 24; Bork 290. And that is so, even if the producer possesses sufficient market power to earn a super-normal profit. That is to say, other things being equal, the producer will benefit by charging his dealers a competitive (or even a higher-than-competitive) wholesale price while encouraging price competition among them. Hence, if the producer is the moving force, the producer must have some special reason for wanting resale price maintenance; and in the absence of, say, concentrated producer markets (where that special reason might consist of a desire to stabilize wholesale prices), that special reason may well reflect the special circumstances just described: new entry, "free riding," or variations on those themes.

The upshot is, as many economists suggest, sometimes resale price maintenance can prove harmful; sometimes it can bring benefits. See, *e.g.*, Brief for Economists as *Amici*

Curiae 16; 8 Areeda & Hovenkamp ¶¶1631–1632, at 306–328; Pitofsky 1495; Scherer 706–707. But before concluding that courts should consequently apply a rule of reason, I would ask such questions as, how often are harms or benefits likely to occur? How easy is it to separate the beneficial sheep from the antitrust goats?

Economic discussion, such as the studies the Court relies upon, can *help* provide answers to these questions, and in doing so, economics can, and should, inform antitrust law. But antitrust law cannot, and should not, precisely replicate economists' (sometimes conflicting) views. That is because law, unlike economics, is an administrative system the effects of which depend upon the content of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients. And that fact means that courts will often bring their own administrative judgment to bear, sometimes applying rules of *per se* unlawfulness to business practices even when those practices sometimes produce benefits. See, *e.g.*, F.M. Scherer & D. Ross, Industrial Market Structure and Economic Performance 335–339 (3d ed. 1990) (hereinafter Scherer & Ross) (describing some circumstances under which price-fixing agreements could be more beneficial than "unfettered competition," but also noting potential costs of moving from a *per se* ban to a rule of reasonableness assessment of such agreements).

I have already described studies and analyses that suggest (though they cannot prove) that resale price maintenance can cause harms with some regularity—and certainly when dealers are the driving force. But what about benefits? How often, for example, will the benefits to which the Court points occur in practice? I can find no economic consensus on this point. There is a consensus in the literature that "free riding" takes place. But "free riding" often takes place in the economy without any legal effort to stop it. Many visitors to California take free rides on the Pacific Coast Highway. We all benefit freely from ideas, such as that of creating the first supermarket. Dealers often take a "free ride" on investments that others have made in building a product's name and reputation. The question is how often the "free riding" problem is serious enough significantly to deter dealer investment.

To be more specific, one can easily *imagine* a dealer who refuses to provide important presale services, say a detailed explanation of how a product works (or who fails to provide a proper atmosphere in which to sell expensive perfume or alligator billfolds), lest customers use that "free" service (or enjoy the psychological benefit arising when a high-priced retailer stocks a particular brand of billfold or handbag) and then buy from another dealer at a lower price. Sometimes this must happen in reality. But does it happen often? We do, after all, live in an economy where firms, despite *Dr. Miles*' *per se* rule, still sell complex technical equipment (as well as expensive perfume and alligator billfolds) to consumers.

All this is to say that the ultimate question is not whether, but *how much,* "free riding" of this sort takes place. And, after reading the briefs, I must answer that question with an uncertain "sometimes." See, *e.g.*, Brief for William S. Comanor and Frederic M. Scherer as *Amici Curiae* 6–7 (noting "skepticism in the economic literature about how often [free riding] actually occurs"); Scherer & Ross 551–555 (explaining the "severe limitations" of the free-rider justification for resale price maintenance); Pitofsky, Why *Dr. Miles* Was Right, 8 Regulation, No. 1, pp. 27, 29–30 (Jan./Feb. 1984) (similar analysis).

How easily can courts identify instances in which the benefits are likely to outweigh potential harms? My own answer is, *not very easily*. For one thing, it is often difficult to identify *who*—producer or dealer—is the moving force behind any given resale price maintenance agreement. Suppose, for example, several large multibrand retailers all sell resale-price-maintained products. Suppose further that small producers set retail prices because they fear that, otherwise, the large retailers will favor (say, by allocating better shelf-space) the goods of other producers who practice resale price maintenance. Who "initiated" this practice, the retailers hoping for considerable insulation from retail competition, or the producers, who simply seek to deal best with the circumstances they find? For another thing, as I just said, it is difficult to determine just when, and where, the "free riding" problem is serious enough to warrant legal protection.

I recognize that scholars have sought to develop check lists and sets of questions that will help courts separate instances where anticompetitive harms are more likely from instances where only benefits are likely to be found. See, *e.g.*, 8 Areeda & Hovenkamp ¶¶1633c–1633e, at 330–339. See also Brief for William S. Comanor and Frederic M. Scherer as *Amici Curiae* 8–10. But applying these criteria in court is often easier said than done. The Court's invitation to consider the existence of "market power," for example, *ante*, at 18, invites lengthy time-consuming argument among competing experts, as they seek to apply abstract, highly technical, criteria to often ill-defined markets. And resale price maintenance cases, unlike a major merger or monopoly case, are likely to prove numerous and involve only private parties. One cannot fairly expect judges and juries in such cases to apply complex economic criteria without making a considerable number of mistakes, which themselves may impose serious costs. See, *e.g.*, H. Hovenkamp, The Antitrust Enterprise 105 (2005) (litigating a rule of reason case is "one of the most costly procedures in antitrust practice"). See also Bok, Section 7 of the Clayton Act and the Merging of Law and Economics, 74 Harv. L. Rev. 226, 238–247 (1960) (describing lengthy FTC efforts to apply complex criteria in a merger case).

Are there special advantages to a bright-line rule? Without such a rule, it is often unfair, and consequently impractical, for enforcement officials to bring criminal proceedings. And since enforcement resources are limited, that loss may tempt some producers or dealers to enter into agreements that are, on balance, anticompetitive.

Given the uncertainties that surround key items in the overall balance sheet, particularly in respect to the "administrative" questions, I can concede to the majority that the problem is difficult. And, if forced to decide now, at most I might agree that the *per se* rule should be slightly modified to allow an exception for the more easily identifiable and temporary condition of "new entry." See Pitofsky 1495. But I am not now forced to decide this question. The question before us is not what should be the rule, starting from scratch. We here must decide whether to change a clear and simple price-related antitrust rule that the courts have applied for nearly a century.

II

We write, not on a blank slate, but on a slate that begins with *Dr. Miles* and goes on to list a century's worth of similar cases, massive amounts of advice that lawyers have provided their clients, and untold numbers of business decisions those clients have taken in reliance upon that advice. See, *e.g.*, *United States* v. *Bausch & Lomb Optical Co.*, 321 U. S. 707, 721 (1944); *Sylvania*, 433 U. S., at 51, n. 18 ("The *per se* illegality of [vertical] price restrictions has been established firmly for many years . . ."). Indeed a Westlaw search shows that *Dr. Miles* itself has been cited dozens of times in this Court and hundreds of times in lower courts. Those who wish this Court to change so well-established a legal precedent bear a heavy burden of proof. See *Illinois Brick Co.* v. *Illinois*, 431 U. S. 720, 736 (1977) (noting, in declining to overrule an earlier case interpreting §4 of the Clayton Act, that "considerations of *stare decisis* weigh heavily in the area of statutory construction, where Congress is free to change this Court's interpretation of its legislation"). I am not aware of any case in which this Court has overturned so well-established a statutory precedent. Regardless, I do not see how the Court can claim that ordinary criteria for overruling an earlier case have been met. See, *e.g.*, *Planned Parenthood of Southeastern Pa.* v. *Casey*, 505 U. S. 833, 854–855 (1992). See also *Federal Election Comm'n* v. *Wisconsin Right to Life, Inc., ante*, at 19–21 (SCALIA, J., concurring in part and concurring in judgment).

A

I can find no change in circumstances in the past several decades that helps the majority's position. In fact, there has been one important change that argues strongly to the contrary. In 1975, Congress repealed the McGuire and Miller-Tydings Acts. See Consumer Goods Pricing Act of 1975, 89 Stat. 801. And it thereby consciously *extended* *Dr. Miles*' *per se* rule. Indeed, at that time the Department of Justice and the FTC, then urging application of the *per se* rule, discussed virtually every argument presented now to this Court as well as others not here presented. And they explained to Congress why Congress should reject them. See Hearings on S. 408, at 176–177 (statement of Thomas E. Kauper, Assistant Attorney General, Antitrust Division); *id.*, at 170–172 (testimony of Lewis A. Engman, Chairman of the FTC); Hearings on H. R. 2384, at 113–114 (testimony of Keith I. Clearwaters, Deputy Assistant Attorney General, Antitrust Division). Congress fully understood, and consequently intended, that the result of its repeal of McGuire and Miller-Tydings would be to make minimum resale price maintenance *per se* unlawful. See, *e.g.*, S. Rep. No. 94–466, pp. 1–3 (1975) ("Without [the exemptions authorized by the Miller-Tydings and McGuire Acts,] the agreements they authorize would violate the antitrust laws. . . . [R]epeal of the fair trade laws generally will prohibit manufacturers from enforcing resale prices"). See also *Sylvania*, *supra*, at 51, n. 18 ("Congress recently has expressed its approval of a *per se* analysis of vertical price restrictions by repealing those provisions of the Miller-Tydings and McGuire Acts allowing fair-trade pricing at the option of the individual States").

Congress did not prohibit this Court from reconsidering the *per se* rule. But enacting major legislation premised upon the existence of that rule constitutes important public reliance upon that rule. And doing so aware of the relevant arguments constitutes even stronger reliance upon the Court's keeping the rule, at least in the absence of some significant change in respect to those arguments.

Have there been any such changes? There have been a few economic studies, described in some of the briefs, that argue, contrary to the testimony of the Justice Department and FTC to Congress in 1975, that resale price maintenance is not harmful. One study, relying on an analysis of litigated resale price maintenance cases from 1975 to 1982, concludes that resale price maintenance does not ordinarily involve producer or dealer collusion. See Ippolito, Resale Price Maintenance: Empirical Evidence from Litigation, 34 J. Law & Econ. 263, 281–282, 292 (1991). But this study equates the failure of plaintiffs to *allege* collusion with the *absence* of collusion—an equation that overlooks the superfluous nature of allegations of horizontal collusion in a resale price maintenance case and the tacit form that such collusion might take. See H. Hovenkamp, Federal Antitrust Policy §11.3c, p. 464, n. 19 (3d ed. 2005); *supra*, at 4–5.

The other study provides a theoretical basis for concluding that resale price maintenance "need not lead to higher retail prices." Marvel & McCafferty, The Political Economy of Resale Price Maintenance, 94 J. Pol. Econ. 1074, 1075 (1986). But this study develops a theoretical model "under the assumption that [resale price maintenance] is efficiency-enhancing." *Ibid.* Its only empirical support is a 1940 study that the authors acknowledge is much criticized. See *id.*, at 1091. And many other economists take a different view. See Brief for William S. Comanor and Frederic M. Scherer as *Amici Curiae* 4.

Regardless, taken together, these studies at most may offer some mild support for the majority's position. But they cannot constitute a major change in circumstances.

Petitioner and some *amici* have also presented us with newer studies that show that resale price maintenance sometimes brings consumer benefits. Overstreet 119–129 (describing numerous case studies). But the proponents of a *per se* rule have always conceded as much. What is remarkable about the majority's arguments is that *nothing* in this respect *is new*. See *supra*, at 3, 12 (citing articles and congressional testimony going back several decades). The only new feature of these arguments lies in the fact that the most current advocates of overruling *Dr. Miles* have abandoned a host of other not-very-persuasive arguments upon which prior resale price maintenance proponents used to rely. See, *e.g.*, 8 Areeda ¶1631a, at 350–352 (listing "'[t]raditional' justifications" for resale price maintenance).

The one arguable exception consists of the majority's claim that "even absent free riding," resale price maintenance "may be the most efficient way to expand the manufacturer's market share by inducing the retailer's performance and allowing it to use its own initiative and experience in providing valuable services." *Ante*, at 12. I cannot count this as an exception, however, because I do not understand how, in the absence of free-riding (and assuming competitiveness), an established producer would need resale price maintenance. Why, on these assumptions, would a dealer not "expand" its "market share" as best that dealer sees fit, obtaining appropriate payment from consumers in the process? There may be an answer to this question. But I have not seen it. And I do not think that we should place significant weight upon justifications that the parties do not explain with sufficient clarity for a generalist judge to understand.

No one claims that the American economy has changed in ways that might support the majority. Concentration in retailing has increased. See, *e.g.*, Brief for Respondent 18 (since minimum resale price maintenance was banned nationwide in 1975, the total number of retailers has dropped while the growth in sales per store has risen); Brief for American Antitrust Institute as *Amicus Curiae* 17, n. 20 (citing private study reporting that the combined sales of the 10 largest retailers worldwide has grown to nearly 30% of total retail sales of top 250 retailers; also quoting 1999 Organisation for Economic Co-operation and Development report stating that the "'last twenty years have seen momentous changes in retail distribution including significant increases in concentration'"); Mamen, Facing Goliath: Challenging the Impacts of Supermarket Consolidation on our Local Economies, Communities, and Food Security, The Oakland Institute, 1 Policy Brief, No. 3, pp. 1, 2 (Spring 2007), http://www.oaklandinstitute.org/pdfs/facing_goliath.pdf (as visited June 25, 2007, and available in Clerks of Court's case file) (noting that "[f]or many decades, the top five food retail firms in the U. S. controlled less than 20 percent of the market"; from 1997 to 2000, "the top five firms increased their market share from 24 to 42 percent of all retail sales"; and "[b]y 2003, they controlled over half of all grocery sales"). That change, other things being equal, may enable (and motivate) more retailers, accounting for a greater percentage of total retail sales volume, to seek resale price maintenance, thereby making it more difficult for price-cutting competitors (perhaps internet retailers) to obtain market share.

Nor has anyone argued that concentration among manufacturers that might use resale price maintenance has diminished significantly. And as far as I can tell, it has not. Consider household electrical appliances, which a study from the late 1950's suggests constituted a significant portion of those products subject to resale price maintenance at that time. See Hollander, United States of America, in Resale Price Maintenance 67, 80–81 (B. Yamey ed. 1966). Although it is somewhat difficult to compare census data from 2002 with that from several decades ago (because of changes in the classification system), it is clear that at least some subsets of the household electrical appliance industry are *more* concentrated, in terms of manufacturer market power, now than they were then. For instance, the top eight domestic manufacturers of household cooking appliances accounted for 68% of the domestic market (measured by value of shipments) in 1963 (the earliest date for which I was able to find data), compared with 77% in 2002. See Dept. of Commerce, Bureau of Census, 1972 Census of Manufacturers, Special Report Series, Concentration Ratios in Manufacturing, No. MC72(SR)–2, p. SR2–38 (1975) (hereinafter 1972 Census); Dept. of Commerce, Bureau of Census, 2002 Economic Census, Concentration Ratios: 2002, No. EC02–31SR–1, p. 55 (2006) (hereinafter 2002 Census). The top eight domestic manufacturers of household laundry equipment accounted for 95% of the domestic market in 1963 (90% in 1958), compared with 99% in 2002. 1972 Census, at SR2–38; 2002 Census, at 55. And the top eight domestic manufacturers of household refrigerators and freezers accounted for 91% of the domestic market in 1963, compared with 95% in 2002. 1972 Census, at SR2–38; 2002 Census, at 55. Increased concentration among manufacturers increases the likelihood that producer-originated resale price maintenance will prove more prevalent today than in years past, and more harmful. At the very least, the majority has not explained how these, or other changes in the economy could help support its position.

In sum, there is no relevant change. And without some such change, there is no ground for abandoning a well-established antitrust rule.

B

With the preceding discussion in mind, I would consult the list of factors that our case law indicates are relevant when we consider overruling an earlier case. JUSTICE SCALIA, writing separately in another of our cases this Term, well summarizes that law. See *Wisconsin Right to Life, Inc., ante*, at 19–21. (opinion concurring in part and concurring in judgment). And every relevant factor he mentions argues against overruling *Dr. Miles* here.

First, the Court applies *stare decisis* more "rigidly" in statutory than in constitutional cases. See *Glidden Co.* v. *Zdanok*, 370 U. S. 530, 543 (1962); *Illinois Brick Co.*, 431 U. S., at 736. This is a statutory case.

Second, the Court does sometimes overrule cases that it decided wrongly only a reasonably short time ago. As JUSTICE SCALIA put it, "[o]verruling a *constitutional* case decided just a few years earlier is far from unprecedented." *Wisconsin Right to Life, ante*, at 19 (emphasis added). We here overrule one *statutory* case, *Dr. Miles*, decided 100 years ago, and we overrule the cases that reaffirmed its *per se* rule in the intervening years. See, *e.g.*, *Trenton Potteries*, 273 U. S., at 399–401; *Bausch & Lomb*, 321 U. S., at 721; *United States* v. *Parke, Davis & Co.*, 362 U. S. 29, 45–47 (1960); *Simpson* v. *Union Oil Co. of Cal.*, 377 U. S. 13, 16–17 (1964).

Third, the fact that a decision creates an "unworkable" legal regime argues in favor of overruling. See *Payne* v. *Tennessee*, 501 U. S. 808, 827–828 (1991); *Swift & Co.* v. *Wickham*, 382 U. S. 111, 116 (1965). Implementation of the *per se* rule, even with the complications attendant the exception allowed for in *United States* v. *Colgate & Co.*, 250 U. S. 300 (1919), has proved practical over the course of the last century, particularly when compared with the many complexities of litigating a case under the "rule of reason" regime. No one has shown how moving from the *Dr. Miles* regime to "rule of reason" analysis would make the legal regime governing minimum resale price maintenance more "administrable," *Wisconsin Right to Life, ante*, at 20 (opinion of SCALIA, J.), particularly since *Colgate* would remain good law with respect to *unreasonable* price maintenance.

Fourth, the fact that a decision "unsettles" the law may argue in favor of overruling. See *Sylvania*, 433 U. S., at 47; *Wisconsin Right to Life, ante*, at 20–21 (opinion of SCALIA, J.). The *per se* rule is well-settled law, as the Court itself has previously recognized. *Sylvania, supra*, at 51, n. 18. It is the majority's change here that will unsettle the law.

Fifth, the fact that a case involves property rights or contract rights, where reliance interests are involved, argues against overruling. *Payne*, *supra*, at 828. This case involves contract rights and perhaps property rights (consider shopping malls). And there has been considerable reliance upon the *per se* rule. As I have said, Congress relied upon the continued vitality of *Dr. Miles* when it repealed Miller-Tydings and McGuire. *Supra*, at 12–13. The Executive Branch argued for repeal on the assumption that *Dr. Miles* stated the law. *Ibid.* Moreover, whole sectors of the economy have come to rely upon the *per se* rule. A factory outlet store tells us that the rule "form[s] an essential part of the regulatory background against which [that firm] and many other discount retailers have financed, structured, and operated their businesses." Brief for Burlington Coat Factory Warehouse Corp. as *Amicus Curiae* 5. The Consumer Federation of America tells us that large low-price retailers would not exist without *Dr. Miles*; minimum resale price maintenance, "by stabilizing price levels and preventing low-price competition, erects a potentially insurmountable barrier to entry for such low-price innovators." Brief for Consumer Federation of America as *Amicus Curiae* 5, 7–9 (discussing, *inter alia*, comments by Wal-Mart's founder 25 years ago that relaxation of the *per se* ban on minimum resale price maintenance would be a "'great danger'" to Wal-Mart's then-relatively-nascent business). See also Brief for American Antitrust Institute as *Amicus Curiae* 14–15, and sources cited therein (making the same point). New distributors, including internet distributors, have similarly invested time, money, and labor in an effort to bring yet lower cost goods to Americans.

This Court's overruling of the *per se* rule jeopardizes this reliance, and more. What about malls built on the assumption that a discount distributor will remain an anchor tenant? What about home buyers who have taken a home's distance from such a mall into account? What about Americans, producers, distributors, and consumers, who have understandably assumed, at least for the last 30 years, that price competition is a legally guaranteed way of life? The majority denies none of this. It simply says that these "reliance interests . . . , like the reliance interests in *Khan*, cannot justify an inefficient rule." *Ante*, at 27.

The Court minimizes the importance of this reliance, adding that it "is also of note" that at the time resale price maintenance contracts were lawful "'no more than a tiny fraction of manufacturers ever employed'" the practice. *Ibid.* (quoting Overstreet 6). By "tiny" the Court means manufacturers that accounted for up to "'ten percent of consumer goods purchases'" annually. *Ibid.*. That figure in today's economy equals just over $300 billion. See Dept. of Commerce, Bureau of Census, Statistical Abstract of the United States: 2007, p. 649 (126th ed.) (over $3 trillion in U. S. retail sales in 2002). Putting the Court's estimate together with the Justice Department's early 1970's study translates a legal regime that permits all resale price maintenance into retail bills that are higher by an average of roughly $750 to $1000 annually for an American family of four. Just how much higher retail bills will be after the Court's decision today, of course, depends upon what is now unknown, namely how courts will decide future cases under a "rule of reason." But these figures indicate that the amounts involved are important to American families and cannot be dismissed as "tiny."

Sixth, the fact that a rule of law has become "embedded" in our "national culture" argues strongly against overruling. *Dickerson* v. *United States*, 530 U. S. 428, 443–444 (2000). The *per se* rule forbidding minimum resale price maintenance agreements has long been "embedded" in the law of antitrust. It involves price, the economy's "'central nervous system.'" *National Soc. of Professional Engineers*, 435 U. S., at 692 (quoting *Socony-Vacuum Oil*, 310 U. S., at 226, n. 59). It reflects a basic antitrust assumption (that consumers often prefer lower prices to more service). It embodies a basic antitrust objective (providing consumers with a free choice about such matters). And it creates an easily administered and enforceable bright line, "Do not agree about price," that businesses as well as lawyers have long understood.

The only contrary *stare decisis* factor that the majority mentions consists of its claim that this Court has "[f]rom the beginning . . . treated the Sherman Act as a common-law statute," and has previously overruled antitrust precedent. *Ante*, at 20, 21–22. It points in support to *State Oil Co.* v. *Khan*, 522 U. S. 3 (1997), overruling *Albrecht* v. *Herald Co.*, 390 U. S. 145 (1968), in which this Court had held that *maximum* resale price agreements were unlawful *per se*, and to *Sylvania*, overruling *United States* v. *Arnold, Schwinn & Co.*, 388 U. S. 365 (1967), in which this

Court had held that producer-imposed territorial limits were unlawful *per se*.

The Court decided *Khan,* however, 29 years after *Albrecht*—still a significant period, but nowhere close to the century *Dr. Miles* has stood. The Court specifically noted the *lack* of any significant reliance upon *Albrecht*. 522 U. S., at 18–19 (*Albrecht* has had "little or no relevance to ongoing enforcement of the Sherman Act"). *Albrecht* had far less support in traditional antitrust principles than did *Dr. Miles*. Compare, *e.g.*, 8 Areeda & Hovenkamp ¶1632, at 316–328 (analyzing potential harms of minimum resale price maintenance), with *id.,* ¶1637, at 352–361 (analyzing potential harms of maximum resale price maintenance). See also, *e.g.*, Pitofsky 1490, n. 17. And Congress had nowhere expressed support for *Albrecht'*s rule. *Khan, supra,* at 19.

In *Sylvania*, the Court, in overruling *Schwinn*, explicitly distinguished *Dr. Miles* on the ground that while Congress had "recently . . . expressed its approval of a *per se* analysis of vertical price restrictions" by repealing the Miller-Tydings and McGuire Acts, "[n]o similar expression of congressional intent exists for nonprice restrictions." 433 U. S., at 51, n. 18. Moreover, the Court decided *Sylvania* only a decade after *Schwinn*. And it based its overruling on a generally perceived need to avoid "confusion" in the law, 433 U. S., at 47–49, a factor totally absent here.

The Court suggests that it is following "the common-law tradition." *Ante* at 26. But the common law would not have permitted overruling *Dr. Miles* in these circumstances. Common-law courts rarely overruled well-established earlier rules outright. Rather, they would over time issue decisions that gradually eroded the scope and effect of the rule in question, which might eventually lead the courts to put the rule to rest. One can argue that modifying the *per se* rule to make an exception, say, for new entry, see Pitofsky 1495, could prove consistent with this approach. To swallow up a century-old precedent, potentially affecting many billions of dollars of sales, is not. The reader should compare today's "common-law" decision with Justice Cardozo's decision in *Allegheny College* v. *National Chautauqua Cty. Bank of Jamestown*, 246 N. Y. 369, 159 N. E. 173 (1927), and note a gradualism that does not characterize today's decision.

Moreover, a Court that rests its decision upon economists' views of the economic merits should also take account of legal scholars' views about common-law overruling. Professors Hart and Sacks list 12 factors (similar to those I have mentioned) that support judicial "adherence to prior holdings." They all support adherence to *Dr. Miles* here. See H. Hart & A. Sacks, The Legal Process 568–569 (W. Eskridge & P. Frickey eds. 1994). Karl Llewellyn has written that the common-law judge's "conscious reshaping" of prior law "must so move as to hold the degree of movement down to the degree to which need truly presses." The Bramble Bush 156 (1960). Where here is the pressing need? The Court notes that the FTC argues here in favor of a rule of reason. See *ante*, at 20–21. But both Congress and the FTC, unlike courts, are well-equipped to gather empirical evidence outside the context of a single case. As neither has done so, we cannot conclude with confidence that the gains from eliminating the *per se* rule will outweigh the costs.

In sum, every *stare decisis* concern this Court has ever mentioned counsels against overruling here. It is difficult for me to understand how one can believe both that (1) satisfying a set of *stare decisis* concerns justifies overruling a recent constitutional decision, *Wisconsin Right to Life, Inc., ante*, at 19–21 (SCALIA, J., joined by KENNEDY and THOMAS, JJ., concurring in part and concurring in judgment), but (2) failing to satisfy any of those same concerns nonetheless permits overruling a longstanding statutory decision. Either those concerns are relevant or they are not.

* * *

The only safe predictions to make about today's decision are that it will likely raise the price of goods at retail and that it will create considerable legal turbulence as lower courts seek to develop workable principles. I do not believe that the majority has shown new or changed conditions sufficient to warrant overruling a decision of such long standing. All ordinary *stare decisis* considerations indicate the contrary. For these reasons, with respect, I dissent.