Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.

441 U.S. 1 (1979)

MR. JUSTICE WHITE delivered the opinion of the Court: This case involves an action under the antitrust and copyright laws brought by respondent Columbia Broadcasting System, Inc. (CBS), against petitioners, American Society of Composers, Authors and Publishers (ASCAP) and Broadcast Music, Inc. (BMI), and their members and affiliates. The basic question presented is whether the issuance by ASCAP and BMI to CBS of blanket licenses to copyrighted musical compositions at fees negotiated by them is price fixing *per se* unlawful under the antitrust laws.

I

CBS operates one of three national commercial television networks, supplying programs to approximately 200 affiliated stations and telecasting approximately 7,500 network programs per year. Many, but not all, of these programs make use of copyrighted music recorded on the soundtrack. CBS also owns television and radio stations in various cities. It is "'the giant of the world in the use of music rights,'" the "'No. 1 outlet in the history of entertainment.'"[2]

Since 1897, the copyright laws have vested in the owner of a copyrighted musical composition the exclusive right to perform the work publicly for profit, but the legal right is not self-enforcing. In 1914, Victor Herbert and a handful of other composers organized ASCAP because those who performed copyrighted music for profit were so numerous and widespread, and most performances so fleeting, that as a practical matter it was impossible for the many individual copyright owners to negotiate with and license the users and to detect unauthorized uses. "ASCAP was organized as a 'clearing-house' for copyright owners and users to solve these problems" associated with the licensing of music. 400 F.Supp. 737, 741 (S.D.N.Y. 1975). As ASCAP operates today, its 22,000 members grant it nonexclusive rights to license nondramatic performances of their works, and ASCAP issues licenses and distributes royalties to copyright owners in accordance with a schedule reflecting the nature and amount of the use of their music and other factors.

BMI, a nonprofit corporation owned by members of the broadcasting industry, was organized in 1939, is affiliated with or represents some 10,000 publishing companies and 20,000 authors and composers, and operates in much the same manner as ASCAP. Almost every domestic copyrighted composition is in the repertory either of ASCAP, with a total of three million compositions, or of BMI, with one million.

Both organizations operate primarily through blanket licenses, which give the licensees the right to perform any and all of the compositions owned by the members or affiliates as often as the licensees desire for a stated term. Fees for blanket licenses are ordinarily a percentage of total revenues or a flat dollar amount, and do not directly depend on the amount or type of music used. Radio and television broadcasters are the largest users of music, and almost all of them hold blanket licenses from both ASCAP and BMI. Until this litigation, CBS held blanket licenses from both organizations for its television network on a continuous basis since the late 1940's and had never attempted to secure any other form of license from either ASCAP or any of its members.

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[2] 400 F.Supp. 737, 771 (S.D.N.Y.1975), quoting a CBS witness. CBS is also a leading music publisher, with publishing subsidiaries affiliated with both ASCAP and BMI, and is the world's largest manufacturer and seller of records and tapes. Ibid.

The complaint filed by CBS charged various violations of the Sherman Act and the copyright laws.[7] CBS argued that ASCAP and BMI are unlawful monopolies and that the blanket license is illegal price fixing, an unlawful tying arrangement, a concerted refusal to deal, and a misuse of copyrights. The District Court, though denying summary judgment to certain defendants, ruled that the practice did not fall within the *per se* rule. After an 8-week trial, limited to the issue of liability, the court dismissed the complaint, rejecting again the claim that the blanket license was price fixing and a *per se* violation of § 1 of the Sherman Act, and holding that since direct negotiation with individual copyright owners is available and feasible there is no undue restraint of trade, illegal tying, misuse of copyrights, or monopolization.

Though agreeing with the District Court's factfinding and not disturbing its legal conclusions on the other antitrust theories of liability, the Court of Appeals held that the blanket license issued to television networks was a form of price fixing illegal *per se* under the Sherman Act. This conclusion, without more, settled the issue of liability under the Sherman Act, established copyright misuse,[9] and required reversal of the District Court's judgment, as well as a remand to consider the appropriate remedy.

*** Because we disagree with the Court of Appeals' conclusions with respect to the *per se* illegality of the blanket license, we reverse its judgment and remand the cause for further appropriate proceedings.

II

In construing and applying the Sherman Act's ban against contracts, conspiracies, and combinations in restraint of trade, the Court has held that certain agreements or practices are so "plainly anticompetitive," *National Society of Professional Engineers v. United States,* 435 U.S. 679, 692 (1978); *Continental T.V., Inc. v. GTE Sylvania, Inc.,* 433 U.S. 36, 50 (1977), and so often "lack . . . any redeeming virtue," *Northern Pac. R. Co. v. United States,* 356 U.S. 1, 5 (1958), that they are conclusively presumed illegal without further examination under the rule of reason generally applied in Sherman Act cases. This *per se* rule is a valid and useful tool of antitrust policy and enforcement. And agreements among competitors to fix prices on their individual goods or services are among those concerted activities that the Court has held to be within the *per se* category. But easy labels do not always supply ready answers.

A

To the Court of Appeals and CBS, the blanket license involves "price fixing" in the literal sense: the composers and publishing houses have joined together into an organization that sets its price for the blanket license it sells. But this is not a question simply of determining whether two or more potential competitors have literally "fixed" a "price." As generally used in the antitrust field, "price fixing" is a shorthand way of describing certain categories of business behavior to which the *per se* rule has been held applicable. The Court of Appeals' literal approach does not alone establish that this particular practice is one of those types or that it is "plainly anticompetitive" and very likely without "redeeming virtue." Literalness is overly simplistic and often overbroad. When two partners set the price of their goods or services they are literally "price fixing," but they are not *per se* in violation of the Sherman Act. See *United States v. Addyston*

[7] CBS seeks injunctive relief for the antitrust violations and a declaration of copyright misuse.

[9] At CBS's suggestion, the Court of Appeals held that the challenged conduct constituted misuse of copyrights solely on the basis of its finding of unlawful price fixing.

Pipe & Steel Co., 85 F. 271, 280 (CA6 1898), aff'd, 175 U.S. 211 (1899). Thus, it is necessary to characterize the challenged conduct as falling within or without that category of behavior to which we apply the label "*per se* price fixing." That will often, but not always, be a simple matter.

Consequently, as we recognized in *United States v. Topco Associates, Inc.,* 405 U.S. 596, 607-608 (1972), "[i]t is only after considerable experience with certain business relationships that courts classify them as *per se* violations . . . ." We have never examined a practice like this one before. ***

B

This litigation and other cases involving ASCAP and its licensing practices have arisen out of the efforts of the creators of copyrighted musical compositions to collect for the public performance of their works, as they are entitled to do under the Copyright Act. As already indicated, ASCAP and BMI originated to make possible and to facilitate dealings between copyright owners and those who desire to use their music. Both organizations plainly involve concerted action in a large and active line of commerce, and it is not surprising that, as the District Court found, "[n]either ASCAP nor BMI is a stranger to antitrust litigation." 400 F.Supp., at 743.

The Department of Justice first investigated allegations of anticompetitive conduct by ASCAP over 50 years ago. A criminal complaint was filed in 1934, but the Government was granted a midtrial continuance and never returned to the courtroom. In separate complaints in 1941, the United States charged that the blanket license, which was then the only license offered by ASCAP and BMI, was an illegal restraint of trade and that arbitrary prices were being charged as the result of an illegal copyright pool. The Government sought to enjoin ASCAP's exclusive licensing powers and to require a different form of licensing by that organization. The case was settled by a consent decree that imposed tight restrictions on ASCAP's operations. Following complaints relating to the television industry, successful private litigation against ASCAP by movie theaters, and a Government challenge to ASCAP's arrangements with similar foreign organizations, the 1941 decree was reopened and extensively amended in 1950.

Under the amended decree, which still substantially controls the activities of ASCAP, members may grant ASCAP only nonexclusive rights to license their works for public performance. Members, therefore, retain the rights individually to license public performances, along with the rights to license the use of their compositions for other purposes. ASCAP itself is forbidden to grant any license to perform one or more specified compositions in the ASCAP repertory unless both the user and the owner have requested it in writing to do so. ASCAP is required to grant to any user making written application a nonexclusive license to perform all ASCAP compositions either for a period of time or on a per-program basis. ASCAP may not insist on the blanket license, and the fee for the per-program license, which is to be based on the revenues for the program on which ASCAP music is played, must offer the applicant a genuine economic choice between the per-program license and the more common blanket license. If ASCAP and a putative licensee are unable to agree on a fee within 60 days, the applicant may apply to the District Court for a determination of a reasonable fee, with ASCAP having the burden of proving reasonableness.[20]

[20] BMI is in a similar situation. The original decree against BMI is reported as *United States v. BMI,* 1940-1943 Trade Cases ¶ 56,096 (E.D. Wis. 1941). A new consent judgment was entered in 1966 following a monopolization complaint filed in 1964. *United States v. BMI,* 1966 Trade Cases ¶ 71,941 (S.D.N.Y.). ***

The 1950 decree, as amended from time to time, continues in effect, and the blanket license continues to be the primary instrument through which ASCAP conducts its business under the decree. The courts have twice construed the decree not to require ASCAP to issue licenses for selected portions of its repertory.[21]

After the consent decrees, the legality of the blanket license was challenged in suits brought by certain ASCAP members against individual radio stations for copyright infringement. The stations raised as a defense that the blanket license was a form of price fixing illegal under the Sherman Act. The parties stipulated that it would be nearly impossible for each radio station to negotiate with each copyright holder separate licenses for the performance of his works on radio. Against this background, and relying heavily on the 1950 consent judgment, the Court of Appeals for the Ninth Circuit rejected claims that ASCAP was a combination in restraint of trade and that the blanket license constituted illegal price fixing. *K-91, Inc. v. Gershwin Publishing Corp.,* 372 F.2d 1 (1967). *** The Department [of Justice] concluded that, in the circumstances of that case, the blanket licenses issued by ASCAP to individual radio stations were neither a *per se* violation of the Sherman Act nor an unreasonable restraint of trade.

As evidenced by its *amicus* brief in the present case, the Department remains of that view. Furthermore, the United States disagrees with the Court of Appeals in this case and urges that the blanket licenses, which the consent decree authorizes ASCAP to issue to television networks, are not *per se* violations of the Sherman Act. It takes no position, however, on whether the practice is an unreasonable restraint of trade in the context of the network television industry.

Finally, we note that Congress itself, in the new Copyright Act, has chosen to employ the blanket license and similar practices. Congress created a compulsory blanket license for secondary transmissions by cable television systems and provided that "[n]otwithstanding any provisions of the antitrust laws, . . . any claimants may agree among themselves as to the proportionate division of compulsory licensing fees among them, may lump their claims together and file them jointly or as a single claim, or may designate a common agent to receive payment on their behalf." 17 U.S.C. § 111(d)(5)(A). *** Though these provisions are not directly controlling, they do reflect an opinion that the blanket license, and ASCAP, are economically beneficial in at least some circumstances.

*** [T]here is no nearly universal view that either the blanket or the per-program licenses issued by ASCAP at prices negotiated by it are a form of price fixing subject to automatic condemnation under the Sherman Act, rather than to a careful assessment under the rule of reason.

III

*** A

As a preliminary matter, we are mindful that the Court of Appeals' holding would appear to be quite difficult to contain. If, as the court held, there is a *per se* antitrust violation whenever ASCAP issues a blanket license to a television network for a single fee, why would it not also be automatically illegal for ASCAP to negotiate and issue blanket licenses to individual radio or television stations or to other users who perform copyrighted music for profit? Likewise, if the present network licenses issued through ASCAP on behalf of its members are *per se* violations,

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[21] *United States v. ASCAP (Application of Shenandoah Valley Broadcasting, Inc.)*, 208 F.Supp. 896 (S.D.N.Y. 1962), aff'd, 331 F.2d 117 (CA2 1964); *United States v. ASCAP (Application of National Broadcasting Co.)*, 1971 Trade Cases ¶ 73,491 (S.D.N.Y. 1970).

why would it not be equally illegal for the members to authorize ASCAP to issue licenses establishing various categories of uses that a network might have for copyrighted music and setting a standard fee for each described use?

Although the Court of Appeals apparently thought the blanket license could be saved in some or even many applications, it seems to us that the *per se* rule does not accommodate itself to such flexibility and that the observations of the Court of Appeals with respect to remedy tend to impeach the *per se* basis for the holding of liability.

CBS would prefer that ASCAP be authorized, indeed directed, to make all its compositions available at standard per-use rates within negotiated categories of use. But if this in itself or in conjunction with blanket licensing constitutes illegal price fixing by copyright owners, CBS urges that an injunction issue forbidding ASCAP to issue any blanket license or to negotiate any fee except on behalf of an individual member for the use of his own copyrighted work or works. Thus, we are called upon to determine that blanket licensing is unlawful across the board. We are quite sure, however, that the *per se* rule does not require any such holding.

B

In the first place, the line of commerce allegedly being restrained, the performing rights to copyrighted music, exists at all only because of the copyright laws. Those who would use copyrighted music in public performances must secure consent from the copyright owner or be liable at least for the statutory damages for each infringement and, if the conduct is willful and for the purpose of financial gain, to criminal penalties. Furthermore, nothing in the Copyright Act of 1976 indicates in the slightest that Congress intended to weaken the rights of copyright owners to control the public performance of musical compositions. Quite the contrary is true. Although the copyright laws confer no rights on copyright owners to fix prices among themselves or otherwise to violate the antitrust laws, we would not expect that any market arrangements reasonably necessary to effectuate the rights that are granted would be deemed a *per se* violation of the Sherman Act. Otherwise, the commerce anticipated by the Copyright Act and protected against restraint by the Sherman Act would not exist at all or would exist only as a pale reminder of what Congress envisioned.[32]

C

More generally, in characterizing this conduct under the *per se* rule, our inquiry must focus on whether the effect and, here because it tends to show effect, see *United States v. United States Gypsum Co.*, 438 U.S. 422, 436 n. 13 (1978), the purpose of the practice are to threaten the proper operation of our predominantly free-market economy—that is, whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output, and in what portion of the market, or instead one designed to "increase economic efficiency and render markets more, rather than less, competitive." *Id.* at 441 n. 16.

The blanket license, as we see it, is not a "naked restrain[t] of trade with no purpose except stifling of competition," *White Motor Co. v. United States*, 372 U.S. 253, 263 (1963), but rather

[32] Because a musical composition can be "consumed" by many different people at the same time and without the creator's knowledge, the "owner" has no real way to demand reimbursement for the use of his property except through the copyright laws *and* an effective way to enforce those legal rights. See *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 162 (1975). It takes an organization of rather large size to monitor most or all uses and to deal with users on behalf of the composers. Moreover, it is inefficient to have too many such organizations duplicating each other's monitoring of use.

accompanies the integration of sales, monitoring, and enforcement against unauthorized copyright use. As we have already indicated, ASCAP and the blanket license developed together out of the practical situation in the marketplace: thousands of users, thousands of copyright owners, and millions of compositions. Most users want unplanned, rapid, and indemnified access to any and all of the repertory of compositions, and the owners want a reliable method of collecting for the use of their copyrights. Individual sales transactions in this industry are quite expensive, as would be individual monitoring and enforcement, especially in light of the resources of single composers. Indeed, as both the Court of Appeals and CBS recognize, the costs are prohibitive for licenses with individual radio stations, nightclubs, and restaurants, and it was in that milieu that the blanket license arose.

A middleman with a blanket license was an obvious necessity if the thousands of individual negotiations, a virtual impossibility, were to be avoided. Also, individual fees for the use of individual compositions would presuppose an intricate schedule of fees and uses, as well as a difficult and expensive reporting problem for the user and policing task for the copyright owner. Historically, the market for public-performance rights organized itself largely around the single-fee blanket license, which gave unlimited access to the repertory and reliable protection against infringement. When ASCAP's major and user-created competitor, BMI, came on the scene, it also turned to the blanket license.

With the advent of radio and television networks, market conditions changed, and the necessity for and advantages of a blanket license for those users may be far less obvious than is the case when the potential users are individual television or radio stations, or the thousands of other individuals and organizations performing copyrighted compositions in public.[34] But even for television network licenses, ASCAP reduces costs absolutely by creating a blanket license that is sold only a few, instead of thousands,[35] of times, and that obviates the need for closely monitoring the networks to see that they do not use more than they pay for.[36] ASCAP also provides the necessary resources for blanket sales and enforcement, resources unavailable to the vast majority of composers and publishing houses. Moreover, a bulk license of some type is a necessary consequence of the integration necessary to achieve these efficiencies, and a necessary consequence of an aggregate license is that its price must be established.

D

This substantial lowering of costs, which is of course potentially beneficial to both sellers and buyers, differentiates the blanket license from individual use licenses. The blanket license is composed of the individual compositions plus the aggregating service. Here, the whole is truly greater than the sum of its parts; it is, to some extent, a different product. The blanket license has certain unique characteristics: It allows the licensee immediate use of covered compositions, without the delay of prior individual negotiations and great flexibility in the choice of musical material. Many consumers clearly prefer the characteristics and cost advantages of this marketable package, and even small-performing rights societies that have occasionally arisen to compete with ASCAP and BMI have offered blanket licenses. Thus, to the extent the blanket license is a different product, ASCAP is not really a joint sales agency offering the individual goods of

[34] And of course changes brought about by new technology or new marketing techniques might also undercut the justification for the practice.

[35] The District Court found that CBS would require between 4,000 and 8,000 individual license transactions per year.

[36] To operate its system for distributing the license revenues to its members, ASCAP relies primarily on the networks' records of which compositions are used.

many sellers, but is a separate seller offering its blanket license, of which the individual compositions are raw material.[40] ASCAP, in short, made a market in which individual composers are inherently unable to compete fully effectively.

E

Finally, we have some doubt—enough to counsel against application of the *per se* rule—about the extent to which this practice threatens the "central nervous system of the economy," *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 226 n. 59 (1940), that is, competitive pricing as the free market's means of allocating resources. Not all arrangements among actual or potential competitors that have an impact on price are *per se* violations of the Sherman Act or even unreasonable restraints. Mergers among competitors eliminate competition, including price competition, but they are not *per se* illegal, and many of them withstand attack under any existing antitrust standard. Joint ventures and other cooperative arrangements are also not usually unlawful, at least not as price-fixing schemes, where the agreement on price is necessary to market the product at all.

Here, the blanket-license fee is not set by competition among individual copyright owners, and it is a fee for the use of any of the compositions covered by the license. But the blanket license cannot be wholly equated with a simple horizontal arrangement among competitors. ASCAP does set the price for its blanket license, but that license is quite different from anything any individual owner could issue. The individual composers and authors have neither agreed not to sell individually in any other market nor use the blanket license to mask price fixing in such other markets. Moreover, the substantial restraints placed on ASCAP and its members by the consent decree must not be ignored. The District Court found that there was no legal, practical, or conspiratorial impediment to CBS's obtaining individual licenses; CBS, in short, had a real choice.

With this background in mind, which plainly enough indicates that over the years, and in the face of available alternatives, the blanket license has provided an acceptable mechanism for at least a large part of the market for the performing rights to copyrighted musical compositions, we cannot agree that it should automatically be declared illegal in all of its many manifestations. Rather, when attacked, it should be subjected to a more discriminating examination under the rule of reason. It may not ultimately survive that attack, but that is not the issue before us today.

IV

*** We reverse that judgment, and the copyright misuse judgment dependent upon it, and remand for further proceedings to consider any unresolved issues that CBS may have properly brought to the Court of Appeals.[48] Of course, this will include an assessment under the rule of reason of the blanket license as employed in the television industry, if that issue was preserved by CBS in the Court of Appeals. ***

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[40] Moreover, because of the nature of the product—a composition can be simultaneously "consumed" by many users—composers have numerous markets and numerous incentives to produce, so the blanket license is unlikely to cause decreased output, one of the normal undesirable effects of a cartel. And since popular songs get an increased share of ASCAP's revenue distributions, composers compete even within the blanket license in terms of productivity and consumer satisfaction.

[48] It is argued that the judgment of the Court of Appeals should nevertheless be affirmed on the ground that the blanket license is a tying arrangement in violation of § 1 of the Sherman Act or on the ground that ASCAP and BMI have monopolized the relevant market contrary to § 2. The District Court and the Court of Appeals rejected both submissions, and we do not disturb the latter's judgment in these respects, particularly since CBS did not file its own petition for certiorari challenging the Court of Appeals' failure to sustain its tying and monopolization claims.

STEVENS, J., dissenting. The Court holds that ASCAP's blanket license is not a species of price-fixing categorically forbidden by the Sherman Act. I agree with that holding. The Court remands the case to the Court of Appeals, leaving open the question whether the blanket license as employed by ASCAP and BMI is unlawful under a rule of reason inquiry. I think that question is properly before us now and should be answered affirmatively. . . .

. . . It is the refusal to license anything less than the entire repertoire—rather than the decision to offer blanket licenses themselves—that raises the serious antitrust questions in this case. . . .

The market for music at issue here is wholly dominated by ASCAP-issued blanket licenses. Virtually every domestic copyrighted composition is in the repertoire of either ASCAP or BMI. And again, virtually without exception, the only means that has been used to secure authority to perform such compositions is the blanket license.

The blanket all-or-nothing license is patently discriminatory. The user purchases full access to ASCAP's entire repertoire, even though his needs could be satisfied by a far more limited selection. The price he pays for this access is unrelated either to the quantity or the quality of the music he actually uses, or, indeed to what he would probably use in a competitive system. Rather, in this unique all-or-nothing system, the price is based on a percentage of the user's advertising revenues, a measure that reflects the customer's ability to pay but is totally unrelated to factors—such as the cost, quality, or quantity of the product—that normally affect price in a competitive market. The ASCAP system requires users to buy more music than they want at a price which, while not beyond their ability to pay and perhaps not even beyond what is "reasonable" for the access they are getting, may well be far higher than what they would choose to spend for music in a competitive system. It is a classic example of economic discrimination.

The record plainly establishes that there is no price competition between separate musical compositions. Under a blanket license, it is no more expensive for a network to play the most popular current hit in prime time than it is to use an unknown composition as background music in a soap opera. Because the cost to the user is unaffected by the amount used on any program or on all programs, the user has no incentive to economize by, for example, substituting what would otherwise be less expensive songs for established favorites or by reducing the quantity of music used on a program. The blanket license thereby tends to encourage the use of more music, and also of a larger share of what is really more valuable music, than would be expected in a competitive system characterized by separate licenses. And since revenues are passed on to composers on a basis reflecting the character and frequency of the use of their music, the tendency is to increase the rewards of the established composers at the expense of those less well known. Perhaps the prospect is in any event unlikely, but the blanket license does not present a new songwriter with any opportunity to try to break into the market by offering his product for sale at an unusually low price. The absence of that opportunity, however unlikely it may be, is characteristic of a cartelized rather than a competitive market.

The current state of the market cannot be explained on the ground that it could not operate competitively, or that issuance of more limited—and thus less restrictive—licenses by ASCAP is not feasible. The District Court's findings disclose no reason why music performing rights could not be negotiated on a per-composition or per-use basis, either with the composer or publisher directly or with an agent such as ASCAP. In fact, ASCAP now compensates composers and publishers on precisely those bases. If distributions of royalties can be calculated on a per-use and per-composition basis, it is difficult to see why royalties could not also be collected in the same way. Moreover, the record also shows that where ASCAP's blanket license scheme does not govern, competitive markets do. A competitive market for "synch rights" exists,23 and after the use of blanket licenses in the motion picture industry was discontinued, such a market promptly developed in that industry. In sum, the record demonstrates that the market at issue here is one that could be highly competitive, but is not competitive at all.

Since the record describes a market that could be competitive and is not, and since that market is dominated by two firms engaged in a single, blanket method of dealing, it surely seems logical to conclude that trade has been restrained unreasonably. ASCAP argues, however, that at least as to CBS, there has been no restraint at all since the network is free to deal directly with copyright holders. . . .

. . . Despite its size, CBS itself may not obtain music on a competitive basis without incurring unprecedented costs and risks. The fear of unpredictable consequences, coupled with the certain and predictable costs and delays associated with a change in its method of purchasing music, unquestionably inhibits any CBS management decision to embark on a competitive crusade. Even if ASCAP offered CBS a special bargain to forestall any such crusade, that special arrangement would not cure the marketwide restraint. . . .

Antitrust policy requires that great aggregations of economic power be closely scrutinized. That duty is especially important when the aggregation is composed of statutory monopoly privileges. Our cases have repeatedly stressed the need to limit the privileges conferred by patent and copyright strictly to the scope of the statutory grant. The record in this case plainly discloses that the limits have been exceeded and that ASCAP and BMI exercise monopoly powers that far exceed the sum of the privileges of the individual copyright holders. Indeed, ASCAP itself argues that its blanket license constitutes a product that is significantly different from the sum of its component parts. I agree with that premise, but I conclude that the aggregate is a monopolistic restraint of trade proscribed by the Sherman Act.

American Needle, Inc. v. National Football League

560 U.S. 183 (2010)

JUSTICE STEVENS delivered the opinion of the Court: "Every contract, combination in the form of a trust or otherwise, or, conspiracy, in restraint of trade" is made illegal by § 1 of the Sherman Act, ch. 647, 26 Stat. 209, as amended, 15 U.S.C. § 1. The question whether an arrangement is a contract, combination, or conspiracy is different from and antecedent to the question whether it unreasonably restrains trade. This case raises that antecedent question about the business of the 32 teams in the National Football League (NFL) and a corporate entity that they formed to manage their intellectual property. We conclude that the NFL's licensing activities constitute concerted action that is not categorically beyond the coverage of § 1. The legality of that concerted action must be judged under the Rule of Reason.

I

Originally organized in 1920, the NFL is an unincorporated association that now includes 32 separately owned professional football teams. Each team has its own name, colors, and logo, and owns related intellectual property. Like each of the other teams in the league, the New Orleans Saints and the Indianapolis Colts, for example, have their own distinctive names, colors, and marks that are well known to millions of sports fans.

Prior to 1963, the teams made their own arrangements for licensing their intellectual property and marketing trademarked items such as caps and jerseys. In 1963, the teams formed National

Football League Properties (NFLP) to develop, license, and market their intellectual property. Most, but not all, of the substantial revenues generated by NFLP have either been given to charity or shared equally among the teams. However, the teams are able to and have at times sought to withdraw from this arrangement.

Between 1963 and 2000, NFLP granted nonexclusive licenses to a number of vendors, permitting them to manufacture and sell apparel bearing team insignias. Petitioner, American Needle, Inc., was one of those licensees. In December 2000, the teams voted to authorize NFLP to grant exclusive licenses, and NFLP granted Reebok International Ltd. an exclusive 10-year license to manufacture and sell trademarked headwear for all 32 teams. It thereafter declined to renew American Needle's nonexclusive license.

American Needle filed this action in the Northern District of Illinois, alleging that the agreements between the NFL, its teams, NFLP, and Reebok violated §§ 1 and 2 of the Sherman Act. In their answer to the complaint, the defendants averred that the teams, NFL, and NFLP were incapable of conspiring within the meaning of § 1 "because they are a single economic enterprise, at least with respect to the conduct challenged." App. 99. After limited discovery, the District Court granted summary judgment on the question "whether, with regard to the facet of their operations respecting exploitation of intellectual property rights, the NFL and its 32 teams are, in the jargon of antitrust law, acting as a single entity." *American Needle, Inc. v. New Orleans La. Saints*, 496 F.Supp.2d 941, 943 (2007). The court concluded "that in that facet of their operations they have so integrated their operations that they should be deemed a single entity rather than joint ventures cooperating for a common purpose." *Ibid.* The Court of Appeals for the Seventh Circuit affirmed. ***

II

As the case comes to us, we have only a narrow issue to decide: whether the NFL respondents are capable of engaging in a "contract, combination . . ., or conspiracy" as defined by § 1 of the Sherman Act, 15 U.S.C. § 1, or, as we have sometimes phrased it, whether the alleged activity by the NFL respondents "must be viewed as that of a single enterprise for purposes of § 1." *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 771 (1984).

Taken literally, the applicability of § 1 to "every contract, combination . . . or conspiracy" could be understood to cover every conceivable agreement, whether it be a group of competing firms fixing prices or a single firm's chief executive telling her subordinate how to price their company's product. But even though, "read literally," § 1 would address "the entire body of private contract," that is not what the statute means. *National Soc. of Professional Engineers v. United States*, 435 U.S. 679, 688 (1978). Not every instance of cooperation between two people is a potential "contract, combination. . ., or conspiracy, in restraint of trade." 15 U.S.C. § 1.

The meaning of the term "contract, combination . . . or conspiracy" is informed by the "'basic distinction'" in the Sherman Act "'between concerted and independent action'" that distinguishes § 1 of the Sherman Act from § 2. *Copperweld*, 467 U.S., at 767, (quoting *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 761 (1984)). Section 1 applies only to concerted action that restrains trade. Section 2, by contrast, covers both concerted and independent action, but only if that action "monopolize[s]," 15 U.S.C. § 2, or "threatens actual monopolization," *Copperweld*, 467 U.S., at 767, a category that is narrower than restraint of trade. Monopoly power may be equally harmful whether it is the product of joint action or individual action.

Congress used this distinction between concerted and independent action to deter anticompetitive conduct and compensate its victims, without chilling vigorous competition through ordinary business operations. The distinction also avoids judicial scrutiny of routine, internal business decisions.

Thus, in § 1 Congress "treated concerted behavior more strictly than unilateral behavior." *Id.*, at 768. This is so because unlike independent action, "[c]oncerted activity inherently is fraught with anticompetitive risk" insofar as it "deprives the marketplace of independent centers of decisionmaking that competition assumes and demands." *Id.*, at 768-769. And because concerted action is discrete and distinct, a limit on such activity leaves untouched a vast amount of business conduct. As a result, there is less risk of deterring a firm's necessary conduct; courts need only examine discrete agreements; and such conduct may be remedied simply through prohibition. Concerted activity is thus "judged more sternly than unilateral activity under § 2," *Copperweld*, 467 U.S., at 768. For these reasons, § 1 prohibits any concerted action "in restraint of trade or commerce," even if the action does not "threate[n] monopolization," *Ibid.* And therefore, an arrangement must embody concerted action in order to be a "contract, combination . . . or conspiracy" under § 1.

III

We have long held that concerted action under § 1 does not turn simply on whether the parties involved are legally distinct entities. Instead, we have eschewed such formalistic distinctions in favor of a functional consideration of how the parties involved in the alleged anticompetitive conduct actually operate.

As a result, we have repeatedly found instances in which members of a legally single entity violated § 1 when the entity was controlled by a group of competitors and served, in essence, as a vehicle for ongoing concerted activity. In *United States v. Sealy, Inc.*, 388 U.S. 350 (1967), for example, a group of mattress manufacturers operated and controlled Sealy, Inc., a company that licensed the Sealy trademark to the manufacturers, and dictated that each operate within a specific geographic area. The Government alleged that the licensees and Sealy were conspiring in violation of § 1, and we agreed. We explained that "[w]e seek the central substance of the situation" and therefore "we are moved by the identity of the persons who act, rather than the label of their hats." *Id.*, at 353. We thus held that Sealy was not a "separate entity, but . . . an instrumentality of the individual manufacturers." *Id.*, at 356. *** We have similarly looked past the form of a legally "single entity" when competitors were part of professional organizations or trade groups.

Conversely, there is not necessarily concerted action simply because more than one legally distinct entity is involved. Although, under a now-defunct doctrine known as the "intraenterprise conspiracy doctrine," we once treated cooperation between legally separate entities as necessarily covered by § 1, we now embark on a more functional analysis. *** We finally reexamined the intraenterprise conspiracy doctrine in *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984), and concluded that it was inconsistent with the "'basic distinction between concerted and independent action.'" *Id.*, at 767. Considering it "perfectly plain that an internal agreement to implement a single, unitary firm's policies does not raise the antitrust dangers that § 1 was designed to police," *id.*, at 769, we held that a parent corporation and its wholly owned subsidiary "are incapable of conspiring with each other for purposes of § 1 of the Sherman Act," *id.*, at 777. We explained that although a parent corporation and its wholly owned subsidiary are "separate" for the purposes of incorporation or formal title, they are controlled by a single center of decisionmaking and they control a single aggregation of economic power. Joint conduct by two such entities does not "depriv[e] the marketplace of independent centers of decisionmaking," *id.*, at 769, and as a result, an agreement between them does not constitute a "contract, combination . . . or conspiracy" for the purposes of § 1.

IV

As *Copperweld* exemplifies, "substance, not form, should determine whether a[n] . . . entity is capable of conspiring under § 1." 467 U.S., at 773, n. 21. This inquiry is sometimes described as asking whether the alleged conspirators are a single entity. That is perhaps a misdescription, however, because the question is not whether the defendant is a legally single entity or has a single name; nor is the question whether the parties involved "seem" like one firm or multiple firms in any metaphysical sense. The key is whether the alleged "contract, combination . . ., or conspiracy" is concerted action—that is, whether it joins together separate decisionmakers. The relevant inquiry, therefore, is whether there is a "contract, combination . . . or conspiracy" amongst "separate economic actors pursuing separate economic interests," *id.*, at 769, such that the agreement "deprives the marketplace of independent centers of decisionmaking," *ibid.*, and therefore of "diversity of entrepreneurial interests," *Fraser v. Major League Soccer, L.L.C.*, 284 F.3d 47, 57 (C.A.1 2002) (Boudin, C.J.), and thus of actual or potential competition, see *Freeman v. San Diego Assn. of Realtors*, 322 F.3d 1133, 1148-1149 (C.A.9 2003) (Kozinski, J.); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 214-215 (C.A.D.C. 1986) (Bork, J.).

Thus, while the president and a vice president of a firm could (and regularly do) act in combination, their joint action generally is not the sort of "combination" that § 1 is intended to cover. Such agreements might be described as "really unilateral behavior flowing from decisions of a single enterprise." *Copperweld*, 467 U.S., at 767. Nor, for this reason, does § 1 cover "internally coordinated conduct of a corporation and one of its unincorporated divisions," *id.*, at 770, because "[a] division within a corporate structure pursues the common interests of the whole," ibid., and therefore "coordination between a corporation and its division does not represent a sudden joining of two independent sources of economic power previously pursuing separate interests," *id.*, at 770-771. Nor, for the same reasons, is "the coordinated activity of a parent and its wholly owned subsidiary" covered. See *id.*, at 771. They "have a complete unity of interest" and thus "[w]ith or without a formal 'agreement,' the subsidiary acts for the benefit of the parent, its sole shareholder." *Ibid.*

Because the inquiry is one of competitive reality, it is not determinative that two parties to an alleged § 1 violation are legally distinct entities. Nor, however, is it determinative that two legally distinct entities have organized themselves under a single umbrella or into a structured joint venture. The question is whether the agreement joins together "independent centers of decisionmaking." *Id.*, at 769. If it does, the entities are capable of conspiring under § 1, and the court must decide whether the restraint of trade is an unreasonable and therefore illegal one.

V

The NFL teams do not possess either the unitary decisionmaking quality or the single aggregation of economic power characteristic of independent action. Each of the teams is a substantial, independently owned, and independently managed business. "[T]heir general corporate actions are guided or determined" by "separate corporate consciousnesses," and "[t]heir objectives are" not "common." *Copperweld*, 467 U.S., at 771. The teams compete with one another, not only on the playing field, but to attract fans, for gate receipts and for contracts with managerial and playing personnel.

Directly relevant to this case, the teams compete in the market for intellectual property. To a firm making hats, the Saints and the Colts are two potentially competing suppliers of valuable trademarks. When each NFL team licenses its intellectual property, it is not pursuing the "common interests of the whole" league but is instead pursuing interests of each "corporation itself," *Copperweld*, 467 U.S., at 770; teams are acting as "separate economic actors pursuing separate economic interests," and each team therefore is a potential "independent cente[r] of decisionmaking," *id.*, at 769. Decisions by NFL teams to license their separately owned trademarks collectively and to only one vendor are decisions that "depriv[e] the marketplace of independent centers of decisionmaking," *ibid.*, and therefore of actual or potential competition.

In defense, respondents argue that by forming NFLP, they have formed a single entity, akin to a merger, and market their NFL brands through a single outlet. But it is not dispositive that the teams have organized and own a legally separate entity that centralizes the management of their intellectual property. An ongoing § 1 violation cannot evade § 1 scrutiny simply by giving the ongoing violation a name and label. "Perhaps every agreement and combination in restraint of trade could be so labeled." *Timken Roller Bearing Co. v. United States*, 341 U.S. 593, 598 (1951).

The NFL respondents may be similar in some sense to a single enterprise that owns several pieces of intellectual property and licenses them jointly, but they are not similar in the relevant functional sense. Although NFL teams have common interests such as promoting the NFL brand, they are still separate, profit-maximizing entities, and their interests in licensing team trademarks are not necessarily aligned. ***

It may be, as respondents argue, that NFLP "has served as the 'single driver" of the teams' "promotional vehicle," "'pursu[ing] the common interests of the whole.'" Brief for NFL Respondents 28 (quoting *Copperweld*, 467 U.S., at 770-771; brackets in original). But illegal restraints often are in the common interests of the parties to the restraint, at the expense of those who are not parties. It is true, as respondents describe, that they have for some time marketed their trademarks jointly. But a history of concerted activity does not immunize conduct from § 1 scrutiny. "Absence of actual competition may simply be a manifestation of the anticompetitive agreement itself." *Freeman*, 322 F.3d, at 1149.

Respondents argue that nonetheless, as the Court of Appeals held, they constitute a single entity because without their cooperation, there would be no NFL football. It is true that "the clubs that make up a professional sports league are not completely independent economic competitors, as they depend upon a degree of cooperation for economic survival." *Brown*, 518 U.S., at 248. But the Court of Appeals' reasoning is unpersuasive.

The justification for cooperation is not relevant to whether that cooperation is concerted or independent action. A "contract, combination . . . or conspiracy," § 1, that is necessary or useful to a joint venture is still a "contract, combination . . . or conspiracy" if it "deprives the marketplace of independent centers of decisionmaking," *Copperweld*, 467 U.S., at 769. Any joint venture involves multiple sources of economic power cooperating to produce a product. And for many such ventures, the participation of others is necessary. But that does not mean that necessity of cooperation transforms concerted action into independent action; a nut and a bolt can only operate together, but an agreement between nut and bolt manufacturers is still subject to § 1 analysis. Nor does it mean that once a group of firms agree to produce a joint product, cooperation amongst those firms must be treated as independent conduct. The mere fact that the teams operate jointly in some sense does not mean that they are immune.

The question whether NFLP decisions can constitute concerted activity covered by § 1 is closer than whether decisions made directly by the 32 teams are covered by § 1. This is so both because NFLP is a separate corporation with its own management and because the record indicates that most of the revenues generated by NFLP are shared by the teams on an equal basis. Nevertheless we think it clear that for the same reasons the 32 teams' conduct is covered by § 1, NFLP's actions also are subject to § 1, at least with regards to its marketing of property owned by the separate teams. NFLP's licensing decisions are made by the 32 potential competitors, and each of them actually owns its share of the jointly managed assets. Apart from their agreement to cooperate in exploiting those assets, including their decisions as the NFLP, there would be nothing to prevent each of the teams from making its own market decisions relating to purchases of apparel and headwear, to the sale of such items, and to the granting of licenses to use its trademarks.

We generally treat agreements within a single firm as independent action on the presumption that the components of the firm will act to maximize the firm's profits. But in rare cases, that presumption does not hold. Agreements made within a firm can constitute concerted action covered by § 1 when the parties to the agreement act on interests separate from those of the firm itself, and the intrafirm agreements may simply be a formalistic shell for ongoing concerted action. See, *e.g.*, *Topco Associates, Inc.*, 405 U.S., at 609; *Sealy*, 388 U.S., at 352-354.

For that reason, decisions by the NFLP regarding the teams' separately owned intellectual property constitute concerted action. Thirty-two teams operating independently through the vehicle of the NFLP are not like the components of a single firm that act to maximize the firm's profits. The teams remain separately controlled, potential competitors with economic interests that are distinct from NFLP's financial well-being. Unlike typical decisions by corporate shareholders, NFLP licensing decisions effectively require the assent of more than a mere majority of shareholders. And each team's decision reflects not only an interest in NFLP's profits but also an interest in the team's individual profits. The 32 teams capture individual economic benefits separate and apart from NFLP profits as a result of the decisions they make for the NFLP. NFLP's decisions thus affect each team's profits from licensing its own intellectual property. "Although the business interests of" the teams "will *often* coincide with those of the" NFLP "as an entity in itself, that commonality of interest exists in every cartel." *Los Angeles Memorial Coliseum Comm'n v. NFL*, 726 F.2d 1381, 1389 (C.A.9 1984) (emphasis added). In making the relevant licensing decisions, NFLP is therefore "an instrumentality" of the teams. *Sealy*, 388 U.S., at 352-354.

If the fact that potential competitors shared in profits or losses from a venture meant that the venture was immune from § 1, then any cartel "could evade the antitrust law simply by creating a 'joint venture' to serve as the exclusive seller of their competing products." *Major League Baseball Properties, Inc. v. Salvino, Inc.*, 542 F.3d 290, 335 (C.A.2 2008) (Sotomayor, J., concurring in judgment). "So long as no agreement," other than one made by the cartelists sitting on the board of the joint venture, "explicitly listed the prices to be charged, the companies could act as monopolies through the 'joint venture.'" *Ibid.* (Indeed, a joint venture with a single management structure is generally a better way to operate a cartel because it decreases the risks of a party to an illegal agreement defecting from that agreement). However, competitors "cannot simply get around" antitrust liability by acting "through a third-party intermediary or 'joint venture'." *Id.*, at 336.

VI

Football teams that need to cooperate are not trapped by antitrust law. "[T]he special characteristics of this industry may provide a justification" for many kinds of agreements. *Brown*, 518 U.S., at 252 (STEVENS, J., dissenting). The fact that NFL teams share an interest in making the entire league successful and profitable, and that they must cooperate in the production and scheduling of games, provides a perfectly sensible justification for making a host of collective decisions. But the conduct at issue in this case is still concerted activity under the Sherman Act that is subject to § 1 analysis.

When "restraints on competition are essential if the product is to be available at all," *per se* rules of illegality are inapplicable, and instead the restraint must be judged according to the flexible Rule of Reason. In such instances, the agreement is likely to survive the Rule of Reason. And depending upon the concerted activity in question, the Rule of Reason may not require a detailed analysis; it "can sometimes be applied in the twinkling of an eye." *NCAA*, 468 U.S., at 109, n. 39.

Other features of the NFL may also save agreements amongst the teams. We have recognized, for example, "that the interest in maintaining a competitive balance" among "athletic teams is legitimate and important," *NCAA*, 468 U.S., at 117. While that same interest applies to the teams in the NFL, it does not justify treating them as a single entity for § 1 purposes when it comes to the marketing of the teams' individually owned intellectual property. It is, however, unquestionably an interest that may well justify a variety of collective decisions made by the teams. What role it properly plays in applying the Rule of Reason to the allegations in this case is a matter to be considered on remand.

* * *

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

Interstate Circuit, Inc. v. United States

306 U.S. 208 (1939)

MR. JUSTICE STONE delivered the opinion of the Court: This case is here on appeal *** from a final decree of the District Court for northern Texas restraining appellants from continuing in a combination and conspiracy condemned by the court as a violation of § 1 of the Sherman Anti-Trust Act, and from enforcing or renewing certain contracts found by the court to have been entered into in pursuance of the conspiracy. *** The case is now before us on findings of the District Court specifically stating that appellants did in fact agree with each other to enter into and carry out the contracts, which the court found to result in unreasonable and therefore unlawful restraints of interstate commerce.

Appellants comprise the two groups of defendants in the District Court. The members of one group of eight corporations which are distributors of motion picture films, and the Texas agents of two of them, are appellants in No. 270. The other group, corporations and individuals engaged in exhibiting motion pictures in Texas, and some of them in New Mexico, appeals in No. 269. The distributor appellants are engaged in the business of distributing in interstate commerce motion picture films, copyrights on which they own or control, for exhibition in theatres throughout the United States. They distribute about 75 per cent of all first-class feature films exhibited in the United States. They solicit from motion picture theatre owners and managers in Texas and other states applications for licenses to exhibit films, and forward the applications, when received from such exhibitors, to their respective New York offices, where they are accepted or rejected. If the applications are accepted, the distributors ship the films from points outside the states of exhibition to their exchanges within those states, from which, pursuant to the license agreements, the films are delivered to the local theatres for exhibition. After exhibition the films are reshipped to the distributors at points outside the state.

The exhibitor group of appellants consists of Interstate Circuit, Inc., and Texas Consolidated Theatres, Inc., and Hoblitzelle and O'Donnell, who are respectively president and general manager of both and in active charge of their business operations. The two corporations are affiliated with each other and with Paramount Pictures Distributing Co., Inc., one of the distributor appellants.

Interstate operates forty-three first-run and second-run motion picture theatres, located in six Texas cities.[1] It has a complete monopoly of first-run theatres in these cities, except for one in Houston operated by one distributor's Texas agent. In most of these theatres the admission price for adults for the better seats at night is 40 cents or more. Interstate also operates several subsequent-run theatres in each of these cities, twenty-two in all, but in all but Galveston there are other subsequent-run theatres which compete with both its first- and subsequent-run theatres in those cities.

Texas Consolidated operates sixty-six theatres, some first- and some subsequent-run houses, in various cities and towns in the Rio Grande Valley and elsewhere in Texas and in New Mexico. In some of these cities there are no competing theatres, and in six leading cities there are no competing first-run theatres. It has no theatres in the six Texas cities in which Interstate operates. That Interstate and Texas Consolidated dominate the motion picture business in the cities

[1] A first-run theatre is one in which a picture is first exhibited in any given locality. A subsequent-run theatre is one in which there is a subsequent exhibition of the same picture in the same locality.

where their theatres are located is indicated by the fact that at the time of the contracts in question Interstate and Consolidated each contributed more than 74 per cent of all the license fees paid by the motion picture theatres in their respective territories to the distributor appellants.

On July 11, 1934, following a previous communication on the subject to the eight branch managers of the distributor appellants, O'Donnell, the manager of Interstate and Consolidated, sent to each of them a letter[3] on the letterhead of Interstate, each letter naming all of them as addressees, in which he asked compliance with two demands as a condition of Interstate's continued exhibition of the distributors' films in its "A" or first-run theatres at a night admission of 40 cents or more.[4] One demand was that the distributors "agree that in selling their product to subsequent runs, that this 'A' product will never be exhibited at any time or in any theatre at a smaller admission price than 25 cents for adults in the evening." The other was that "on 'A' pictures which are exhibited at a night admission of 40 cents or more—they shall never be exhibited in conjunction with another feature picture under the so-called policy of double features." The letter added that with respect to the 'Rio Grande Valley situation', with which Consolidated alone was concerned, "We must insist that all pictures exhibited in our 'A' theatres at a maximum night admission price of 35 cents must also be restricted to subsequent runs in the Valley at 25 cents."

The admission price customarily charged for preferred seats at night in independently operated subsequent-run theatres in Texas at the time of these letters was less than 25 cents. In

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[3] The letter follows:

Interstate Circuit, Inc.,
Majestic Theatre Building,
Dallas, Texas. July 11, 1934.

Messrs.: J.B. Dugger, Herbert MacIntyre, Sol Sachs, C.E. Hilgers, Leroy Bickel, J.B. Underwood, E.S. Olsmyth, Doak Roberts.

Gentlemen: On April 25th, the writer notified you that in purchasing product for the coming season 34-35, it would be necessary for all distributors to take into consideration in the sale of subsequent runs that Interstate Circuit, Inc., will not agree to purchase product to be exhibited in its 'A' theatres at a price of 40 cents or more for night admission, unless distributors agree that in selling their product to subsequent runs, that this 'A' product will never be exhibited at any time or in any theatre at a smaller admission price than 25 cents for adults in the evening.

In addition to this price restriction, we also request that on 'A' pictures which are exhibited at a night admission price of 40 cents or more—they shall never be exhibited in conjunction with another feature picture under the so-called policy of double-features.

At this time the writer desires to again remind you of these restrictions due to the fact that there may be some delay in consummating all our feature film deals for the coming season, and it is imperative that in your negotiations that you afford us this clearance.

In the event that a distributor sees fit to sell his product to subsequent runs in violation of this request, it definitely means that we cannot negotiate for his product to be exhibited in our 'A' theatres at top admission prices.

We naturally, in purchasing subsequent runs from the distributors in certain of our cities, must necessarily eliminate double featuring and maintain the maximum 25 cents admission price, which we are willing to do.

Right at this time the writer wishes to call your attention to the Rio Grande Valley situation. We must insist that all pictures exhibited in our 'A' theatres at a maximum night admission price of 35 cents must also be restricted to subsequent runs in the Valley at 25 cents. Regardless of the number of days which may intervene, we feel that in exploiting and selling the distributors' product, that subsequent runs should be restricted to at least a 25 cents admission scale.

The writer will appreciate your acknowledging your complete understanding of this letter.

Sincerely,

(Signed) R. J. O'Donnell."

[4] A Class "A" picture is a "feature picture" having five reels or more of film each approximately 1,000 feet in length, shown in theatres of the specified Texas cities charging 40 cents or more for adult admission at night. Approximately fifty per cent. of pictures released by the distributor defendants in the Texas cities in 1934-1935 were Class "A" pictures.

seventeen of the eighteen independent theatres of this kind whose operations were described by witnesses the admission price was less than 25 cents. In one only was it 25 cents. In most of them the admission was 15 cents or less. It was also the general practice in those theatres to provide double bills either on certain days of the week or with any feature picture which was weak in drawing power. The distributor appellants had generally provided in their license contracts for a minimum admission price of 10 or 15 cents, and three of them had included provisions restricting doublebilling. But none was at any time previously subject to contractual compulsion to continue the restrictions. The trial court found that the proposed restrictions constituted an important departure from prior practice.

The local representatives of the distributors, having no authority to enter into the proposed agreements, communicated the proposal to their home offices. Conferences followed between Hoblitzelle and O'Donnell, acting for Interstate and Consolidated, and the representatives of the various distributors. In these conferences each distributor was represented by its local branch manager and by one or more superior officials from outside the state of Texas. In the course of them each distributor agreed with Interstate for the 1934-35 season to impose both the demanded restrictions upon their subsequent-run licensees in the six Texas cities served by Interstate, except Austin and Galveston. While only two of the distributors incorporated the agreement to impose the restrictions in their license contracts with Interstate, the evidence establishes, and it is not denied, that all joined in the agreement, four of them after some delay in negotiating terms other than the restrictions and not now material. These agreements for the restrictions—with the immaterial exceptions noted—were carried into effect by each of the distributors' imposing them on their subsequent-run licensees in the four Texas cities during the 1934-35 season. One agreement, that of Metro-Goldwyn-Mayer Distributing Corporation, was for three years. The others were renewed in the two following seasons and all were in force when the present suit was begun.

None of the distributors yielded to the demand that subsequent runs in towns in the Rio Grande Valley served by Consolidated should be restricted. One distributor, Paramount, which was affiliated with Consolidated, agreed to impose the restrictions in certain other Texas and New Mexico cities.

The trial court found that the distributor appellants agreed and conspired among themselves to take uniform action upon the proposals made by Interstate, and that they agreed and conspired with each other and with Interstate to impose the demanded restrictions upon all subsequent-run exhibitors in Dallas, Fort Worth, Houston and San Antonio; that they carried out the agreement by imposing the restrictions upon their subsequent-run licensees in those cities, causing some of them to increase their admission price to 25 cents, either generally or when restricted pictures were shown, and to abandon doublebilling of all such pictures, and causing the other subsequent-run exhibitors, who were either unable or unwilling to accept the restrictions, to be deprived of any opportunity to exhibit the restricted pictures, which were the best and most popular of all new feature pictures; that the effect of the restrictions upon "low-income members of the community" patronizing the theatres of these exhibitors was to withhold from them altogether the "best entertainment furnished by the motion picture industry;" and that the restrictions operated to increase the income of the distributors and of Interstate and to deflect attendance from later-run exhibitors who yielded to the restrictions to the first-run theatres of Interstate.

The court concluded as matters of law that the agreement of the distributors with each other and those with Interstate to impose the restrictions upon subsequent-run exhibitors and the carrying of the agreements into effect, with the aid and participation of Hoblitzelle and O'Donnell, constituted a combination and conspiracy in restraint of interstate commerce in violation of the Sherman Act. It also concluded that each separate agreement between Interstate and a distributor that Interstate should subject itself to the restrictions in its subsequent-run theatres and that the distributors should impose the restrictions on all subsequent-run theatres in the Texas cities as a condition of supplying them with its feature pictures, was likewise a violation of the Act.

It accordingly enjoined the conspiracy and restrained the distributors from enforcing the restrictions in their license agreements with subsequent-run exhibitors and from enforcing the contracts or any of them. This included both the contracts of Interstate with the distributors and the contract between Consolidated and Paramount, whereby the latter agreed to impose the restrictions upon subsequent-run theatres in Texas and New Mexico served by it.

The Agreement Among the Distributors.

Although the films were copyrighted, appellants do not deny that the conspiracy charge is established if the distributors agreed among themselves to impose the restrictions upon subsequent-run exhibitors. As is usual in cases of alleged unlawful agreements to restrain commerce, the government is without the aid of direct testimony that the distributors entered into any agreement with each other to impose the restrictions upon subsequent-run exhibitors. In order to establish agreement it is compelled to rely on inferences drawn from the course of conduct of the alleged conspirators.

The trial court drew the inference of agreement from the nature of the proposals made on behalf of Interstate and Consolidated; from the manner in which they were made; from the substantial unanimity of action taken upon them by the distributors; and from the fact that appellants did not call as witnesses any of the superior officials who negotiated the contracts with Interstate or any official who, in the normal course of business, would have had knowledge of the existence or non-existence of such an agreement among the distributors. This conclusion is challenged by appellants because not supported by subsidiary findings or by the evidence. We think this inference of the trial court was rightly drawn from the evidence. In the view we take of the legal effect of the cooperative action of the distributor appellants in carrying into effect the restrictions imposed upon subsequent-run theatres in the four Texas cities and of the legal effect of the separate agreements for the imposition of those restrictions entered into between Interstate and each of the distributors, it is unnecessary to discuss in great detail the evidence concerning this aspect of the case.

The O'Donnell letter named on its face as addressees the eight local representatives of the distributors, and so from the beginning each of the distributors knew that the proposals were under consideration by the others. Each was aware that all were in active competition and that without substantially unanimous action with respect to the restrictions for any given territory there was risk of a substantial loss of the business and good will of the subsequent-run and independent exhibitors, but that with it there was the prospect of increased profits. There was, therefore, strong motive for concerted action, full advantage of which was taken by Interstate and Consolidated in presenting their demands to all in a single document.

There was risk, too, that without agreement diversity of action would follow. Compliance with the proposals involved a radical departure from the previous business practices of the industry and a drastic increase in admission prices of most of the subsequent-run theatres. Acceptance of the proposals was discouraged by at least three of the distributors' local managers. Independent exhibitors met and organized a futile protest which they presented to the representatives of Interstate and Consolidated. While as a result of independent negotiations either of the two restrictions without the other could have been put into effect by any one or more of the distributors and in any one or more of the Texas cities served by Interstate, the negotiations which ensued and which in fact did result in modifications of the proposals resulted in substantially unanimous action of the distributors, both as to the terms of the restrictions and in the selection of the four cities where they were to operate.

*** But we are unable to find in the record any persuasive explanation, other than agreed concert of action, of the singular unanimity of action on the part of the distributors by which the proposals were carried into effect as written in four Texas cities but not in a fifth or in the Rio Grande Valley. Numerous variations in the form of the provisions in the distributors' license agreements and the fact that in later years two of them extended the restrictions into all six cities, do not weaken the significance or force of the nature of the response to the proposals made by all the distributor appellants. It taxes credulity to believe that the several distributors would, in the circumstances, have accepted and put into operation with substantial unanimity such far-reaching changes in their business methods without some understanding that all were to join, and we reject as beyond the range of probability that it was the result of mere chance.

*** The trial court, interpreting the letter in the light of the whole evidence, which showed unmistakably that one purpose of both demands was to protect first-run houses from competition of subsequent-run houses, concluded that the substance of the proposals in one case as in the other was that the restrictions upon the subsequent-run theatres were to be imposed only in the same city in which the first run had occurred. We agree with its conclusion, but in any event since the demand made by Interstate was phrased as broadly as that made by Texas Consolidated, both as to the kind of pictures affected and the scope of the restriction, we can find no basis for saying that one was more limited in its essentials than the other, or that any explanation is thus afforded of the unanimous acceptance of the demands of Interstate in four of the six cities affected by the proposal, and the unanimous rejection of the demand of Consolidated. In the face of this action and similar unanimity with respect to other features of the proposals, and the strong motive for such unanimity of action, we decline to speculate whether there may have been other and more legitimate reasons for such action not disclosed by the record, but which, if they existed, were known to appellants. ***

This inference was supported and strengthened when the distributors, with like unanimity, failed to tender the testimony, at their command, of any officer or agent of a distributor who knew, or was in a position to know, whether in fact an agreement had been reached among them for concerted action. When the proof supported, as we think it did, the inference of such concert, the burden rested on appellants of going forward with the evidence to explain away or contradict it. They undertook to carry that burden by calling upon local managers of the distributors to testify that they had acted independently of the other distributors, and that they did not have conferences with or reach agreements with the other distributors or their representatives. The failure under the circumstances to call as witnesses those officers who did have authority to act for the distributors and who were in a position to know whether they had acted in pursuance of agreement is itself persuasive that their testimony, if given, would have been unfavorable to appellants. The production of weak evidence when strong is available can lead only to the conclusion that the strong would have been adverse.

While the District Court's finding of an agreement of the distributors among themselves is supported by the evidence, we think that in the circumstances of this case such agreement for the imposition of the restrictions upon subsequent-run exhibitors was not a prerequisite to an unlawful conspiracy. It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that cooperation was essential to successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce, which, we will presently point out, was unreasonable within the meaning of the Sherman Act, and knowing it, all participated in the plan. The evidence is persuasive that each distributor early became aware that the others had joined. With that knowledge they renewed the arrangement and carried it into effect for the two successive years.

It is elementary that an unlawful conspiracy may be and often is formed without simultaneous action or agreement on the part of the conspirators. Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act. ***

We think the conclusion is unavoidable that the conspiracy and each contract between Interstate and the distributors by which those consequences were effected are violations of the Sherman Act and that the District Court rightly enjoined enforcement and renewal of these agreements, as well as of the conspiracy among the distributors.

Affirmed.

Theatre Enterprises, Inc. v. Paramount Film Distributing Corp.

346 U.S. 537 (1954)

MR. JUSTICE CLARK delivered the opinion of the Court: Petitioner brought this suit for treble damages and an injunction under §§ 4 and 16 of the Clayton Act, alleging that respondent motion picture producers and distributors had violated the antitrust laws by conspiring to restrict "first-run" pictures to downtown Baltimore theatres, thus confining its suburban theatre to subsequent runs and unreasonable "clearances."[5] After hearing the evidence a jury returned a general verdict for respondents. The Court of Appeals for the Fourth Circuit affirmed the judgment based on the verdict. We granted certiorari.

*** The opinion of the Court of Appeals contains a complete summary of the evidence presented to the jury. We need not recite that evidence again. It is sufficient to note that petitioner owns and operates the Crest Theatre, located in a neighborhood shopping district some six miles from the downtown shopping center in Baltimore, Maryland. The Crest, possessing the most modern improvements and appointments, opened on February 26, 1949. Before and after the opening, petitioner, through its president, repeatedly sought to obtain first-run features for the theatre. Petitioner approached each respondent separately, initially requesting exclusive first-

[5] "A clearance is the period of time, usually stipulated in license contracts, which must elapse between runs of the same feature within a particular area or in specified theatres." *United States v. Paramount Pictures, Inc.*, 1948, 334 U.S. 131, 144, note 6.

runs, later asking for first-runs on a "day and date" basis.[7] But respondents uniformly rebuffed petitioner"'s efforts and adhered to an established policy of restricting first-runs in Baltimore to the eight downtown theatres. Admittedly there is no direct evidence of illegal agreement between the respondents and no conspiracy is charged as to the independent exhibitors in Baltimore, who account for 63% of first-run exhibitions. The various respondents advanced much the same reasons for denying petitioner's offers. Among other reasons they asserted that day and date first-runs are normally granted only to noncompeting theatres. Since the Crest is in "substantial competition" with the downtown theatres, a day and date arrangement would be economically unfeasible. And even if respondents wished to grant petitioner such a license, no downtown exhibitor would waive his clearance rights over the Crest and agree to a simultaneous showing. As a result, if petitioner were to receive first-runs, the license would have to be an exclusive one. However, an exclusive license would be economically unsound because the Crest is a suburban theatre, located in a small shopping center, and served by limited public transportation facilities; and, with a drawing area of less than one-tenth that of a downtown theatre, it cannot compare with those easily accessible theatres in the power to draw patrons. Hence the downtown theatres offer far greater opportunities for the widespread advertisement and exploitation of newly released features, which is thought necessary to maximize the overall return from subsequent runs as well as first-runs. The respondents, in the light of these conditions, attacked the guaranteed offers of petitioner, one of which occurred during the trial, as not being made in good faith. Respondents Loew's and Warner refused petitioner an exclusive license because they owned the three downtown theatres receiving their first-run product.

The crucial question is whether respondents' conduct toward petitioner stemmed from independent decision or from an agreement, tacit or express. To be sure, business behavior is admissible circumstantial evidence from which the fact finder may infer agreement. *Interstate Circuit, Inc. v. United States*, 1939, 306 U.S. 208; *United States v. Masonite Corp.*, 316 U.S. 265 (1942); *United States v.Bausch & Lomb Optical Co.,* 321 U.S. 707 (1944); *American Tobacco Co. v. United States*, 328 U.S. 781 (1946); *United States v. Paramount Pictures, Inc.*, 334 U.S. 131 (1948). But this Court has never held that proof of parallel business behavior conclusively establishes agreement or, phrased differently, that such behavior itself constitutes a Sherman Act offense. Circumstantial evidence of consciously parallel behavior may have made heavy inroads into the traditional judicial attitude toward conspiracy; but "conscious parallelism" has not yet read conspiracy out of the Sherman Act entirely. Realizing this, petitioner attempts to bolster its argument for a directed verdict by urging that the conscious unanimity of action by respondents should be "measured against the background and findings in the *Paramount* case." In other words, since the same respondents had conspired in the *Paramount* case to impose a uniform system of runs and clearances without adequate explanation to sustain them as reasonable restraints of trade, use of the same device in the present case should be legally equated to conspiracy. But the *Paramount* decrees, even if admissible, were only prima facie evidence of a conspiracy covering the area and existing during the period there involved. Alone or in conjunction with the other proof of the petitioner, they would form no basis for a directed verdict. Here each of the respondents had denied the existence of any collaboration and in addition had introduced evidence of the local conditions surrounding the Crest operation which, they contended, precluded it from being a successful first-run house. They also attacked the good faith of the guaranteed

[7] A first-run "day-and-date" means that two theatres exhibit a first-run at the same time. Had petitioner's request for a day and date first-run been granted, the Crest and a downtown theatre would have exhibited the same features simultaneously.

offers of the petitioner for first-run pictures and attributed uniform action to individual business judgment motivated by the desire for maximum revenue. This evidence, together with other testimony of an explanatory nature, raised fact issues requiring the trial judge to submit the issue of conspiracy to the jury. ***

Kleen Products LLC v. Georgia Pacific LLC

910 F.3d 927 (7th Cir. 2018)

WOOD, CHIEF JUDGE: Oligopolies have always posed problems for conventional antitrust law: without something that can be called an agreement, they elude scrutiny under section 1 of the Sherman Act, 15 USC 1, and yet no individual firm has enough market power to be subject to Sherman Act section 2, 15 USC 2. Tacit collusion is easy in those markets, see *In re Text Messaging Antitrust Litigation*, 782 F.3d 867 (7th Cir. 2015), and firms have little incentive to compete on the basis of price, "preferring to share the profits [rather] than to fight with each other." *Joe Sanfelippo Cabs, Inc. v. City of Milwaukee*, 839 F.3d 613, 615 (7th Cir. 2016).

This appeal concerns the fine line between agreement and tacit collusion, or, put another way, conscious parallelism. Direct purchasers of containerboard ("the Purchasers") charged multiple manufacturers with conspiring to increase prices and reduce output between 2004 and 2010. We affirmed the district court's decision to certify a nationwide class of buyers. *Kleen Prods. LLC v. Int'l Paper Co.*, 831 F.3d 919 (7th Cir. 2016). Before and after that ruling, most of the defendants settled with the Purchasers. But two companies—Georgia-Pacific LLC and WestRock CP, LLC—decided to fight. They persuaded the district court that there was not enough evidence of a conspiracy to proceed to trial. We agree with that assessment and affirm the judgment dismissing the case.

I

A

Containerboard is the name of the material used in countless boxes: it consists of a corrugated layer of heavy paper sandwiched between two smooth pieces of linerboard. Demand is relatively inelastic, meaning that customers will not defect to other products even if the price goes up, because the available substitutes are inferior. Containerboard is manufactured at large, costly mills, which are hard to duplicate, given both the high cost of construction and the myriad of environmental laws that must be satisfied. A handful of major players dominate the industry. Those players include the original defendants in this suit: International Paper ("IP"), Georgia-Pacific, Temple-Inland, Inc., WestRock, Weyerhaeuser Co., Norampac Holdings U.S. Inc., and Packaging Corporation of America ("PCA").

During the early 2000s, prices for containerboard were low. But from February 2004 to November 2010, they rose dramatically. The original defendants attempted to institute price increases on 15 different occasions. The pattern was a common one. After one company announced that it would raise its prices for containerboard, the rest followed suit with identical or comparable increases in the ensuing hours, days, or weeks. (The one exception was a failed attempt in which there were three hold-outs.) Such efforts took place from time to time. For example, in March 2003, the defendants attempted an ultimately unsuccessful increase. Of the proposed hikes from 2004 to 2010, Georgia-Pacific, WestRock, and a non-defendant each led the effort twice. The price increases were sustained nine times, a 60% success rate.

While containerboard prices rose, containerboard production capacity fell in North America (despite the inelasticity of demand and growth throughout the rest of the globe). The initial defendants were not immune from this decline. The Purchasers' expert concluded that the defendant companies reduced their production capacity by an amount almost double that of non-defendants, though they used different strategies to accomplish this goal. They closed a significant number of mills during the class period—WestRock alone was responsible for more than a third of those closures. WestRock also took care, through measures such as buyer selection and machinery sales, to avoid adding containerboard supply into the market. Georgia-Pacific kept all its mills running, but it slowed the rate of production. It would periodically "slow back" production by idling or shutting down machines and taking extra downtime. While these practices diminished supply to the point that it sometimes pinched, in the end Georgia-Pacific never missed an order. And the company actually increased its overall capacity by acquiring a new mill in 2007.

During this period, the defendants were in regular communication. Company executives and other employees spoke by phone and at trade association meetings every few days. The record does not reveal the contents of all these conversations, but at least some dealt with the timing and pricing of interfirm trading of containerboard—a common practice.

Internal and public-facing statements made by the defendants' employees shed light on these economic developments. Some email exchanges may be read to imply that the defendants had foreknowledge of other companies' proposed increases before they were announced. For example, just before three price hikes, a PCA employee offered an opinion about how high prices would need to go over the next year and a half in order to recover the cost of capital. A Georgia-Pacific staffer wrote "the party begins" when discussing an increase attempt. A WestRock vice president emailed that the company "always follow[s] IP," even though in fact "always" was an overstatement. And a Weyerhaeuser employee discussed a specific increase two days before WestRock first made its new price public. Other statements support the inference that a coordinated plan was in place. For instance, a Weyerhaeuser employee wrote that he "made up a bunch" of information in a report about what was learned from customers about competition, asking others to "be more specific" to stay "out of anti-trust legal issues." A Norampac executive, discussing problems with the industry, said "you have to be ready to let go business if you want to keep the price up," and "everybody needs to do the same thing."

Georgia-Pacific and WestRock made their own incriminating remarks. Because some details remain under seal in this court, some of our examples are a bit vague, but we have reviewed the sealed materials and they are consistent with the remainder of the evidence. A WestRock vice-president made remarks in an email that could easily be construed as an undertaking to follow-the-leader. A different vice-president complained that the company "ha[d] no choice but to support [a price increase] initiative" and that WestRock "ha[d] done [its] part." At one point, a company employee wrote that the "only way to get paid is to have a 1994-95 situation where the tide rises for all boats," perhaps referring to the containerboard industry's earlier run-ins with antitrust law. See, e.g., *In re Linerboard Antitrust Litig.*, 305 F.3d 145 (3d Cir. 2002). Publicly, WestRock's CEO was reported to have said that the company had a restructuring plan to "cut supply enough at [WestRock] to force price increases throughout the industry." Georgia-Pacific's president gave a speech during the period in question urging the industry to resist customer requests for price breaks.

B

In September 2010, the Purchasers filed a putative class action alleging violations of section 1 of the Sherman Act. 15 USC 1. *** Both sides moved for summary judgment. Before the court acted on those motions, some of the defendants settled with the Purchasers. The district court granted the remaining defendants, Georgia-Pacific and WestRock, summary judgment. In a lengthy opinion that delved deeply into the Purchasers' evidence, the court concluded that the record, viewed holistically in the light most favorable to the Purchasers, did not tend to rule out that the defendants had acted independently. With only the final approval of settlement agreements pending, the district court entered partial final judgment for the remaining defendants under Rule 54(b). The Purchasers ask us to revisit that ruling.

II

Section 1 of the Sherman Act prohibits every "contract, combination, ... or conspiracy in restraint of trade...." Courts have understood for more than a century that this language does not ban all contracts, but instead reaches only agreements that restrict competition. *Copperweld Corp. v. Indep. Tube Corp.*, 467 U.S. 752, 768 (1984); see also *Broadcast Music, Inc. v. Columbia Broadcasting Sys., Inc.*, 441 U.S. 1 (1979). In the absence of an agreement, the antitrust laws forbid only monopolization or attempts to monopolize, see 15 USC 2, as well as a few other arrangements including anticompetitive mergers and acquisitions, see 15 USC 18. But this case concerns only section 1; the plaintiffs make no claim that any of the defendants has even attempted to monopolize, much less succeeded in such an effort. We can therefore disregard all other antitrust theories and focus on the question whether the district court correctly decided that the Purchasers did not present enough evidence to permit a trier of fact to find the agreement necessary for section 1 liability. As the Supreme Court put it in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), "at the summary judgment stage a § 1 plaintiff's offer of conspiracy evidence must tend to rule out the possibility that the defendants were acting independently." Id. at 554, citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986).

It is worth recalling that an antitrust plaintiff, like all others, is entitled to try to meet that burden with either direct or circumstantial evidence. Antitrust plaintiffs do not face a heightened burden to defeat summary judgment. As Rule 56 generally commands, we draw all reasonable inferences in favor of the non-moving party, here the Purchasers. It is the substantive law, however, that establishes what the plaintiff must address. The Purchasers needed evidence that would allow a trier of fact to nudge the ball over the 50-yard line and rationally to say that the existence of an agreement is more likely than not. Put more directly, they must put on the table "some evidence which, if believed, would support a finding of concerted behavior." *Toys "R" Us Inc. v. FTC*, 221 F.3d 928, 935 (7th Cir. 2000).

Armed with bountiful circumstantial evidence, the Purchasers accuse the defendant manufacturers of agreeing to restrict the supply of containerboard and thereby to create market conditions that would support significantly higher prices. The district court properly considered "economic evidence suggesting that the defendants were not in fact competing, and non-economic evidence suggesting that they were not competing because they had agreed not to compete." *In re High Fructose Corn Syrup Antitrust Litig.*, 295 F.3d 651, 655 (7th Cir. 2002). It then drew and compared the corresponding inferences from each data point. After determining that each piece of evidence individually did not rule out the possibility of independent action, it reviewed the evidence in the aggregate, as required. The court concluded that because no individual piece of evidence tended to show collusion, the combined probative value was zero. We are not so sure of that. While no single piece of information may win the day, the whole may be greater than the sum of its parts in tending to exclude the possibility of conscious parallelism.

Nonetheless, our assessment of the district court's decision is de novo, and so we need only satisfy ourselves that we have the proper standard in mind. Viewing the evidence and reasonable inferences in the Purchasers' favor, we ask whether they have produced any evidence that would rule out the hypothesis that the defendants were engaged in self-interested but lawful oligopolistic behavior during the relevant period. Despite the volume of evidence the Purchasers submitted in opposition to summary judgment, we find ourselves in agreement with the district court's ultimate conclusion. *** We conclude that nothing in this record would permit a trier of fact to conclude that the defendants were colluding, rather than behaving in their independent self-interest.

III

A

We start with some structural evidence about the containerboard industry. As we noted in our earlier encounter with this litigation, the market has certain structural features that make it "conducive to successful collusion," such as a small number of manufacturers, vertical integration, inelastic demand, a standardized commodity product, and high barriers to entry. *Kleen Prods.*, 831 F.3d at 927-28. These characteristics make it easier for companies either to form a cartel or to follow the leader independently. *Text Messaging*, 782 F.3d at 871-72. We explained why this is so in our 2015 *Text Messaging* opinion:

> [I]f a small number of competitors dominates a market, they will find it safer and easier to fix prices than if there are many competitors of more or less equal size. For the fewer the conspirators, the lower the cost of negotiation and the likelihood of defection.... But the other side of this coin is that the fewer the firms, the easier it is for them to engage in "follow the leader" pricing ("conscious parallelism," as lawyers call it, "tacit collusion" as economists prefer to call it)—which means coordinating their pricing without an actual agreement to do so. As for the apparent anomaly of competitors' raising prices in the face of falling costs, ... this may be not because they've agreed not to compete but because all of them have determined independently that they may be better off with a higher price. That higher price, moreover—the consequence of parallel but independent decisions to raise prices—may generate even greater profits (compared to competitive pricing) if costs are falling, provided that consumers do not have attractive alternatives.

Text Messaging, 782 F.3d at 871-72. Because of the competing inferences that can be drawn from this market structure, the district court properly found that the economic evidence did not tend to exclude the possibility of independent action.

B

Next, we turn to more specific evidence that the Purchasers offered. In establishing both defendants' failure to compete, the Purchasers rely heavily on the 15 price hikes that occurred over the class period. But one must take care with the inferences that can be drawn from such evidence. Following a competitor's price increases can be consistent with rational self-interest in oligopolies. A firm in a tight oligopoly might think that it will reap greater profits if it imitates, rather than undermines, its peers' price hikes. *Brooke Grp. Ltd. v. Brown & Williamson Tobacco*

Corp., 509 U.S. 209, 227 (1993). And it might reach that conclusion without any conscious coordination with its competitors. For that reason, "it is not a violation of antitrust law for a firm to raise its price, counting on its competitors to do likewise (but without any communication with them on the subject). ..." *Text Messaging*, 782 F.3d at 876.

1

The task before any plaintiff is thus to find and produce evidence that reveals coordination or agreement (even a wink and a nod—formal agreements have never been required for purposes of Sherman Act section 1). For instance, foreknowledge of price increases may be persuasive evidence that an agreement was afoot. See *In re Chocolate Confectionary Antitrust Litig.*, 801 F.3d 383, 408 (3d Cir. 2015). The Purchasers here attempt to carry their burden by emphasizing the timing of the price increase attempts, which they describe as "lockstep." They urge us to draw the inference that such tight congruence of price movements could not have occurred unless the competitors had an inside scoop. But a close look at the record reveals that the Purchasers overstate how coordinated these hikes actually were. Different manufacturers, including non-defendants, led the attempts. Sometimes companies followed suit over a month later. Even the attempts that saw quick turnaround times do little to raise suspicions. If it is in a company's self-interest to imitate a price leader's increase, why wait to enjoy the benefit? The Purchasers accuse the defendants of lying when they claim to have explored independently a possible increase. But there is no evidence supporting this allegation.

The Purchasers' "proof" of prior knowledge amounts to nothing more than speculation. They emphasize a March 2004 PCA memorandum that said "at least three $40-50 increases over the next 18 months" were needed to recoup the cost of capital. By September 2005, three attempts to raise prices had indeed occurred. But this supposed smoking gun could be nothing more than a somewhat accurate industry prediction. That two of the increases were for $50 is unsurprising, given that most of the 15 attempts were for $40 or $50. More tellingly, the PCA employee did not accurately predict three successful increases, since the second one failed and the third was only for $30.

The evidence that Georgia-Pacific provided or received advance notice is even weaker. The best that the Purchasers offer is a comment made by a Georgia-Pacific employee that "the party begins," following a discussion that a few manufacturers had announced an increase. This remark could merely express enthusiasm about the upward trend in pricing.

Another aspect of the Purchasers' argument is that the rising prices throughout the class period reflect an abrupt change in business practices. If that is an accurate description of what happened, it might support an inference of conspiracy. But before the inference can be drawn, we have looked for a shift in firm behavior, as opposed to external market conditions. In the present case, the Purchasers' evidence reveals only changed market conditions. For instance, they point to complaints that manufacturers made about aggressively competitive pricing that took place before, but not during, the class period. Yet the shift may be explained by external factors, such as the emergence from the economic downturn of 2008, which occurred in the middle of the class period. And in terms of the companies' behavior—the relevant inquiry—the manufacturers had attempted to raise prices before the class period as well. A continuation of a historic pattern—including of parallel price increase announcements—does not plausibly allow one to infer the existence of a cartel.

A further strike against the Purchasers' case is the failure rate of the manufacturers' efforts: 40% of the attempted increases did not hold. The district court pondered why a company would risk treble damages by colluding on an often-ineffective plan when tacitly following price hikes had no downside risk. Perhaps the Purchasers have a good answer to that question: when potential profits are in the billions, even 60% odds provide a substantial incentive. But that at best leaves matters in equipoise.

If this was a cartel, it would have tried to impose disciplinary measures on the "cheaters" who did not go along with the price increases. But that type of evidence is conspicuously absent, even though nearly half the price hikes failed. The Purchasers propose two possible mechanisms for enforcement, but they have not pointed to any evidence indicating that either one was used. It is true that a cartel may exist with only soft measures of control or ineffective enforcement. Even if that is so, however, the absence of evidence about enforcement does nothing to dissipate the inference of independent behavior. We are still left with price increases that appear to be just as consistent with independent action as with collusion.

2

The second half of the Purchasers' theory focuses on supposedly coordinated reductions of output through mill closures and machine slowdowns. Supply behavior is highly relevant because price-fixing arrangements often function through restrictions of output. But not every supply-side change is equally suggestive of a conspiracy. Conduct that is easily reversed may be consistent with self-interested decision-making.

An example illustrates the point. Suppose Company X takes its machines offline more frequently in order to reduce its supply. If competitors follow suit, and industry-wide production falls, all companies can charge more for the commodity and potentially reap greater profits. But what if instead the competitors maintain their supply and woo Company X's customers. Because Company X's reduction strategy was flexible, it can quickly get its machines running and filling orders again, minimizing any losses. In contrast, if Company X had lowered its production by selling its mills or equipment, it could not rapidly undo its efforts while competitors came knocking on customers' doors. *** Firms take significant risks by reducing their output in an inflexible manner, unless there is an enforceable agreement in place to ensure that competitors will follow suit. Because [this behavior] makes "little economic sense" absent coordination, evidence of less-reversible supply restrictions supports an inference of conspiracy.

During the class period, the North American market saw a drop in overall capacity for containerboard. The original defendants collectively were responsible for 19 mill closures. Yet Georgia-Pacific not only kept its mills open; it also purchased a new mill. The Purchasers respond that Georgia-Pacific underutilized its machines, but Georgia-Pacific has an answer for that: its run-to-demand strategy. Under this strategy, which dated back to 1999, Georgia-Pacific aimed to produce just enough containerboard to fill orders without creating excess inventory. Internal communications suggest that this strategy led to some close calls when filling orders, but Georgia-Pacific always found a way to meet its customer demand. Moreover, its acquisition of a mill allowed it to increase its production capacity over the class period.

The Purchasers' strongest evidence undercutting Georgia-Pacific's account are comments in performance reviews that credit employees for getting price increases by keeping inventory low. Because Georgia-Pacific did not have sufficient market power to alter containerboard pricing on its own, the Purchasers insist that these statements can be understood only as proof of an anticompetitive agreement. But underusing machinery is the kind of flexible behavior that is consistent with rational attempts to raise prices through watchful attention to one's competitors' actions. Far from perilous, had Georgia-Pacific's efforts not paid off, it could have increased its output quickly. Georgia-Pacific's supply behavior does not point towards its having a role in any conspiracy.

3

As ammunition against both defendants, the Purchasers cite the frequent contacts that company executives had by phone and at trade association meetings. They allege that the defendants' regular communications and trades served as opportunities for collusion. Some courts have held that this type of information flow, especially between executives, may be probative of conspiracy. But having the opportunity to conspire does not necessarily imply that wrongdoing occurred. Especially when companies have legitimate business reasons for their contacts, plaintiffs must offer some evidence that moves beyond speculation about the content of what was conveyed.

The Purchasers have no evidence indicating that the executives discussed illicit price-fixing or output restriction deals during their calls or meetings. They rely instead on the frequency and timing of the contacts. For example, 20 calls were made in the days around a Georgia-Pacific-led price increase, despite the fact that the company had predicted flat pricing just two weeks earlier. That is not enough. We cannot put much stock in the frequency of contacts, given the amount of trading that was taking place among the firms.

Furthermore, we hesitate to impugn the companies' intentions solely from the timing of the contacts. To be clear, we do not see the frequency of the calls and meetings as evidence tending to exclude collusion. Such a rule would create an incentive for businesses to make constant phone calls in order to immunize themselves from antitrust liability. Here, however, though some trade association meetings occurred before price-increase proposals, most of Georgia-Pacific's announcements were not preceded by meetings. The Purchasers' speculation about the content of the frequent interfirm contacts is not enough to create a jury issue.

4

Incriminating remarks by defendants' employees can support the inference that a conspiracy existed. The Purchasers flag a few comments that they see as particularly inculpatory. For starters, a Weyerhaeuser employee wrote that he "made up a bunch" of information in a report and instructed others to "be more specific" to keep the company "out of anti-trust legal issues." In addition, while discussing problems with the industry, a Norampac executive said "you have to be ready to let go business if you want to keep the price up," and "everybody needs to do the same thing."

Yet even if these statements are enough to create a triable question about the presence of an agreement generally, they are not enough to show that Georgia-Pacific was a part of that cartel. On this front, the Purchasers present little proof. They point to a speech in which Georgia-Pacific's CEO supposedly suggested that the industry should "say 'no' on deals" that, though competitive, are not profitable. But that is hardly an earthshattering insight, even if proof of the statement were possible without the use of hearsay contained in newspaper articles reporting on the speech. And the account of an attendee rejects the rumors, stating that this message "was not said nor implied." And the CEO claimed in his deposition that he was speaking only about Georgia-Pacific, not the industry, needing to decline deals. Like their economic proof, the Purchasers' noneconomic evidence—even when viewed with the parallel conduct—does not exclude the possibility that Georgia-Pacific acted in a self-interested but permissible way.

C

Some of the Purchasers' evidence was particular to WestRock, to which we now turn. There is a wrinkle in its potential liability: in June 2010, just shy of the close of the class period, WestRock received a discharge in bankruptcy, for which it had filed in 2009. At that moment, it was free of any antitrust liability incurred up to the date of discharge. Nonetheless, WestRock is potentially liable for the alleged conspiracy if there is evidence it rejoined the cartel post-discharge. We must therefore look to see if there is evidence that would permit a trier of fact both to find the initial agreement, and to find that WestRock rejoined that agreement after its discharge. *** Even assuming (favorably to the Purchasers) that WestRock was part of a cartel, they fall short on presenting evidence that WestRock was involved post-discharge. ***

IV

The outcome of this case flows directly from both the limitation in section 1 of the Sherman Act to anticompetitive agreements and the Supreme Court's cautions against interfering with individual firm behavior in ways that could inadvertently distort incentives to compete. In *Matsushita*, the Court warned against "mistaken inferences ... [that] chill the very conduct the antitrust laws are designed to protect."' *Matsushita*, 475 U.S. at 594.

Scholars, lawmakers, and courts have yet to agree on a regulatory regime that can address oligopolistic behavior that leads to higher prices and reduced consumer choice, without stifling normal business activity. For now, we follow established law to the effect that "'conscious parallelism' has not yet read conspiracy out of the Sherman Act entirely." *Twombly*, 550 U.S. at 552 (citation omitted). Because the evidence proffered by the Purchasers does not tend to exclude the possibility that Georgia-Pacific and WestRock engaged only in tacit collusion, we AFFIRM the judgment of the district court.

National Collegiate Athletic Ass'n v. Alston

594 U.S. 69 (2021)

JUSTICE GORSUCH, delivered the opinion of the Court. In the Sherman Act, Congress tasked courts with enforcing a policy of competition on the belief that market forces "yield the best allocation" of the Nation's resources. *National Collegiate Athletic Assn. v. Board of Regents of Univ. of Okla.*, 468 U.S. 85, 104, n. 27 (1984). The plaintiffs before us brought this lawsuit alleging that the National Collegiate Athletic Association (NCAA) and certain of its member institutions violated this policy by agreeing to restrict the compensation colleges and universities may offer the student-athletes who play for their teams. After amassing a vast record and conducting an exhaustive trial, the district court issued a 50-page opinion that cut both ways. The court refused to disturb the NCAA's rules limiting undergraduate athletic scholarships and other compensation related to athletic performance. At the same time, the court struck down NCAA rules limiting the education-related benefits schools may offer student-athletes—such as rules that prohibit schools from offering graduate or vocational school scholarships. Before us, the student-athletes do not challenge the district court's judgment. But the NCAA does. In essence, it seeks immunity from the normal operation of the antitrust laws and argues, in any event, that the district court should have approved all of its existing restraints. We took this case to consider those objections.

I

A

*** [In 1929], the Carnegie Foundation produced a report on college athletics that found them still "sodden with the commercial and the material and the vested interests that these forces have created." H. Savage, The Carnegie Foundation for the Advancement of Teaching, American College Athletics Bull. 23, p. 310 (1929). Schools across the country sought to leverage sports to bring in revenue, attract attention, boost enrollment, and raise money from alumni. The University of California's athletic revenue was over $480,000, while Harvard's football revenue alone came in at $429,000. College football was "not a student's game"; it was an "organized commercial enterprise" featuring athletes with "years of training," "professional coaches," and competitions that were "highly profitable." Id., at viii.

The commercialism extended to the market for student-athletes. Seeking the best players, many schools actively participated in a system "under which boys are offered pecuniary and other inducements to enter a particular college." Id., at xiv-xv. One coach estimated that a rival team "spent over $200,000 a year on players." A. Zimbalist, Unpaid Professionals 9 (1999). In 1939, freshmen at the University of Pittsburgh went on strike because upperclassmen were reportedly earning more money. Crabb, The Amateurism Myth: A Case for a New Tradition, 28 Stan. L. & Pol'y Rev. 181, 190 (2017). In the 1940s, Hugh McElhenny, a halfback at the University of Washington, "became known as the first college player 'ever to take a cut in salary to play pro football.'" Zimbalist 22-23. He reportedly said: "'[A] wealthy guy puts big bucks under my pillow every time I score a touchdown. Hell, I can't afford to graduate.'" Id., at 211, n. 17. In 1946, a commentator offered this view: "[W]hen it comes to chicanery, double-dealing, and general undercover work behind the scenes, big-time college football is in a class by itself." Woodward, Is College Football on the Level?, Sport, Nov. 1946, Vol. 1, No. 3, p. 35.

In 1948, the NCAA sought to do more than admonish. It adopted the "Sanity Code." Colleges Adopt the 'Sanity Code' To Govern Sports, N.Y. Times, Jan. 11, 1948, p. 1, col. 1. The code reiterated the NCAA's opposition to "promised pay in any form." Hearings before the Subcommittee on Oversight and Investigations of the House Committee on Interstate and Foreign Commerce, 95th Congress, 2d Sess., pt. 2, p. 1094 (1978). But for the first time the code also authorized colleges and universities to pay athletes' tuition. And it created a new enforcement mechanism—providing for the "suspension or expulsion" of "proven offenders." Colleges Adopt 'Sanity Code,' N. Y. Times, p. 1, col. 1. To some, these changes sought to substitute a consistent, above-board compensation system for the varying under-the-table schemes that had long proliferated. To others, the code marked "the beginning of the NCAA behaving as an effective cartel," by enabling its member schools to set and enforce "rules that limit the price they have to pay for their inputs (mainly the 'student-athletes')." Zimbalist 10.

The rules regarding student-athlete compensation have evolved ever since. In 1956, the NCAA expanded the scope of allowable payments to include room, board, books, fees, and "cash for incidental expenses such as laundry." In re *National Collegiate Athletic Assn. Athletic Grant-in-Aid Cap Antitrust Litig.*, 375 F.Supp.3d 1058, 1063 (ND Cal. 2019) (hereinafter D.Ct.Op.). In 1974, the NCAA began permitting paid professionals in one sport to compete on an amateur basis in another. In 2014, the NCAA "announced it would allow athletic conferences to authorize their member schools to increase scholarships up to the full cost of attendance." *O'Bannon v. National Collegiate Athletic Assn.*, 802 F.3d 1049, 1054-1055 (CA9 2015). The 80 member schools of the "Power Five" athletic conferences—the conferences with the highest revenue in Division I—promptly voted to raise their scholarship limits to an amount that is generally several thousand dollars higher than previous limits. *D.Ct.Op.*, at 1064.

In recent years, changes have continued. The NCAA has created the "Student Assistance Fund" and the "Academic Enhancement Fund" to "assist student-athletes in meeting financial needs," "improve their welfare or academic support," or "recognize academic achievement." Id., at 1072. These funds have supplied money to student-athletes for "postgraduate scholarships" and "school supplies," as well as "benefits that are not related to education," such as "loss-of-value insurance premiums," "travel expenses," "clothing," and "magazine subscriptions." Id., at 1072, n. 15. In 2018, the NCAA made more than $84 million available through the Student Activities Fund and more than $48 million available through the Academic Enhancement Fund. Id., at 1072. Assistance may be provided in cash or in kind, and there is no limit to the amount any particular student-athlete may receive. Id., at 1073. Since 2015, disbursements to individual students have sometimes been tens of thousands of dollars above the full cost of attendance. Ibid.

The NCAA has also allowed payments "'incidental to athletics participation,'" including awards for "participation or achievement in athletics" (like "qualifying for a bowl game") and certain "payments from outside entities" (such as for "performance in the Olympics"). Id., at 1064, 1071, 1074. The NCAA permits its member schools to award up to (but no more than) two annual "Senior Scholar Awards" of $10,000 for students to attend graduate school after their athletic eligibility expires. Id., at 1074. Finally, the NCAA allows schools to fund travel for student-athletes' family members to attend "certain events." Id., at 1069. ***

The NCAA's current broadcast contract for the March Madness basketball tournament is worth $1.1 billion annually. See id., at 1077, n. 20. Its television deal for the FBS conference's College Football Playoff is worth approximately $470 million per year. See id., at 1063; Bachman, ESPN Strikes Deal for College Football Playoff, Wall Street Journal, Nov. 21, 2012. Beyond these sums, the Division I conferences earn substantial revenue from regular-season games. For example, the Southeastern Conference (SEC) "made more than $409 million in revenues from television contracts alone in 2017, with its total conference revenues exceeding $650 million that year." *D.Ct.Op.*, at 1063. All these amounts have "increased consistently over the years." Ibid.

Those who run this enterprise profit in a different way than the student-athletes whose activities they oversee. The president of the NCAA earns nearly $4 million per year. Commissioners of the top conferences take home between $2 to $5 million. College athletic directors average more than $1 million annually. And annual salaries for top Division I college football coaches approach $11 million, with some of their assistants making more than $2.5 million.

B

The plaintiffs are current and former student-athletes in men's Division I FBS football and men's and women's Division I basketball. They filed a class action against the NCAA and 11 Division I conferences (for simplicity's sake, we refer to the defendants collectively as the NCAA). The student-athletes challenged the "current, interconnected set of NCAA rules that limit the compensation they may receive in exchange for their athletic services." *D.Ct.Op.*, at 1062, 1065, n. 5. Specifically, they alleged that the NCAA's rules violate §1 of the Sherman Act, which prohibits "contract[s], combination[s], or conspirac[ies] in restraint of trade or commerce." 15 U.S.C. §1.

After pretrial proceedings stretching years, the district court conducted a 10-day bench trial. It heard experts and lay witnesses from both sides, and received volumes of evidence and briefing, all before issuing an exhaustive decision. *** In applying the rule of reason, the district court began by observing that the NCAA enjoys "near complete dominance of, and exercise[s] monopsony power in, the relevant market"—which it defined as the market for "athletic services in men's and women's Division I basketball and FBS football, wherein each class member participates in his or her sport-specific market." *D.Ct.Op.*, at 1097. The "most talented athletes are concentrated" in the "markets for Division I basketball and FBS football." Id., at 1067. There are no "viable substitutes," as the "NCAA's Division I essentially is the relevant market for elite college football and basketball." Id., at 1067, 1070. In short, the NCAA and its member schools have the "power to restrain student-athlete compensation in any way and at any time they wish, without any meaningful risk of diminishing their market dominance." Id., at 1070.

The district court then proceeded to find that the NCAA's compensation limits "produce significant anticompetitive effects in the relevant market." Id., at 1067. Though member schools compete fiercely in recruiting student-athletes, the NCAA uses its monopsony power to "cap artificially the compensation offered to recruits." Id., at 1097. In a market without the challenged restraints, the district court found, "competition among schools would increase in terms of the compensation they would offer to recruits, and student-athlete compensation would be higher as a result." Id., at 1068. "Student-athletes would receive offers that would more closely match the value of their athletic services." Ibid. And notably, the court observed, the NCAA "did not meaningfully dispute" any of this evidence. Id., at 1067; see also Tr. of Oral Arg. 31 ("[T]here's no dispute that the—the no-pay-for-play rule imposes a significant restraint on a relevant antitrust market").

The district court next considered the NCAA's procompetitive justifications for its restraints. The NCAA suggested that its restrictions help increase output in college sports and maintain a competitive balance among teams. But the district court rejected those justifications, *D.Ct.Op.*, at 1070, n. 12, and the NCAA does not pursue them here. The NCAA's only remaining defense was that its rules preserve amateurism, which in turn widens consumer choice by providing a unique product—amateur college sports as distinct from professional sports. Admittedly, this asserted benefit accrues to consumers in the NCAA's seller-side consumer market rather than to student-athletes whose compensation the NCAA fixes in its buyer-side labor market. But, the NCAA argued, the district court needed to assess its restraints in the labor market in light of their procompetitive benefits in the consumer market—and the district court agreed to do so. Id., at 1098.

Turning to that task, the court observed that the NCAA's conception of amateurism has changed steadily over the years. The court noted that the NCAA "nowhere define[s] the nature of the amateurism they claim consumers insist upon." *D.Ct.Op.*, at 1070. And, given all this, the court struggled to ascertain for itself "any coherent definition" of the term, id., at 1074, noting the testimony of a former SEC commissioner that he's "'never been clear on . . . what is really meant by amateurism.'" Id., at 1070-1071.

Nor did the district court find much evidence to support the NCAA's contention that its compensation restrictions play a role in consumer demand. As the court put it, the evidence failed "to establish that the challenged compensation rules, in and of themselves, have any direct connection to consumer demand." Id., at 1070. *** At the same time, however, the district court did find that one particular aspect of the NCAA's compensation limits "may have some effect in preserving consumer demand." Id., at 1082. Specifically, the court found that rules aimed at ensuring "student-athletes do not receive unlimited payments unrelated to education" could play some role in product differentiation with professional sports and thus help sustain consumer demand for college athletics. Id., at 1083.

The court next required the student-athletes to show that "substantially less restrictive alternative rules" existed that "would achieve the same procompetitive effect as the challenged set of rules." Id., at 1104. The district court emphasized that the NCAA must have "ample latitude" to run its enterprise and that courts "may not use antitrust laws to make marginal adjustments to broadly reasonable market restraints." Ibid. (internal quotation marks omitted). In light of these standards, the court found the student-athletes had met their burden in some respects but not others. The court rejected the student-athletes' challenge to NCAA rules that limit athletic scholarships to the full cost of attendance and that restrict compensation and benefits unrelated to education. These may be price-fixing agreements, but the court found them to be reasonable in light of the possibility that "professional-level cash payments. . . could blur the distinction between college sports and professional sports and thereby negatively affect consumer demand." Ibid.

The court reached a different conclusion for caps on education-related benefits—such as rules that limit scholarships for graduate or vocational school, payments for academic tutoring, or paid posteligibility internships. Id., at 1088. On no account, the court found, could such education-related benefits be "confused with a professional athlete's salary." Id., at 1083. If anything, they "emphasize that the recipients are students." Ibid. Enjoining the NCAA's restrictions on these forms of compensation alone, the court concluded, would be substantially less restrictive than the NCAA's current rules and yet fully capable of preserving consumer demand for college sports. Id., at 1088.

The court then entered an injunction reflecting its findings and conclusions. Nothing in the order precluded the NCAA from continuing to fix compensation and benefits unrelated to education; limits on athletic scholarships, for example, remained untouched. The court enjoined the NCAA only from limiting education-related compensation or benefits that conferences and schools may provide to student-athletes playing Division I football and basketball. App. to Pet.

for Cert. in No. 20-512, p. 167a, ¶1. The court's injunction further specified that the NCAA could continue to limit cash awards for academic achievement—but only so long as those limits are no lower than the cash awards allowed for athletic achievement (currently $5,980 annually). The court added that the NCAA and its members were free to propose a definition of compensation or benefits "'related to education.'" App. to Pet. for Cert. in No. 20-512, at 168a, ¶4. And the court explained that the NCAA was free to regulate how conferences and schools provide education-related compensation and benefits. The court further emphasized that its injunction applied only to the NCAA and multi-conference agreements—thus allowing individual conferences (and the schools that constitute them) to impose tighter restrictions if they wish. Id., at 169a, ¶6. The district court's injunction issued in March 2019, and took effect in August 2020.

Both sides appealed. The student-athletes said the district court did not go far enough; it should have enjoined all of the NCAA's challenged compensation limits, including those "untethered to education," like its restrictions on the size of athletic scholarships and cash awards. *In re National Collegiate Athletic Assn. Athletic Grant-in-Aid Cap Antitrust Litig.*, 958 F.3d 1239, 1263 (CA9 2020). The NCAA, meanwhile, argued that the district court went too far by weakening its restraints on education-related compensation and benefits. In the end, the court of appeals affirmed in full, explaining its view that "the district court struck the right balance in crafting a remedy that both prevents anticompetitive harm to Student-Athletes while serving the procompetitive purpose of preserving the popularity of college sports." Ibid.

C

Unsatisfied with this result, the NCAA asks us to reverse to the extent the lower courts sided with the student-athletes. For their part, the student-athletes do not renew their across-the-board challenge to the NCAA's compensation restrictions. Accordingly, we do not pass on the rules that remain in place or the district court's judgment upholding them. Our review is confined to those restrictions now enjoined.

Before us, as through much of the litigation below, some of the issues most frequently debated in antitrust litigation are uncontested. The parties do not challenge the district court's definition of the relevant market. They do not contest that the NCAA enjoys monopoly (or, as it's called on the buyer side, monopsony) control in that labor market—such that it is capable of depressing wages below competitive levels and restricting the quantity of student-athlete labor. Nor does the NCAA dispute that its member schools compete fiercely for student-athletes but remain subject to NCAA-issued-and-enforced limits on what compensation they can offer. Put simply, this suit involves admitted horizontal price fixing in a market where the defendants exercise monopoly control.

Other significant matters are taken as given here too. No one disputes that the NCAA's restrictions in fact decrease the compensation that student-athletes receive compared to what a competitive market would yield. No one questions either that decreases in compensation also depress participation by student-athletes in the relevant labor market—so that price and quantity are both suppressed. Nor does the NCAA suggest that, to prevail, the plaintiff student-athletes must show that its restraints harm competition in the seller-side (or consumer facing) market as well as in its buyer-side (or labor) market.

Meanwhile, the student-athletes do not question that the NCAA may permissibly seek to justify its restraints in the labor market by pointing to procompetitive effects they produce in the consumer market. Some amici argue that "competition in input markets is incommensurable with competition in output markets," and that a court should not "trade off" sacrificing a legally cognizable interest in competition in one market to better promote competition in a different one; review should instead be limited to the particular market in which antitrust plaintiffs have asserted their injury. Brief for American Antitrust Institute as Amicus Curiae 3, 11-12. But the parties before us do not pursue this line.

II

A

With all these matters taken as given, we express no views on them. Instead, we focus only on the objections the NCAA does raise. Principally, it suggests that the lower courts erred by subjecting its compensation restrictions to a rule of reason analysis. In the NCAA's view, the courts should have given its restrictions at most an "abbreviated deferential review," Brief for Petitioner in No. 20-512, p. 14, or a "'quick look,'" Brief for Petitioners in No. 20-520, p. 18, before approving them. ***

The NCAA accepts that its members collectively enjoy monopsony power in the market for student-athlete services, such that its restraints can (and in fact do) harm competition. See *D.Ct.Op.*, at 1067. Unlike customers who would look elsewhere when a small van company raises its prices above market levels, the district court found (and the NCAA does not here contest) that student-athletes have nowhere else to sell their labor. Even if the NCAA is a joint venture, then, it is hardly of the sort that would warrant quick-look approval for all its myriad rules and restrictions.

Nor does the NCAA's status as a particular type of venture categorically exempt its restraints from ordinary rule of reason review. We do not doubt that some degree of coordination between competitors within sports leagues can be procompetitive. Without some agreement among rivals—on things like how many players may be on the field or the time allotted for play—the very competitions that consumers value would not be possible. See *Board of Regents*, 468 U.S., at 101 (quoting R. Bork, The Antitrust Paradox 278 (1978)). Accordingly, even a sports league with market power might see some agreements among its members win antitrust approval in the "'twinkling of an eye.'" *American Needle*, 560 U.S., at 203.

But this insight does not always apply. That some restraints are necessary to create or maintain a league sport does not mean all "aspects of elaborate interleague cooperation are." Id., at 199, n. 7. While a quick look will often be enough to approve the restraints "necessary to produce a game," ibid., a fuller review may be appropriate for others.

The NCAA's rules fixing wages for student-athletes fall on the far side of this line. Nobody questions that Division I basketball and FBS football can proceed (and have proceeded) without the education-related compensation restrictions the district court enjoined; the games go on. Instead, the parties dispute whether and to what extent those restrictions in the NCAA's labor market yield benefits in its consumer market that can be attained using substantially less restrictive means. That dispute presents complex questions requiring more than a blink to answer.

B

Even if background antitrust principles counsel in favor of the rule of reason, the NCAA replies that a particular precedent ties our hands. The NCAA directs our attention to *Board of Regents*, where this Court considered the league's rules restricting the ability of its member schools to televise football games. 468 U.S., at 94. *** Given the sensitivity of antitrust analysis to market realities—and how much has changed in this market—we think it would be particularly unwise to treat an aside in *Board of Regents* as more than that. ***

C

The NCAA submits that a rule of reason analysis is inappropriate for still another reason—because the NCAA and its member schools are not "commercial enterprises" and instead oversee intercollegiate athletics "as an integral part of the undergraduate experience." The NCAA represents that it seeks to "maintain amateurism in college sports as part of serving [the] societally important non-commercial objective" of "higher education." Id., at 3.

Here again, however, there may be less of a dispute than meets the eye. The NCAA does not contest that its restraints affect interstate trade and commerce and are thus subject to the Sherman Act. *** Nor, on the other side of the equation, does anyone contest that the status of the NCAA's members as schools and the status of student-athletes as students may be relevant in assessing consumer demand as part of a rule of reason review.

With this much agreed it is unclear exactly what the NCAA seeks. To the extent it means to propose a sort of judicially ordained immunity from the terms of the Sherman Act for its restraints of trade—that we should overlook its restrictions because they happen to fall at the intersection of higher education, sports, and money—we cannot agree. ***

III

A

While the NCAA devotes most of its energy to resisting the rule of reason in its usual form, the league lodges some objections to the district court's application of it as well. When describing the rule of reason, this Court has sometimes spoken of "a three-step, burden-shifting framework" as a means for "'distinguish[ing] between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest.'" *American Express Co.,* 585 U.S., at ___ (slip op., at 9). As we have described it, "the plaintiff has the initial burden to prove that the challenged restraint has a substantial anticompetitive effect." Ibid. Should the plaintiff carry that burden, the burden then "shifts to the defendant to show a procompetitive rationale for the restraint." Ibid. If the defendant can make that showing, "the burden shifts back to the plaintiff to demonstrate that the procompetitive efficiencies could be reasonably achieved through less anticompetitive means." Id., at ___-___ (slip op., at 9-10). ***

In the proceedings below, the district court followed circuit precedent to apply a multistep framework closely akin to *American Express's.* As its first step, the district court required the student-athletes to show that "the challenged restraints produce significant anticompetitive effects in the relevant market." *D.Ct.Op.*, at 1067. This was no slight burden. According to one amicus, courts have disposed of nearly all rule of reason cases in the last 45 years on the ground that the plaintiff failed to show a substantial anticompetitive effect. Brief for 65 Professors of Law, Business, Economics, and Sports Management as Amici Curiae 21, n. 9 ("Since 1977, courts decided 90% (809 of 897) on this ground"). This suit proved different. As we have seen, based on a voluminous record, the district court held that the student-athletes had shown the NCAA enjoys the power to set wages in the market for student-athletes' labor—and that the NCAA has exercised that power in ways that have produced significant anticompetitive effects.

See *D.Ct.Op.*, at 1067. Perhaps even more notably, the NCAA "did not meaningfully dispute" this conclusion. Ibid.

Unlike so many cases, then, the district court proceeded to the second step, asking whether the NCAA could muster a procompetitive rationale for its restraints. Id., at 1070. This is where the NCAA claims error first crept in. On its account, the district court examined the challenged rules at different levels of generality. At the first step of its inquiry, the court asked whether the NCAA's entire package of compensation restrictions has substantial anticompetitive effects collectively. Yet, at the second step, the NCAA says the district court required it to show that each of its distinct rules limiting student-athlete compensation has procompetitive benefits individually. The NCAA says this mismatch had the result of effectively—and erroneously—requiring it to prove that each rule is the least restrictive means of achieving the procompetitive purpose of differentiating college sports and preserving demand for them.

We agree with the NCAA's premise that antitrust law does not require businesses to use anything like the least restrictive means of achieving legitimate business purposes. *** Even worse, "[r]ules that seek to embody every economic complexity and qualification may well, through the vagaries of administration, prove counter-productive, undercutting the very economic ends they seek to serve." *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 234 (CA1 1983) (BREYER, J.). After all, even "[u]nder the best of circumstances," applying the antitrust laws "'can be difficult'"—and mistaken condemnations of legitimate business arrangements "'are especially costly, because they chill the very'" procompetitive conduct "'the antitrust laws are designed to protect.'" *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 414 (2004). ***

While we agree with the NCAA's legal premise, we cannot say the same for its factual one. Yes, at the first step of its inquiry, the district court held that the student-athletes had met their burden of showing the NCAA's restraints collectively bear an anticompetitive effect. And, given that, yes, at step two the NCAA had to show only that those same rules collectively yield a procompetitive benefit. The trouble for the NCAA, though, is not the level of generality. It is the fact that the district court found unpersuasive much of its proffered evidence. See *D.Ct.Op.*, at 1070-1076, 1080-1083. Recall that the court found the NCAA failed "to establish that the challenged compensation rules . . . have any direct connection to consumer demand." Id., at 1070.

***[W]e see nothing about the district court's analysis that offends the legal principles the NCAA invokes. The court's judgment ultimately turned on the key question at the third step: whether the student-athletes could prove that "substantially less restrictive alternative rules" existed to achieve the same procompetitive benefits the NCAA had proven at the second step. Ibid. Of course, deficiencies in the NCAA's proof of procompetitive benefits at the second step influenced the analysis at the third. But that is only because, however framed and at whichever step, anticompetitive restraints of trade may wind up flunking the rule of reason to the extent the evidence shows that substantially less restrictive means exist to achieve any proven procompetitive benefits.

Simply put, the district court nowhere—expressly or effectively—required the NCAA to show that its rules constituted the least restrictive means of preserving consumer demand. Rather, it was only after finding the NCAA's restraints "'patently and inexplicably stricter than is necessary'" to achieve the procompetitive benefits the league had demonstrated that the district court proceeded to declare a violation of the Sherman Act. *D.Ct.Op.*, at 1104. That demanding standard hardly presages a future filled with judicial micromanagement of legitimate business decisions.

B

In a related critique, the NCAA contends the district court "impermissibly redefined" its "product" by rejecting its views about what amateurism requires and replacing them with its preferred conception. Brief for Petitioner in No. 20-512, at 35-36.

This argument, however, misapprehends the way a defendant's procompetitive business justification relates to the antitrust laws. Firms deserve substantial latitude to fashion agreements that serve legitimate business interests—agreements that may include efforts aimed at introducing a new product into the marketplace. But none of that means a party can relabel a restraint as a product feature and declare it "immune from §1 scrutiny." *American Needle*, 560 U.S., at 199, n. 7. ***

The NCAA's argument not only misapprehends the inquiry, it would require us to overturn the district court's factual findings. While the NCAA asks us to defer to its conception of amateurism, the district court found that the NCAA had not adopted any consistent definition. Instead, the court found, the NCAA's rules and restrictions on compensation have shifted markedly over time. The court found, too, that the NCAA adopted these restrictions without any reference to "considerations of consumer demand," id., at 1100, and that some were "not necessary to preserve consumer demand," id., at 1075, 1080, 1104. None of this is product redesign; it is a straightforward application of the rule of reason.

C

Finally, the NCAA attacks as "indefensible" the lower courts' holding that substantially less restrictive alternatives exist capable of delivering the same procompetitive benefits as its current rules. Brief for Petitioner in No. 20-512, at 46. The NCAA claims, too, that the district court's injunction threatens to "micromanage" its business. Id., at 50.

Once more, we broadly agree with the legal principles the NCAA invokes. As we have discussed, antitrust courts must give wide berth to business judgments before finding liability. Similar considerations apply when it comes to the remedy. Judges must be sensitive to the possibility that the "continuing supervision of a highly detailed decree" could wind up impairing rather than enhancing competition. *Trinko*, 540 U.S., at 415. Costs associated with ensuring compliance with judicial decrees may exceed efficiencies gained; the decrees themselves may unintentionally suppress procompetitive innovation and even facilitate collusion. Judges must be wary, too, of the temptation to specify "the proper price, quantity, and other terms of dealing"—cognizant that they are neither economic nor industry experts. *Trinko*, 540 U.S., at 408. Judges must be open to reconsideration and modification of decrees in light of changing market realities, for "what we see may vary over time." *California Dental*, 526 U.S., at 781. And throughout courts must have a healthy respect for the practical limits of judicial administration: "An antitrust court is unlikely to be an effective day-to-day enforcer" of a detailed decree, able to keep pace with changing market dynamics alongside a busy docket. *Trinko*, 540 U.S., at 415. Nor should any court "'impose a duty . . . that it cannot explain or adequately and reasonably supervise.'" Ibid. In short, judges make for poor "central planners" and should never aspire to the role. Id., at 408.

Once again, though, we think the district court honored these principles. The court enjoined only restraints on education-related benefits—such as those limiting scholarships for graduate school, payments for tutoring, and the like. The court did so, moreover, only after finding that relaxing these restrictions would not blur the distinction between college and professional sports and thus impair demand—and only after finding that this course represented a significantly (not marginally) less restrictive means of achieving the same procompetitive benefits as the NCAA's current rules.

Even with respect to education-related benefits, the district court extended the NCAA considerable leeway. As we have seen, the court provided that the NCAA could develop its own definition of benefits that relate to education and seek modification of the court's injunction to reflect that definition. The court explained that the NCAA and its members could agree on rules regulating how conferences and schools go about providing these education-related benefits. The court said that the NCAA and its members could continue fixing education-related cash awards, too—so long as those "limits are never lower than the limit" on awards for athletic performance. *D.Ct.Op.*, at 1104. And the court emphasized that its injunction applies only to the NCAA and multiconference agreements; individual conferences remain free to reimpose every single enjoined restraint tomorrow—or more restrictive ones still.

In the end, it turns out that the NCAA's complaints really boil down to three principal objections.

First, the NCAA worries about the district court's inclusion of paid posteligibility internships among the education-related benefits it approved. The NCAA fears that schools will use internships as a way of circumventing limits on payments that student-athletes may receive for athletic performance. *** The court refused to enjoin NCAA rules prohibiting its members from providing compensation or benefits unrelated to legitimate educational activities—thus leaving the league room to police phony internships. As we've observed, the district court also allowed the NCAA to propose (and enforce) rules defining what benefits do and do not relate to education. Accordingly, the NCAA may seek whatever limits on paid internships it thinks appropriate. And, again, the court stressed that individual conferences may restrict internships however they wish. All these features underscore the modesty of the current decree.

Second, the NCAA attacks the district court's ruling that it may fix the aggregate limit on awards schools may give for "academic or graduation" achievement no lower than its aggregate limit on parallel athletic awards (currently $5,980 per year). *D.Ct.Op.*, at 1104. This, the NCAA asserts, "is the very definition of a professional salary." Brief for Petitioner in No. 20-512, at 48. The NCAA also represents that "[m]ost" of its currently permissible athletic awards are "for genuine individual or team achievement" and that "[m]ost . . . are received by only a few student-athletes each year." Ibid. Meanwhile, the NCAA says, the district court's decree would allow a school to pay players thousands of dollars each year for minimal achievements like maintaining a passing GPA.

The basis for this critique is unclear. The NCAA does not believe that the athletic awards it presently allows are tantamount to a professional salary. And this portion of the injunction sprang directly from the district court's finding that the cap on athletic participation awards "is an amount that has been shown not to decrease consumer demand." *D.Ct.Op.*, at 1088. Indeed, there was no evidence before the district court suggesting that corresponding academic awards would impair consumer interest in any way. Again, too, the district court's injunction affords the NCAA leeway. It leaves the NCAA free to reduce its athletic awards. And it does not ordain what criteria schools must use for their academic and graduation awards. So, once more, if the

NCAA believes certain criteria are needed to ensure that academic awards are legitimately related to education, it is presently free to propose such rules—and individual conferences may adopt even stricter ones.

Third, the NCAA contends that allowing schools to provide in-kind educational benefits will pose a problem. This relief focuses on allowing schools to offer scholarships for "graduate degrees" or "vocational school" and to pay for things like "computers" and "tutoring." App. to Pet. for Cert. in No. 20-512, at 167a-168a, ¶2. But the NCAA fears schools might exploit this authority to give student-athletes "'luxury cars'" "to get to class" and "other unnecessary or inordinately valuable items" only "nominally" related to education. Brief for Petitioner in No. 20-512, at 48-49.

Again, however, this over-reads the injunction in ways we have seen and need not belabor. Under the current decree, the NCAA is free to forbid in-kind benefits unrelated to a student's actual education; nothing stops it from enforcing a "no Lamborghini" rule. And, again, the district court invited the NCAA to specify and later enforce rules delineating which benefits it considers legitimately related to education. To the extent the NCAA believes meaningful ambiguity really exists about the scope of its authority—regarding internships, academic awards, in-kind benefits, or anything else—it has been free to seek clarification from the district court since the court issued its injunction three years ago. The NCAA remains free to do so today. To date, the NCAA has sought clarification only once—about the precise amount at which it can cap academic awards—and the question was quickly resolved. Before conjuring hypothetical concerns in this Court, we believe it best for the NCAA to present any practically important question it has in district court first.

When it comes to fashioning an antitrust remedy, we acknowledge that caution is key. Judges must resist the temptation to require that enterprises employ the least restrictive means of achieving their legitimate business objectives. Judges must be mindful, too, of their limitations—as generalists, as lawyers, and as outsiders trying to understand intricate business relationships. Judges must remain aware that markets are often more effective than the heavy hand of judicial power when it comes to enhancing consumer welfare. And judges must be open to clarifying and reconsidering their decrees in light of changing market realities. Courts reviewing complex business arrangements should, in other words, be wary about invitations to "set sail on a sea of doubt." *United States v. Addyston Pipe & Steel Co.*, 85 F.271, 284 (CA6 1898) (Taft, J.). But we do not believe the district court fell prey to that temptation. Its judgment does not float on a sea of doubt but stands on firm ground—an exhaustive factual record, a thoughtful legal analysis consistent with established antitrust principles, and a healthy dose of judicial humility.

*

***

The judgment is Affirmed.

JUSTICE KAVANAUGH, concurring: *** I join the Court's excellent opinion in full. But this case involves only a narrow subset of the NCAA's compensation rules—namely, the rules restricting the education-related benefits that student athletes may receive, such as post-eligibility scholarships at graduate or vocational schools. The rest of the NCAA's compensation rules are not at issue here and therefore remain on the books. Those remaining compensation rules generally restrict student athletes from receiving compensation or benefits from their colleges for playing sports. And those rules have also historically restricted student athletes from receiving money from endorsement deals and the like.

I add this concurring opinion to underscore that the NCAA's remaining compensation rules also raise serious questions under the antitrust laws. Three points warrant emphasis.

First, the Court does not address the legality of the NCAA's remaining compensation rules. *** Second, although the Court does not weigh in on the ultimate legality of the NCAA's remaining compensation rules, the Court's decision establishes how any such rules should be analyzed going forward. After today's decision, the NCAA's remaining compensation rules should receive ordinary "rule of reason" scrutiny under the antitrust laws. *** Third, there are serious questions whether the NCAA's remaining compensation rules can pass muster under ordinary rule of reason scrutiny. Under the rule of reason, the NCAA must supply a legally valid procompetitive justification for its remaining compensation rules. As I see it, however, the NCAA may lack such a justification.

The NCAA acknowledges that it controls the market for college athletes. The NCAA concedes that its compensation rules set the price of student athlete labor at a below-market rate. And the NCAA recognizes that student athletes currently have no meaningful ability to negotiate with the NCAA over the compensation rules.

The NCAA nonetheless asserts that its compensation rules are procompetitive because those rules help define the product of college sports. Specifically, the NCAA says that colleges may decline to pay student athletes because the defining feature of college sports, according to the NCAA, is that the student athletes are not paid.

In my view, that argument is circular and unpersuasive. The NCAA couches its arguments for not paying student athletes in innocuous labels. But the labels cannot disguise the reality: The NCAA's business model would be flatly illegal in almost any other industry in America. All of the restaurants in a region cannot come together to cut cooks' wages on the theory that "customers prefer" to eat food from low-paid cooks. Law firms cannot conspire to cabin lawyers' salaries in the name of providing legal services out of a "love of the law." Hospitals cannot agree to cap nurses' income in order to create a "purer" form of helping the sick. News organizations cannot join forces to curtail pay to reporters to preserve a "tradition" of public-minded journalism. Movie studios cannot collude to slash benefits to camera crews to kindle a "spirit of amateurism" in Hollywood.

Price-fixing labor is price-fixing labor. And price-fixing labor is ordinarily a textbook antitrust problem because it extinguishes the free market in which individuals can otherwise obtain fair compensation for their work. See, e.g., *Texaco Inc. v. Dagher*, 547 U.S. 1, 5 (2006). Businesses like the NCAA cannot avoid the consequences of price-fixing labor by incorporating price-fixed labor into the definition of the product. Or to put it in more doctrinal terms, a monopsony cannot launder its price-fixing of labor by calling it product definition.

The bottom line is that the NCAA and its member colleges are suppressing the pay of student athletes who collectively generate billions of dollars in revenues for colleges every year. Those enormous sums of money flow to seemingly everyone except the student athletes. College presidents, athletic directors, coaches, conference commissioners, and NCAA executives take in six- and seven-figure salaries. Colleges build lavish new facilities. But the student athletes who generate the revenues, many of whom are African American and from lower-income backgrounds, end up with little or nothing. See Brief for African American Antitrust Lawyers as Amici Curiae 13-17.

Everyone agrees that the NCAA can require student athletes to be enrolled students in good standing. But the NCAA's business model of using unpaid student athletes to generate billions of dollars in revenue for the colleges raises serious questions under the antitrust laws. In particular, it is highly questionable whether the NCAA and its member colleges can justify not paying student athletes a fair share of the revenues on the circular theory that the defining characteristic of college sports is that the colleges do not pay student athletes. And if that asserted justification is unavailing, it is not clear how the NCAA can legally defend its remaining compensation rules.

If it turns out that some or all of the NCAA's remaining compensation rules violate the antitrust laws, some difficult policy and practical questions would undoubtedly ensue. Among them: How would paying greater compensation to student athletes affect non-revenue-raising sports? Could student athletes in some sports but not others receive compensation? How would any compensation regime comply with Title IX? If paying student athletes requires something like a salary cap in some sports in order to preserve competitive balance, how would that cap be administered? And given that there are now about 180,000 Division I student athletes, what is a financially sustainable way of fairly compensating some or all of those student athletes?

Of course, those difficult questions could be resolved in ways other than litigation. Legislation would be one option. Or colleges and student athletes could potentially engage in collective bargaining (or seek some other negotiated agreement) to provide student athletes a fairer share of the revenues that they generate for their colleges, akin to how professional football and basketball players have negotiated for a share of league revenues. Cf. *Brown v. Pro Football, Inc.*, 518 U.S. 231, 235-237 (1996); *Wood v. National Basketball Assn.*, 809 F. 2d 954, 958-963 (CA2 1987) (R. Winter, J.). Regardless of how those issues ultimately would be resolved, however, the NCAA's current compensation regime raises serious questions under the antitrust laws.

To be sure, the NCAA and its member colleges maintain important traditions that have become part of the fabric of America—game days in Tuscaloosa and South Bend; the packed gyms in Storrs and Durham; the women's and men's lacrosse championships on Memorial Day weekend; track and field meets in Eugene; the spring softball and baseball World Series in Oklahoma City and Omaha; the list goes on. But those traditions alone cannot justify the NCAA's decision to build a massive money-raising enterprise on the backs of student athletes who are not fairly compensated. Nowhere else in America can businesses get away with agreeing not to pay their workers a fair market rate on the theory that their product is defined by not paying their workers a fair market rate. And under ordinary principles of antitrust law, it is not evident why college sports should be any different. The NCAA is not above the law.

Polygram Holding, Inc. v. Federal Trade Commission

416 F.3d 29 (D.C. Cir. 2005)

GINSBURG, CHIEF JUDGE. PolyGram Holding, Inc. and several of its affiliates petition for review of an order of the Federal Trade Commission holding PolyGram violated § 5 of the Federal Trade Commission Act, 15 U.S.C. § 45. As detailed below, PolyGram entered into an agreement with Warner Communications, Inc. to distribute the recording of a concert to be given by "The Three Tenors" in 1998. The two companies later entered into a separate agreement to suspend, for ten weeks, advertising and discounting of two earlier Three Tenors concert albums, one distributed by PolyGram and the other by Warner. The Commission held the latter agreement unlawful and prohibited PolyGram from entering into any similar agreement in the future. We agree with the Commission that, although not a per se violation of antitrust law, the agreement was presumptively unlawful and PolyGram failed to rebut that presumption. We therefore deny PolyGram's petition for review.

I. Background

Here are the facts as found by the Commission in its order and opinion of July 28, 2003. See *In re PolyGram Holding, Inc.* . . . The Three Tenors—José Carreras, Placido Domingo, and Luciano Pavarotti—put on spectacular concerts coinciding with the World Cup soccer finals in 1990, 1994, and 1998. PolyGram distributed the recording of the 1990 concert, which became one of the best-selling classical albums of all time. Warner distributed the 1994 concert album, which also met with great success. Both albums remained on the top-ten classical list throughout 1994, 1995, and 1996.

In late 1997 PolyGram and Warner agreed jointly to distribute the recording of The Three Tenors' July 1998 concert. Warner, which had the worldwide rights, retained the United States rights but licensed to PolyGram the exclusive right to distribute the 1998 album outside the United States, and the companies agreed to share equally the worldwide profit or loss on the project. The agreement also obligated PolyGram and Warner to consult with one another on all "marketing and promotional activities" for the 1998 concert album, but each company was free ultimately to pursue its own marketing strategy and to continue exploiting its earlier Three Tenors concert album without limitation. The agreement also provided that PolyGram and Warner would collaborate on the distribution of any future Three Tenors album released through August 2002.

Representatives of PolyGram and Warner first met in January 1998 to discuss "marketing and operational issues." One of PolyGram's representatives voiced concern about the effect of marketing the earlier Three Tenors albums upon the prospects for the 1998 concert album and suggested the two companies impose an "advertising moratorium" surrounding the 1998 release, which was scheduled for August 1. According to notes of their next meeting (in March) PolyGram and Warner representatives agreed that "a big push" on the earlier albums "shouldn't take place before November 15." After that meeting, each company instructed its affiliates to cease all promotion of the 1990 and 1994 Three Tenors albums for approximately six weeks, beginning in late July or early August.

Apparently Warner's overseas division did not get the message because in May it announced an aggressive marketing campaign, scheduled to run through December, to discount and to promote the 1994 album throughout Europe. When PolyGram learned of this, it threatened to "retaliate" by cutting the price of its 1990 album. Accusations then flew between the two companies about which had started the imminent price war. Meanwhile, in June the promoter of The Three Tenors concert informed PolyGram and Warner that the repertoire for the 1998 concert would substantially overlap those of the 1990 and 1994 concerts, which in the view of both PolyGram and Warner executives jeopardized the commercial viability of the forthcoming concert album.

By the time The Three Tenors performed in Paris on July 10, PolyGram and Warner had exchanged letters reaffirming their commitment to suspend advertising and discounting the 1990 and 1994 concert albums and agreeing the moratorium would run from August 1 through October 15. About a week later, however, PolyGram's Senior Marketing Director, who had passed on the details of the agreement to PolyGram's General Counsel, sent a memorandum around the company stating, "Contrary to any previous suggestion, there has been no agreement with [Warner] in relation to the pricing and marketing of the previous Three Tenors albums." Warner followed suit on August 10, sending a letter to PolyGram repudiating any pricing or advertising restrictions relative to its 1994 album. At the same time, however, PolyGram and Warner executives privately assured one another their respective companies intended to honor the agreement, and in fact the companies did substantially comply with the agreement through October 15, 1998.

In 2001 the Commission issued complaints against PolyGram and Warner charging that, by entering into the moratorium agreement, the companies had engaged in an unfair method of competition in violation of § 5 of the FTC Act. Warner soon consented to an order barring it from making any similar agreement in the future. PolyGram contested the charge and, after a trial, an Administrative Law Judge ruled that PolyGram had violated § 5 and ordered PolyGram, like Warner, to refrain from making any similar agreement in the future.

The Commission affirmed the order of the ALJ. . . . [U]pon closer inspection, the Commission confirmed its initial conclusion that the moratorium agreement was an unreasonable restraint of trade in violation of § 1 of the Sherman Act and, hence, an unfair method of competition in violation of § 5 of the FTC Act.

II. Analysis

PolyGram raises four objections to the decision of the Commission: First, the Commission should not have rejected the free-rider justification as legally insufficient because the moratorium agreement had a legitimate, procompetitive purpose reasonably related to the joint venture. Second, the Commission was required to show the restraints actually harmed competition before it could require PolyGram to proffer a competitive justification. Third, the Commission's findings concerning the competitive impact of the restraint were not supported by substantial evidence. Finally, there is no danger the same conduct will recur, so the Commission's prohibitory remedy is unreasonable.

The Commission's findings of fact are conclusive if supported by substantial evidence. See 15 U.S.C. § 45(c). The legal issues are "for the courts to resolve, although even in considering such issues the courts are to give some deference to the Commission's informed judgment that a particular commercial practice is to be condemned as 'unfair.' " *FTC v. Ind. Fed'n of Dentists,* 476 U.S. 447, 454 (1987) (*IFD*).

The Supreme Court's approach to evaluating a § 1 claim has gone through a transition over the last twenty-five years, from a dichotomous categorical approach to a more nuanced and case-specific inquiry. In 1978, just before the transition began, the Court summarized its doctrine as follows:

> There are . . . two complementary categories of antitrust analysis. In the first category are agreements whose nature and necessary effect are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality—they are "illegal per se." In the second category are agreements whose competitive effect can only be evaluated by analyzing the facts particular to the business, the history of the restraint, and the reasons why it was imposed.

Nat'l Soc'y of Prof'l Eng'rs v. FTC, 435 U.S. 679, 692 (1978).

Courts and commentators have recognized the trade-offs inherent in each category. Per se analysis, which requires courts to generalize about the utility of a challenged practice, reduces the cost of decision-making but correspondingly raises the total cost of error by making it more likely some practices will be held unlawful in circumstances where they are harmless or even procompetitive. See, *e.g., Arizona v. Maricopa County Med. Soc.,* 457 U.S. 332, 344 (1982) ("For the sake of business certainty and litigation efficiency, we have tolerated the invalidation of some agreements that a full-blown inquiry might have proved to be reasonable"); Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law, ¶ 1509c (2d ed. 2003) (observing that per se analysis "dispenses with costly proof requirements, such as proof of market power," but consequently "produces a certain number of false positives"). The converse-increased litigation cost but reduced cost of error-obtains under the rule of reason, which requires an exhaustive inquiry into all the myriad factors "bearing on whether the conduct is on balance anticompetitive or procompetitive." Donald F. Turner, *The Durability, Relevance, and Future of American Antitrust Policy,* 75 Cal. L. Rev. 797, 800 (1987); see Frank H. Easterbrook, *The Limits of Antitrust,* 63 Tex. L. Rev. 1, 12–13 (1984) ("When everything is relevant, nothing is dispositive . . . . Litigation costs are the product of vague rules combined with high stakes, and nowhere is that combination more deadly than in antitrust litigation under the Rule of Reason").

Since *Professional Eng'rs*, the Supreme Court has steadily moved away from the dichotomous approach—under which every restraint of trade is either unlawful per se, and hence not susceptible to a procompetitive justification, or subject to full-blown rule-of-reason analysis—toward one in which the extent of the inquiry is tailored to the suspect conduct in each particular case. For instance, the Court did not hold unlawful per se an agreement limiting the number of football games each participating college could sell to television, which agreement was challenged in *NCAA v. Board of Regents,* 468 U.S. 85, 100 (1984) (recognizing but declining to apply doctrine that "[h]orizontal price-fixing and output limitation are ordinarily condemned as a matter of law under an 'illegal per se' approach"); or the refusal of an organization of dentists to provide x-rays to dental insurers, which was at issue in *IFD,* 476 U.S. at 458 ("Although this Court has in the past stated that group boycotts are unlawful per se, we decline to resolve this case by forcing the Federation's policy into the 'boycott' pigeonhole and invoking the per se rule") (citations omitted). Compare, *e.g., United States v. Socony-Vacuum Oil Co.,* 310 U.S. 150 (1940) (price-fixing per se unlawful); and *Klor's, Inc. v. Broadway-Hale Stores, Inc.,* 359 U.S. 207 (1959) (group boycott per se unlawful).

At the same time, however, in *NCAA* and *IFD* the Court did not insist upon the elaborate market analysis ordinarily required under the rule of reason to prove the defendant had market power and the restraint it imposed had an anticompetitive effect. See *NCAA,* 468 U.S. at 109 (rule of reason analysis unnecessary in light of district court's finding price and output not responsive to demand); *IFD,* 476 U.S. at 459 ("While this is not price-fixing as such, no elaborate industry analysis is required to demonstrate the anticompetitive character of such an agreement"). The Court instead adopted an intermediate inquiry, since dubbed the "quick look," to evaluate horizontal restraints of trade. *See, e.g.,* Areeda & Hovenkamp, Antitrust Law, ¶ 1911a.

It would be somewhat misleading, however, to say the "quick look" is just a new category of analysis intermediate in complexity between "per se" condemnation and full-blown "rule of reason" treatment, for that would suggest the Court has moved from a dichotomy to a trichotomy, when in fact it has backed away from any reliance upon fixed categories and toward a continuum. The Court said as much in *California Dental Ass'n v. FTC:*

> The truth is that our categories of analysis of anticompetitive effect are less fixed than terms like "per se," "quick look," and "rule of reason" tend to make them appear. We have recognized, for example, that there is often no bright line separating per se from Rule of Reason analysis, since considerable inquiry into market conditions may be required before the application of any so-called "per se" condemnation is justified.

526 U.S. 756, 779 (1999).

Rather than focusing upon the category to which a particular restraint should be assigned, therefore, the Court emphasized the basic point that under § 1 the essential inquiry is "whether . . . the challenged restraint enhances competition." *Id.* at 779–80 (quoting *NCAA,* 468 U.S. at

104). In order to make that determination, a court must make "an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint," *id.* at 781, which in some cases may not require a full-blown market analysis. The Court continued:

> The object is to see whether the experience of the market has been so clear, or necessarily will be, that a confident conclusion about the principal tendency of a restriction will follow from a quick (or at least quicker) look, in place of a more sedulous one. And of course what we see may vary over time, if rule-of-reason analyses in case after case reach identical conclusions.

Id.; cf. United States v. Microsoft, 253 F.3d 34, 84 (D.C. Cir. 2001) (declining to condemn per se tying arrangements involving platform software products because there was "no close parallel in prior antitrust cases" and "simplistic application of per se tying rules carries a serious risk of harm").

In this case, as we have said, the Commission analyzed PolyGram's conduct under the legal framework it had devised in *Mass. Board* (1988), which it maintains is consistent with the Supreme Court's teaching of more than a decade later in *California Dental* (1999). The *Mass. Board* analysis proceeds in several distinct steps: First, the Commission must determine whether it is obvious from the nature of the challenged conduct that it will likely harm consumers. If so, then the restraint is deemed "inherently suspect" and, unless the defendant comes forward with some plausible (and legally cognizable) competitive justification for the restraint, summarily condemned. "Such justifications," the Commission explained, "may consist of plausible reasons why practices that are competitively suspect as a general matter may not be expected to have adverse consequences in the context of the particular market in question, or they may consist of reasons why the practices are likely to have beneficial effects for consumers."

If the defendant does offer such an explanation, then the Commission "must address the justification" in one of two ways. First, the Commission may explain why it can confidently conclude, without adducing evidence, that the restraint very likely harmed consumers. Alternatively, the Commission may provide the tribunal with sufficient evidence to show that anticompetitive effects are in fact likely. If the Commission succeeds in either way, then the evidentiary burden shifts to the defendant to show the restraint in fact does not harm consumers or has "procompetitive virtues" that outweigh its burden upon consumers.

PolyGram argues the Commission's framework conflicts with Supreme Court precedent by condemning a restraint that is not per se illegal without the Commission having to prove the restraint actually harms competition. According to PolyGram, "proof of actual anticompetitive effect (or market power as its surrogate) is required in *any* Rule of Reason case."

For reasons we have already explained, we reject PolyGram's attempt to locate the appropriate analysis, and the concomitant burden of proof, by reference to the vestigial line separating per se analysis from the rule of reason. See Areeda & Hovenkamp, Antitrust Law, ¶ 1511a ("judges and litigants too often assume erroneously that the classification, per se or rule of reason, necessarily determines what must or may be alleged and proved, made the subject of detailed findings, or submitted to the jury"). At bottom, the Sherman Act requires the court to ascertain whether the challenged restraint hinders competition; the Commission's framework, at least as the Commission applied it in this case, does just that.

We therefore accept the Commission's analytical framework. If, based upon economic learning and the experience of the market, it is obvious that a restraint of trade likely impairs competition, then the restraint is presumed unlawful and, in order to avoid liability, the defendant must either identify some reason the restraint is unlikely to harm consumers or identify some competitive benefit that plausibly offsets the apparent or anticipated harm. That much follows from the caselaw; for instance, in *NCAA* the Court held that a "naked restraint on price and output requires some competitive justification even in the absence of a detailed market analysis." 468 U.S. at 110. Similarly, in *IFD*, the Supreme Court ruled a horizontal agreement to withhold services could not be sustained because the dentists failed to advance any "credible argument" that "some countervailing procompetitive virtue . . . [redeemed] an agreement limiting consumer choice by impeding the 'ordinary give and take of the market place.'" 476 U.S. at 459; see also *California Dental,* 526 U.S. at 771 (remanding for closer look at challenged advertising restrictions after concluding they "might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition").

Although the Commission uses the term "inherently suspect" to describe those restraints that judicial experience and economic learning have shown to be likely to harm consumers, we note that, under the Commission's own framework, the rebuttable presumption of illegality arises not necessarily from anything "inherent" in a business practice but from the close family resemblance between the suspect practice and another practice that already stands convicted in the court of consumer welfare. The Commission appears to acknowledge, as it must, that as economic learning and market experience evolve, so too will the class of restraints subject to summary adjudication. See *California Dental,* 526 U.S. at 781 (the ability of a court to draw "a confident conclusion about the principal tendency of a restraint . . . may vary over time, if rule-of-reason analyses in case after case reach identical conclusions"); see also *Broadcast Music, Inc. v. CBS,* 441 U.S. 1, 9 (1979) ("it is only after considerable experience with certain business relationships that courts classify them as per se violations"). See generally Industrial Concentration: The New Learning (Harvey J. Goldschmid, H. Michael Mann, J. Fred Weston, eds., 1974).

That said, we have no difficulty with the Commission's conclusion that PolyGram's agreement with Warner in all likelihood had a deleterious effect upon consumers—unless, that is, PolyGram comes forward with some plausible explanation to the contrary. An agreement between joint venturers to restrain price cutting and advertising with respect to products not part of the joint venture looks suspiciously like a naked price-fixing agreement between competitors, which would ordinarily be condemned as per se unlawful. The Supreme Court has recognized time and again that agreements restraining autonomy in pricing and advertising impede the "ordinary give and take of the market place." *IFD,* 476 U.S. at 459; see also *NCAA,* 468 U.S. at 107 ("[r]estrictions on price and output are the paradigmatic examples of restraints of trade that the Sherman Act was intended to prohibit"); *Bates v. State Bar of Ariz.,* 433 U.S. 350, 364 (1977) (advertising "serves to inform the public of the availability, nature, and prices of products and services, and thus performs an indispensable role in the allocation of resources in a free enterprise system").

PolyGram's fate in this case therefore rests upon the plausibility of the sole competitive justification it proffered for the moratorium agreement, namely, that the restrictions on discounting and advertising enhanced the long-term profitability of all three concert albums and promoted the "Three Tenors" brand. According to PolyGram, each company was concerned the other would "free ride" on the promotional activities of the joint venture by promoting its own earlier concert album; as a result fewer Three Tenors albums would be sold overall and the joint venture would be less likely to create future products, such as a "greatest hits" album or a boxed set. Thus, PolyGram likens the moratorium agreement here to the restraint at issue in *Polk Brothers, Inc. v. Forest City Enterprises,* 776 F.2d 185 (7th Cir.1985), where two potential retail competitors collaborated to build a store offering some of each company's products but agreed not to sell competing products at the new store. Because the restraint arguably promoted productivity and output by controlling each participant's ability to free-ride on the other's promotional efforts, the court, rather than condemning the restraint summarily, went on to evaluate it under the rule of reason. *Id.* at 190.

At first glance PolyGram's contention has some force; the moratorium appears likely to have mitigated the "spillover" effects that could be expected to follow an aggressive launch of the 1998 album. Absent the moratorium, that is, a consumer, after learning of the new album through the joint venture's advertising, might decide that he would be just as happy with an older concert album, especially if the older album were then available at a discount. The "free-riding" to be eliminated by the moratorium agreement, however, was nothing more than the competition of products that were not part of the joint undertaking. Why not an agreement by which PolyGram and Warner would eliminate advertising and price competition on all their records for a time while they focused exclusively upon promoting the new Three Tenors album? The "procompetitive" justification PolyGram offers is "nothing less than a frontal assault on the basic policy of the Sherman Act." *National Soc'y of Prof'l Eng'rs,* 435 U.S. at 695.

To take the Commission's example, if General Motors were vigorously to advertise the release of a new model SUV, other SUV manufacturers would no doubt reap some of the benefit of GM's efforts. But that would not mean General Motors and its competitors could lawfully agree to restrict prices and advertising on existing SUV models in return for General Motors giving its rivals a share of its profit on the new model. Nor would an agreement to restrain prices and advertising on existing SUVs be lawful if General Motors were to release the new model SUV as a joint venture with one of its competitors. *Id.* at 45. A restraint cannot be justified solely on the ground that it increases the profitability of the enterprise that introduces the new product, regardless whether that enterprise is a joint venture or a solo undertaking. And it simply does not matter whether the new SUV would have been profitable absent the restraint; if the only way a new product can profitably be introduced is to restrain the legitimate competition of older products, then one must seriously wonder whether consumers are genuinely benefitted by the new product. As the Supreme Court said in *Catalano, Inc. v. Target Sales, Inc.,* 446 U.S. 643, 649 (1980),

> in any case in which competitors are able to increase the price level or to curtail production by agreement, it could be argued that the agreement has the effect of making the market more attractive to potential new entrants. If that potential justifies horizontal agreements among competitors imposing one kind of voluntary restraint or another on their competitive freedom, it would seem to follow that the more successful an agreement is in raising the price level, the safer it is from antitrust attack. Nothing could be more inconsistent with our cases. . . .

In sum, because PolyGram has failed to identify any competitive justification for its agreement with Warner to refrain from advertising or discounting their competitive Three Tenors products, we hold it violated § 5 of the FTC Act. Hence, we need not go on to determine whether the Commission's findings of fact concerning actual competitive harm are supported by substantial evidence.

Finally, we hold the remedy ordered by the Commission was reasonable. The Commission found there was a significant risk that, if not prohibited from doing so, PolyGram would enter into similar arrangements in the future. That determination is supported by substantial evidence. The record shows the condition that gave rise to the moratorium agreement—namely, the company "fear[ed] that a new release by one of [its] recording artists may lose sales to the artist's older albums owned by a competitor,"—is a recurrent one in the record industry; therefore, PolyGram would have the same incentive in the future to enter into other agreements to restrain advertising and price discounting.

III. Conclusion

For the foregoing reasons, PolyGram's petition for review is *Denied.*

Standard Fashion Co. v. Magrane-Houston Co.
258 U.S. 346 (1922)

MR. JUSTICE DAY delivered the opinion of the Court: Petitioner brought suit in the United States District Court for the District of Massachusetts to restrain the respondent from violating a certain contract concerning the sale of patterns for garments worn by women and children, called standard patterns. The bill was dismissed by the District Court and its decree was affirmed by the Circuit Court of Appeals.

Petitioner is a New York corporation engaged in the manufacture and distribution of patterns. Respondent conducted a retail dry goods business at the corner of Washington street and Temple place in the city of Boston. On November 14, 1914, the parties entered into a contract by which the petitioner granted to the respondent an agency for the sale of standard patterns at respondent's store, for a term of two years from the date of the contract, and from term to term thereafter until the agreement should be terminated as thereinafter provided. *** Respondent agreed to purchase a substantial number of standard fashion sheets, to purchase and keep on hand at all times, except during the period of exchange, $1,000 value in standard patterns at net invoice price, and to pay petitioner for the pattern stock to be selected by it on terms of payment which are stated. Respondent agreed not to assign or transfer the agency, or to remove it from its original location, without the written consent of the petitioner, and not to sell or permit to be sold on its premises during the term of the contract any other make of patterns, and not to sell standard patterns except at labeled prices. Respondent agreed to permit petitioner to take account of pattern stock whenever it desired, to pay proper attention to the sale of standard patterns, to conserve the best interests of the agency at all times, and to reorder promptly as patterns were sold. Either party desiring to terminate the agreement was required to give the other party 3 months' notice in writing within 30 days after the expiration of any contract period, the agency to continue during such 3 months. Upon expiration of such notice respondent agreed to promptly return to petitioner all standard patterns, and petitioner agreed to credit respondent for the same on receipt in good order at three-fourths cost. ***

The principal question in the case, and the one upon which the writ of certiorari was granted, involves the construction of section 3 of the Clayton Act. That section, so far as pertinent here, provides:

> "It shall be unlawful * * * to * * * make a sale or contract for sale of goods * * * or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods * * * of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

The contract contains an agreement that the respondent shall not sell or permit to be sold on its premises during the term of the contract any other make of patterns. It is shown that on or about July 1, 1917, the respondent discontinued the sale of the petitioner's patterns and placed on sale in its store patterns of a rival company known as the McCall Company.

It is insisted by the petitioner that the contract is not one of sale, but is one of agency or joint venture; but an analysis of the contract shows that a sale was in fact intended and made. It is provided that patterns returned for exchange must have been purchased from the petitioner. Respondent agreed to purchase a certain number of patterns. Upon expiration of the notice of termination the respondent agreed to promptly return all standard patterns bought under the contract. In the event of the disposition of the business property of the respondent at Washington street and Temple place, the respondent might deliver its stock of standard patterns to the petitioner for repurchase under the repurchase clause of the contract.

Full title and dominion passed to the buyer. While this contract is denominated one of agency, it is perfectly apparent that it is one of sale. The contract required the purchaser not to deal in goods of competitors of the seller. It is idle to say that the covenant was limited to the premises of the purchaser, and that sales might be made by it elsewhere. The contract should have a reasonable construction. The purchaser kept a retail store in Boston. It was not contemplated that it would make sales elsewhere. The covenant, read in the light of the circumstances in which it was made, is one by which the purchaser agreed not to sell any other make of patterns while the contract was in force. The real question is: Does the contract of sale come within the third section of the Clayton Act, because the covenant not to sell the patterns of others "may be to substantially lessen competition or tend to create a monopoly"?

The Clayton Act, as its title and the history of its enactment discloses, was intended to supplement the purpose and effect of other anti-trust legislation, principally the Sherman Act of 1890. The latter act had been interpreted by this court to apply to contracts, combinations and conspiracies which unduly obstruct the free and natural flow of commerce. ***

As the Sherman Act was usually administered, when a case was made out, it resulted in a decree dissolving the combination, sometimes with unsatisfactory results so far as the purpose to maintain free competition was concerned.

The Clayton Act sought to reach the agreements embraced within its sphere in their incipiency, and in the section under consideration to determine their legality by specific tests of its own which declared illegal contracts of sale made upon the agreement or understanding that the purchaser shall not deal in the goods of a competitor or competitors of the seller, which "may substantially lessen competition or tend to create a monopoly."

*** Section 3 condemns sales or agreement where the effect of such sale or contract of sale "may" be to substantially lessen competition or tend to create monopoly. It thus deals with consequences to follow the making of the restrictive covenant limiting the right of the purchaser to deal in the goods of the seller only. But we do not think that the purpose in using the word "may" was to prohibit the mere possibility of the consequences described. It was intended to prevent such agreements as would under the circumstances disclosed probably lessen competition, or create an actual tendency to monopoly. That it was not intended to reach every remote lessening of competition is shown in the requirement that such lessening must be substantial.

Both courts below found that the contract interpreted in the light of the circumstances surrounding the making of it was within the provisions of the Clayton Act as one which substantially lessened competition and tended to create monopoly. These courts put special stress upon the fact found that of 52,000 so-called pattern agencies in the entire country, the petitioner, or its holding company controlling it and two other pattern companies, approximately controlled two-fifths of such agencies. As the Circuit Court of Appeals, summarizing the matter, pertinently observed:

> "The restriction of each merchant to one pattern manufacturer must in hundreds, perhaps in thousands, of small communities amount to giving such single pattern manufacturer a monopoly of the business in such community. Even in the larger cities, to limit to a single pattern maker the pattern business of dealers most resorted to by customers

> whose purchases tend to give fashions their vogue, may tend to facilitate further combinations; so that the plaintiff, or some other aggressive concern, instead of controlling two-fifths, will shortly have almost, if not quite, all the pattern business."

We agree with these conclusions, and have no doubt that the contract, properly interpreted, with its restrictive covenant, brings it fairly within the section of the Clayton Act under consideration.

Affirmed.

Northwest Wholesale Stationers, Inc., v. Pacific Stationery and Printing Co.

472 U.S. 284 (1985)

JUSTICE BRENNAN delivered the opinion of the Court: This case requires that we decide whether a *per se* violation of § 1 of the Sherman Act occurs when a cooperative buying agency comprising various retailers expels a member without providing any procedural means for challenging the expulsion. The case also raises broader questions as to when *per se* antitrust analysis is appropriately applied to joint activity that is susceptible of being characterized as a concerted refusal to deal.

I

*** Petitioner Northwest Wholesale Stationers is a purchasing cooperative made up of approximately 100 office supply retailers in the Pacific Northwest States. The cooperative acts as the primary wholesaler for the retailers. Retailers that are not members of the cooperative can purchase wholesale supplies from Northwest at the same price as members. At the end of each year, however, Northwest distributes its profits to members in the form of a percentage rebate on purchases. Members therefore effectively purchase supplies at a price significantly lower than do nonmembers. Northwest also provides certain warehousing facilities. The cooperative arrangement thus permits the participating retailers to achieve economies of scale in purchasing and warehousing that would otherwise be unavailable to them. In fiscal 1978 Northwest had $5.8 million in sales.

Respondent Pacific Stationery & Printing Co. sells office supplies at both the retail and wholesale levels. Its total sales in fiscal 1978 were approximately $7.6 million; the record does not indicate what percentage of revenue is attributable to retail and what percentage is attributable to wholesale. Pacific became a member of Northwest in 1958. In 1974 Northwest amended its bylaws to prohibit members from engaging in both retail and wholesale operations. A grandfather clause preserved Pacific's membership rights. In 1977 ownership of a controlling share of the stock of Pacific changed hands, and the new owners did not officially bring this change to the attention of the directors of Northwest. This failure to notify apparently violated another of Northwest's bylaws.

In 1978 the membership of Northwest voted to expel Pacific. Most factual matters relevant to the expulsion are in dispute. No explanation for the expulsion was advanced at the time, and Pacific was given neither notice, a hearing, nor any other opportunity to challenge the decision. Pacific argues that the expulsion resulted from Pacific's decision to maintain a wholesale operation. Northwest contends that the expulsion resulted from Pacific's failure to notify the cooperative members of the change in stock ownership. *** It is undisputed that Pacific received approximately $10,000 in rebates from Northwest in 1978, Pacific's last year of membership.

Beyond a possible inference of loss from this fact, however, the record is devoid of allegations indicating the nature and extent of competitive injury the expulsion caused Pacific to suffer. ***

The Court of Appeals for the Ninth Circuit reversed, holding "that the uncontroverted facts of this case support a finding of *per se* liability." 715 F.2d 1393, 1395 (1983). The court reasoned that the cooperative's expulsion of Pacific was an anticompetitive concerted refusal to deal with Pacific on equal footing, which would be a *per se* violation of § 1 in the absence of any specific legislative mandate for self-regulation sanctioning the expulsion. ***

II

The decision of the cooperative members to expel Pacific was certainly a restraint of trade in the sense that every commercial agreement restrains trade. Whether this action violates § 1 of the Sherman Act depends on whether it is adjudged an *unreasonable* restraint. Rule-of-reason analysis guides the inquiry, unless the challenged action falls into the category of "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." *Northern Pacific R. Co. v. United States*, 356 U.S. 1, 5.

This *per se* approach permits categorical judgments with respect to certain business practices that have proved to be predominantly anticompetitive. Courts can thereby avoid the "significant costs" in "business certainty and litigation efficiency" that a full-fledged rule-of-reason inquiry entails. *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 343-344 (1982). The decision to apply the *per se* rule turns on "whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output ... or instead one designed to 'increase economic efficiency and render markets more, rather than less, competitive.' " *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 19-20 (1979) (citations omitted).

This Court has long held that certain concerted refusals to deal or group boycotts are so likely to restrict competition without any offsetting efficiency gains that they should be condemned as *per se* violations of § 1 of the Sherman Act. See *Klor's, Inc. v. Broadway-Hale Stores, Inc.,* 359 U.S. 207 (1959); *Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.,* 364 U.S. 656 (1961); *Associated Press v. United States,* 326 U.S. 1 (1945); *Fashion Originators' Guild of America, Inc. v. FTC,* 312 U.S. 457 (1941). The question presented in this case is whether Northwest's decision to expel Pacific should fall within this category of activity that is conclusively presumed to be anticompetitive. The Court of Appeals held that the exclusion of Pacific from the cooperative should conclusively be presumed unreasonable on the ground that Northwest provided no procedural protections to Pacific. Even if the lack of procedural protections does not justify a conclusive presumption of predominantly anticompetitive effect, the mere act of expulsion of a competitor from a wholesale cooperative might be argued to be sufficiently likely to have such effects under the present circumstances and therefore to justify application of the *per se* rule. These possibilities will be analyzed separately.

*** B

This case therefore turns *** on whether the decision to expel Pacific is properly viewed as a group boycott or concerted refusal to deal mandating *per se* invalidation. "Group boycotts" are often listed among the classes of economic activity that merit *per se* invalidation under § 1. See *Klor's, Inc. v. Broadway-Hale Stores, Inc.,* 359 U.S., at 212. Exactly what types of activity fall within the forbidden category is, however, far from certain. "[T]here is more confusion about the scope and operation of the *per se* rule against group boycotts than in reference to any other aspect of the *per se* doctrine." L. Sullivan, Law of Antitrust 229-230 (1977). ***

Cases to which this Court has applied the *per se* approach have generally involved joint efforts by a firm or firms to disadvantage competitors by "either directly denying or persuading or coercing suppliers or customers to deny relationships the competitors need in the competitive struggle." Sullivan, *supra*, at 261-262. See, *e.g., Radiant Burners, Inc. v. Peoples Gas Light & Coke Co.,* 364 U.S. 656 (1961) (denial of necessary certification of product); *Associated Press v. United States*, 326 U.S. 1 (1945) (denial of important sources of news); *Klor's, Inc., supra* (denial of wholesale supplies). In these cases, the boycott often cut off access to a supply, facility, or market necessary to enable the boycotted firm to compete*; Radiant Burners, Inc., supra,* and frequently the boycotting firms possessed a dominant position in the relevant market. *E.g., Associated Press, supra; Fashion Originators' Guild of America, Inc. v. FTC,* 312 U.S. 457 (1941). In addition, the practices were generally not justified by plausible arguments that they were intended to enhance overall efficiency and make markets more competitive. Under such circumstances the likelihood of anticompetitive effects is clear and the possibility of countervailing procompetitive effects is remote.

Although a concerted refusal to deal need not necessarily possess all of these traits to merit *per se* treatment, not every cooperative activity involving a restraint or exclusion will share with the *per se* forbidden boycotts the likelihood of predominantly anticompetitive consequences. ***

Wholesale purchasing cooperatives such as Northwest are not a form of concerted activity characteristically likely to result in predominantly anticompetitive effects. Rather, such cooperative arrangements would seem to be "designed to increase economic efficiency and render markets more, rather than less, competitive." *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc., supra,* 441 U.S., at 20. The arrangement permits the participating retailers to achieve economies of scale in both the purchase and warehousing of wholesale supplies, and also ensures ready access to a stock of goods that might otherwise be unavailable on short notice. The cost savings and order-filling guarantees enable smaller retailers to reduce prices and maintain their retail stock so as to compete more effectively with larger retailers.

Pacific, of course, does not object to the existence of the cooperative arrangement, but rather raises an antitrust challenge to Northwest's decision to bar Pacific from continued membership. It is therefore the action of expulsion that must be evaluated to determine whether *per se* treatment is appropriate. The act of expulsion from a wholesale cooperative does not necessarily imply anticompetitive animus and thereby raise a probability of anticompetitive effect. See *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc., supra*, at 9. Wholesale purchasing cooperatives must establish and enforce reasonable rules in order to function effectively. Disclosure rules, such as the one on which Northwest relies, may well provide the cooperative with a needed means for monitoring the creditworthiness of its members. Nor would the expulsion characteristically be likely to result in predominantly anticompetitive effects, at least in the type of situation this case presents. Unless the cooperative possesses market power or exclusive access to an element essential to effective competition, the conclusion that expulsion is virtually always likely to have an anticompetitive effect is not warranted. Absent such a showing with respect to a cooperative buying arrangement, courts should apply a rule-of-reason analysis. At no time has Pacific made a threshold showing that these structural characteristics are present in this case.

The District Court appears to have followed the correct path of analysis—recognizing that not all concerted refusals to deal should be accorded *per se* treatment and deciding this one should not. The foregoing discussion suggests, however, that a satisfactory threshold determination whether anticompetitive effects would be likely might require a more detailed factual picture of market structure than the District Court had before it. Nonetheless, in our judgment the District Court's rejection of *per se* analysis in this case was correct. A plaintiff seeking application of the *per se* rule must present a threshold case that the challenged activity falls into a category likely to have predominantly anticompetitive effects. The mere allegation of a concerted refusal to deal does not suffice because not all concerted refusals to deal are predominantly anticompetitive. When the plaintiff challenges expulsion from a joint buying cooperative, some showing must be made that the cooperative possesses market power or unique access to a business element necessary for effective competition. Focusing on the argument that the lack of procedural safeguards required *per se* liability, Pacific did not allege any such facts. Because the Court of Appeals applied an erroneous *per se* analysis in this case, the court never evaluated the District Court's rule-of-reason analysis rejecting Pacific's claim. A remand is therefore appropriate for the limited purpose of permitting appellate review of that determination. ***

Leegin Creative Leather Products, Inc. v. PSKS, Inc.

551 U.S. 877 (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." 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."

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." 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." 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. ***

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. "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. 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). ***

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, 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. 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.

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. *** 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. 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. 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. 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. 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. 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. 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.

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. 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.

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. 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); H. Hovenkamp, The Antitrust Enterprise: Principle and Execution 186 (2005) (hereinafter Hovenkamp) (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. 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. 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. 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. 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. 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. 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. Respondent is mistaken in relying on pricing effects absent a further showing of anticompetitive conduct. For, as has been indicated already, the antitrust laws are designed primarily to protect interbrand competition, from which lower prices can later result. 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.

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. 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." See *GTE Sylvania*, 433 U.S., at 52, n. 19. 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, The Law and Economics of Resale Price Maintenance, 13 Rev. Indus. Org. 57, 67 (1998) (hereinafter Mathewson & Winter).

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. 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. Resale price maintenance should be subject to more careful scrutiny, by contrast, if many competing manufacturers adopt 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. If, by contrast, a manufacturer adopted the policy independent of retailer pressure, the restraint is less likely to promote anticompetitive conduct. 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. 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.

Stare decisis is not as significant in this case, however, because the issue before us is the scope of 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). 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. 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. In the antitrust context the fact that a decision has been "called into serious question" justifies our reevaluation of it. *Khan*, *supra*, at 21.

*** The Court's treatment of vertical restraints has progressed away from *Dr. Miles'* strict approach. *** 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)). 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). ***

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. 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. The economic effects of unilateral and concerted price setting are in general the same. 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. Even with the stringent standards in *Monsanto* and *Business Electronics*, this danger can lead, and has led, rational manufacturers to take wasteful measures. 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. 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. 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.

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. 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.

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). 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. ***

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, 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. ***

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

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

It is so ordered.

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

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.

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. 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.

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. 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%.

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").

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. 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. 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. 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.

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. 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. 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.

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."

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. 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, 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.

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." 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. 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. 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 over-ruling an earlier case have been met. See also *Federal Election Comm'n v. Wisconsin Right to Life, Inc.*, --- U.S. ----, 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. 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.

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.

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.

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. 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. 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.

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. 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. 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. 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. 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. 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.*, --- U.S. at ---- (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. 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*, --- U.S., at ---- (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.

Third, the fact that a decision creates an "unworkable" legal regime argues in favor of overruling. 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*, --- U.S., at ---- (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*, --- U.S., at --- - ---- (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. 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. The Executive Branch argued for repeal on the assumption that *Dr. Miles* stated the law. 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). 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*.

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. That figure in today's economy equals just over $300 billion. 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. 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*. 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*. And Congress had nowhere expressed support for *Albrecht's* rule.

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. ***

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 over-ruling a recent constitutional decision, *Wisconsin Right to Life, Inc.*, --- U.S., at ---- - ---- (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.

United States v. Apple, Inc.

791 F.3d 290 (2nd Cir. 2015)

DEBRA ANN LIVINGSTON, CIRCUIT JUDGE: Since the invention of the printing press, the distribution of books has involved a fundamentally consistent process: compose a manuscript, print and bind it into physical volumes, and then ship and sell the volumes to the public. In late 2007, Amazon.com, Inc. ("Amazon") introduced the Kindle, a portable device that carries digital copies of books, known as "ebooks." This innovation had the potential to change the centuries-old process for producing books by eliminating the need to print, bind, ship, and store them. Amazon began to popularize the new way to read, and encouraged consumers to buy the Kindle by offering desirable books—new releases and *New York Times* bestsellers—for $9.99. Publishing companies, which have traditionally stood at the center of the multi-billion dollar book-producing industry, saw Amazon's ebooks, and particularly its $9.99 pricing, as a threat to their way of doing business.

By November 2009, Apple, Inc. ("Apple") had plans to release a new tablet computer, the iPad. Executives at the company saw an opportunity to sell ebooks on the iPad by creating a virtual marketplace on the device, which came to be known as the "iBookstore." Working within a tight timeframe, Apple went directly into negotiations with six of the major publishing companies in the United States. In two months, it announced that five of those companies—Hachette, Harpercollins, Macmillan, Penguin, and Simon & Schuster (collectively, the "Publisher Defendants")—had agreed to sell ebooks on the iPad under arrangements whereby the publishers had the authority to set prices, and could set the prices of new releases and *New York Times* bestsellers as high as $19.99 and $14.99, respectively. Each of these agreements, by virtue of its terms, resulted in each Publisher Defendant receiving *less* per ebook sold via Apple as opposed to Amazon, even given the higher consumer prices. Just a few months after the iBookstore opened, however, every one of the Publisher Defendants had taken control over pricing from Amazon and had raised the prices on many of their ebooks, most notably new releases and bestsellers.

The United States Department of Justice ("DOJ" or "Justice Department") and 33 states and territories (collectively, "Plaintiffs") filed suit in the United States District Court for the Southern District of New York, alleging that Apple, in launching the iBookstore, had conspired with the Publisher Defendants to raise prices across the nascent ebook market. This agreement, they argued, violated § 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 *et seq.* ("Sherman Act"), and state antitrust laws. All five Publisher Defendants settled and signed consent decrees, which prohibited them, for a period, from restricting ebook retailers' ability to set prices. Then, after a three-week bench trial, the district court (Cote, J.) concluded that, in order to induce the Publisher Defendants to participate in the iBookstore and to avoid the necessity of itself competing with Amazon over the retail price of ebooks, Apple orchestrated a conspiracy among the Publisher Defendants to raise the price of ebooks—particularly new releases and *New York Times* bestsellers. *United States v. Apple Inc.*, 952 F. Supp. 2d 638, 647 (S.D.N.Y. 2013). The district court found that the agreement constituted a *per se* violation of the Sherman Act and, in the alternative, unreasonably restrained trade under the rule of reason. On September 5, 2013, the district court entered final judgment on the liability finding and issued an injunctive order that, *inter alia*, prevents Apple from entering into agreements with the Publisher Defendants that restrict its ability to set, alter, or reduce the price of ebooks, and requires Apple to apply the same terms and conditions to ebook applications sold on its devices as it does to other applications.

On appeal, Apple contends that the district court's liability finding was erroneous and that the provisions of the injunction related to its pricing authority and ebook applications are not necessary to protect the public. *** Because we conclude that the district court did not err in deciding that Apple violated § 1 of the Sherman Act, and because we also conclude that the district court's injunction was lawful and consistent with preventing future anticompetitive harms, we affirm.

BACKGROUND

I. Factual Background

We begin not with Kindles and iPads, but with printed "trade books," which are "general interest fiction and non-fiction" books intended for a broad readership. *Apple*, 952 F. Supp. 2d at 648 n.4. In the United States, the six largest publishers of trade books, known in the publishing world as the "Big Six," are Hachette, HarperCollins, Macmillan, Penguin, Random House, and Simon & Schuster. Together, the Big Six publish many of the biggest names in fiction and nonfiction; during 2010, their titles accounted for over 90% of the *New York Times* bestsellers in the United States. *Id.* at 648 n.5.

For decades, trade book publishers operated under a fairly consistent business model. When a new book was ready for release to the public, the publisher would sell hardcover copies to retailers at a "wholesale" price and recommend resale to consumers at a markup, known as the "list" price. After the hardcover spent enough time on the shelves—often a year—publishers would release a paperback copy at lower "list" and "wholesale" prices. In theory, devoted readers would pay the higher hardcover price to read the book when it first came out, while more casual fans would wait for the paperback.

A. Amazon's Kindle

On November 19, 2007, Amazon released the Kindle: a portable electronic device that allows consumers to purchase, download, and read ebooks. At the time, there was only one other ereader available in the emerging ebook market, and Amazon's Kindle quickly gained traction. In 2007, ebook revenue in North America was only $70 million, a tiny amount relative to the approximately $30 billion market for physical trade books. *** Amazon followed a "wholesale" business model similar to the one used with print books: publishers recommended a digital list price and received a wholesale price for each ebook that Amazon sold. In exchange, Amazon could sell the publishers' ebooks on the Kindle and determine the retail price. At least early on, publishers tended to recommend a digital list price that was about 20% lower than the print list price to reflect the fact that, with an ebook, there is no cost for printing, storing, packaging, shipping, or returning the books.

Where Amazon departed from the publishers' traditional business model was in the sale of new releases and *New York Times* bestsellers. Rather than selling more expensive versions of these books upon initial release (as publishers encouraged by producing hardcover books before paperback copies), Amazon set the Kindle price at one, stable figure—$9.99. At this price, Amazon was selling "certain" new releases and bestsellers at a price that "roughly matched," or was slightly lower than, the wholesale price it paid to the publishers. *Apple*, 952 F. Supp. 2d at 649. ***

B. The Publishers' Reactions

Despite the small number of ebook sales compared to the overall market for trade books, top executives in the Big Six saw Amazon's $9.99 pricing strategy as a threat to their established way of doing business. *** In the short term, these members of the Big Six thought that Amazon's lower-priced ebooks would make it more difficult for them to sell hardcover copies of new releases, "which were often priced," as the district court noted, "at thirty dollars or more," *Apple*, 952 F. Supp. 2d at 649, as well as *New York Times* bestsellers. Further down the road, the publishers feared that consumers would become accustomed to the uniform $9.99 price point for these ebooks, permanently driving down the price they could charge for print versions of the books. Moreover, if Amazon became powerful enough, it could demand lower wholesale prices from the Big Six or allow authors to publish directly with Amazon, cutting out the publishers entirely. *** The executives of the Big Six also recognized that their problem was a collective one. ***

The most significant attack that the publishers considered and then undertook, however, was to withhold new and bestselling books from Amazon until the hardcover version had spent several months in stores, a practice known as "windowing." Members of the Big Six both kept one another abreast of their plans to window, and actively pushed others toward the strategy. *** Ultimately, however, the publishers viewed even this strategy to save their business model as self-destructive. Employees inside the publishing companies noted that windowing encouraged piracy, punished ebook consumers, and harmed long-term sales. ***

C. Apple's Entry into the ebook Market

Apple is one of the world's most innovative and successful technology companies. Its hardware sells worldwide and supports major software marketplaces like iTunes and the App Store. But in 2009, Apple lacked a dedicated marketplace for ebooks or a hardware device that could offer an outstanding reading experience. The pending release of the iPad, which Apple intended to announce on January 27, 2010, promised to solve that hardware deficiency.

Eddy Cue, Apple's Senior Vice President of Internet Software and Services and the director of Apple's digital content stores, saw the opportunity for an ebook marketplace on the iPad. *** Jobs approved Cue's plan for an ebook marketplace—which came to be known as the iBookstore—in November 2009. ***

D. Apple's Negotiations with the Publishers

1. Initial Meetings

Apple held its first meetings with each of the Big Six between December 15 and 16. The meetings quickly confirmed Cue's suspicions about the industry. As he wrote to Jobs after speaking with three of the publishers, "[c]learly, the biggest issue is new release pricing" and "Amazon is definitely not liked much because of selling below cost for NYT Best Sellers." J.A. 326-27. Many publishers also emphasized that they were searching for a strategy to regain control over pricing. Apple informed each of the Big Six that it was negotiating with the other major publishers, that it hoped to begin selling ebooks within the next 90 days, and that it was seeking a critical mass of participants in the iBookstore and would launch only if successful in reaching this goal. *** Most importantly for the publishers, however, Cue's team also expressed Apple's belief that Amazon's $9.99 price point was not ingrained in consumers' minds, and that Apple could sell new releases and *New York Times* bestsellers for somewhere between $12.99 and $14.99. In return, Apple requested that the publishers decrease their wholesale prices so that the company could make a small profit on each sale.

These meetings spurred a flurry of communications reporting on the "[t]errific news[,]" as Reidy put it in an email to Leslie Moonves, her superior at parent company CBS Corporation ("CBS"), that Apple "was not interested in a low price point for digital books" and didn't want "Amazon's $9.95 [sic] to continue." *Apple*, 952 F. Supp. 2d at 658 (first alteration in original) (internal quotation marks omitted). Significantly, these communications included numerous exchanges *between* executives at different Big Six publishers who, the district court found, "hashed over their meetings with Apple with one another." *Id.* The district court found that the frequent telephone calls among the Publisher Defendants during the period of their negotiations with Apple "represented a departure from the ordinary pattern of calls among them." *Id.* at 655 n.14.

2. The Agency Model

Meanwhile, Cue, Moerer, and Saul returned to Apple's headquarters to develop a business model for the iBookstore. *** It was at this point that Cue's team, recognizing its opportunity, abandoned the wholesale business model for a new, agency model. Unlike a wholesale model, in an agency relationship the *publisher* sets the price that consumers will pay for each ebook. Then, rather than the retailer paying the publisher for each ebook that it sells, the publisher pays the retailer a fixed percentage of each sale. In essence, the retailer receives a commission for distributing the publisher's ebooks. Under the system Apple devised, publishers would have the freedom to set ebook prices in the iBookstore, and would keep 70% of each sale. The remaining 30% would go to Apple as a commission.

This switch to an agency model obviated Apple's concerns about negotiating wholesale prices with the Big Six while ensuring that Apple profited on every sale. It did not, however, solve all of the company's problems. Because the agency model handed the publishers control over pricing, it created the risk that the Big Six would sell ebooks in the iBookstore at far higher prices than Kindle's $9.99 offering. If the prices were too high, Apple could be left with a brand new marketplace brimming with titles, but devoid of customers.

To solve this pricing problem, Cue's team initially devised two strategies. First, they realized that they could maintain "realistic prices" by establishing price caps for different types of books. J.A. 359. Of course, these caps would need to be higher than Amazon's $9.99 price point, or Apple would face the same difficult price negotiations that it sought to avoid by switching away from the wholesale model. But at this point Apple was not content to open its iBookstore offering prices higher than the competition. ***

Apple next concluded, then, as the district court found, that "[t]o ensure that the iBookstore would be competitive at higher prices, Apple . . . needed to eliminate all retail price competition." *Id.* at 659. Thus, rather than simply agreeing to price caps above Amazon's $9.99 price point, Apple created a second requirement: publishers must switch all of their other ebook retailers—including Amazon—to an agency pricing model. ***

On January 4 and 5, Apple sent essentially identical emails to each member of the Big Six to explain its agency model proposal. Each email described the commission split between Apple and the publishers and recommended three price caps: $14.99 for hardcover books with list prices above $35; $12.99 for hardcover books with list prices below $35; and $9.99 for all other trade books. The emails also explained that, "to sell ebooks at realistic prices . . . all [other] resellers of new titles need to be in [the] agency model" as well. J.A. 360. Or, as Cue told Reidy, "all publishers" would need to move "all retailers" to an agency model. J.A. 2060.

3. The "Most-Favored-Nation" Clause

Cue's thoughts on the agency model continued to evolve after the emails on January 4 and 5. Most significantly, Saul—Cue's in-house counsel—devised an alternative to explicitly requiring publishers to switch other retailers to agency. This alternative involved the use of a "most-favored nation" clause ("MFN Clause" or "MFN"). In general, an MFN Clause is a contractual provision that requires one party to give the other the best terms that it makes available to any competitor. In the context of Apple's negotiations, the MFN Clause mandated that, "[i]f, for any particular New Release in hardcover format, the . . . Customer Price [in the iBookstore] at any time is or becomes higher than a customer price offered by any other reseller . . ., then [the] Publisher shall designate a new, lower Customer Price [in the iBookstore] to meet such lower [customer price]." J.A. 559. Put differently, the MFN would require the publisher to offer any ebook in Apple's iBookstore for no more than what the same ebook was offered elsewhere, such as from Amazon.

On January 11, Apple sent each of the Big Six a proposed eBook Agency Distribution Agreement (the "Contracts"). As described in the January 4 and 5 emails, these Contracts would split the proceeds from each ebook sale between the publisher and Apple, with the publisher receiving 70%, and would set price caps on ebooks at $14.99, $12.99, and $9.99 depending on the book's hardcover price. But unlike the initial emails, the Contracts contained MFN Clauses in place of the requirement that publishers move all other retailers to an agency model. Apple then assured each member of the Big Six that it was being offered the same terms as the others.

The Big Six understood the economic incentives that the MFN Clause created. Suppose a new hardcover release sells at a list price of $25, and a wholesale price of $12.50. With Amazon, the publishers had been receiving the wholesale price (or a slightly lower digital wholesale price) for every ebook copy of the volume sold on Kindle, even if Amazon ultimately sold the ebook for less than that wholesale price. Under Apple's initial agency model—with price caps but no MFN Clause—the publishers already stood to make *less* money per ebook with Apple. Because Apple capped the ebook price of a $25 hardcover at $12.99 and took 30% of that price, publishers could only expect to make $8.75 per sale. But what the publishers sacrificed in short-term revenue, they hoped to gain in long-term stability by acquiring more control over pricing and, accordingly, the ability to protect their hardcover sales.

The MFN Clause changed the situation by making it imperative, not merely desirable, that the publishers wrest control over pricing from ebook retailers generally. Under the MFN, if Amazon stayed at a wholesale model and continued to sell ebooks at $9.99, the publishers would be forced to sell in the iBookstore, too, at that same $9.99 price point. The result would be the worst of both worlds: *lower* short-term revenue and *no* control over pricing. The publishers recognized that, as a practical matter, this meant that the MFN Clause would force them to move Amazon to an agency relationship. *** Apple understood this dynamic as well. *** Cue bluntly put it, "any decent MFN forces the model" away from wholesale and to agency. *Id.* (internal quotation marks omitted). ***

Thus, the terms of the negotiation between Apple and the publishers became clear: Apple wanted quick and successful entry into the ebook market and to eliminate retail price competition with Amazon. In exchange, it offered the publishers an opportunity "to confront Amazon as one of an organized group . . . united in an effort to eradicate the $9.99 price point." *Id.* at 664. Both sides needed a critical mass of publishers to achieve their goals. The MFN played a pivotal role in this *quid pro quo* by "stiffen[ing] the spines of the [publishers] to ensure that they would demand new terms from Amazon," and protecting Apple from retail price competition. *Id.* at 665.

4. Final Negotiations

The proposed Contracts sparked intense negotiations as Cue's team raced to assemble enough publishers to announce the iBookstore by January 27. *** In a set of meetings between January 13 and 14, the majority of the Big Six expressed a general willingness to adopt an agency model, but refused to do so with the price limits Apple demanded. Cue responded by asking Jobs for permission to create a more lenient price cap system. Under this new regime, *New York Times* bestsellers could sell for $14.99 if the hardcover was listed above $30, and for $12.99 if listed below that price. As for new releases, a $12.99 cap would apply to hardcovers priced between $25 and $27.50; a $14.99 cap would apply to hardcovers selling for up to $30; and, if the hardcover sold for over $30, publishers could sell the ebook for between $16.99 and $19.99. Jobs responded that he could "live with" the pricing "as long as [the publishers] move Amazon to the agen[cy] model too." J.A. 499.

Cue proposed this new pricing regime to the Big Six on January 16 and, with only 11 days remaining before the iPad launch, turned up the pressure. *** By January 22, two publishers—Simon & Schuster and Hachette—had verbally committed to join the iBookstore, while a third, Penguin, had agreed to Apple's terms in principle. *** To make matters worse, "[p]ress reports on January 18 and 19 alerted the publishing world and Amazon to the Publishers' negotiations with Apple," *Apple*, 952 F. Supp. 2d at 670-71, and Amazon learned from Random House that it was facing "pressure from other publishers . . . to move to [the] agency model because Apple had made it clear that unless all of the Big Six participated, they wouldn't bother with building a bookstore," J.A. 1520. Representatives from Amazon descended on New York for a set of long-scheduled meetings with the publishers. As the district court found, "[i]n separate conversations on January 20 and over the next few days, the Publisher Defendants all told Amazon that they wanted to change to an agency distribution model with Amazon." *Apple*, 952 F. Supp. 2d at 672. ***

HarperCollins was the fifth, and final, publisher to agree in principle to Apple's proposal. Murray, its CEO, "remained unhappy over the size of Apple's commission and the existence of price caps." *Id.* at 673 n.39. Unable to negotiate successfully with Murray, Cue asked Jobs to contact James Murdoch, the CEO of the publisher's parent company, and "tell him we have 3 signed so there is no leap of faith here." *Id.* at 675 (internal quotation marks omitted). After a series of emails, Jobs summarized Apple's position to Murdoch:

> [W]e simply don't think the ebook market can be successful with pricing higher than $12.99 or $14.99. Heck, Amazon is selling these books at $9.99, and who knows, maybe they are right and we will fail even at $12.99. But we're willing to try at the prices we've proposed. . . . As I see it, [HarperCollins] has the following choices: (1) Throw in with [A]pple and see if we can all make a go of this to create a real mainstream ebooks market at $12.99 and $14.99. (2) Keep going with Amazon at $9.99. You will make a bit more money in the short term, but in the medium term Amazon will tell you they will be paying you 70% of $9.99. They have shareholders too. (3) Hold back your books from Amazon. Without a way for customers to buy your ebooks, they will steal them.

Id. at 677. Cue also emailed Murray to inform him that four other publishers had signed their agreements. Murray then called executives at both Hachette and Macmillan before agreeing to Apple's terms.

As the district court found, during the period in January during which Apple concluded its agreements with the Publisher Defendants, "Apple kept the Publisher Defendants apprised about who was in and how many were on board." *Id.* at 673. The Publisher Defendants also kept in close communication. As the district court noted, "[i]n the critical negotiation period, over the three days between January 19 and 21, Murray, Reidy, Shanks, Young, and Sargeant called one another 34 times, with 27 calls exchanged on January 21 alone." *Id.* at 674.

By the January 27 iPad launch, five of the Big Six—Hachette, HarperCollins, Macmillan, Penguin, and Simon & Schuster—had agreed to participate in the iBookstore. The lone holdout, Random House, did not join because its executives believed it would fare better under a wholesale pricing model and were unwilling to make a complete switch to agency pricing. Steve Jobs announced the iBookstore as part of his presentation introducing the iPad. When asked after the presentation why someone should purchase an ebook from Apple for $14.99 as opposed to $9.99 with Amazon or Barnes & Noble, Jobs confidently replied, "[t]hat won't be the case . . . the price will be the same. . . . [P]ublishers will actually withhold their [e]books from Amazon . . . because they are not happy with the price." A day later, Jobs told his biographer the publishers' position with Amazon: "[y]ou're going to sign an agency contract or we're not going to give you the books." J.A. 891 (internal quotation marks omitted).

E. Negotiations with Amazon

Jobs's boast proved to be prophetic. While the Publisher Defendants were signing Apple's Contracts, they were also informing Amazon that they planned on changing the terms of their agreements with it to an agency model. However, their move against Amazon began in earnest on January 28, the day after the iPad launch. That afternoon, John Sargent flew to Seattle to deliver an ultimatum on behalf of Macmillan: that Amazon would switch its ebook sales agreement with Macmillan to an agency model or suffer a seven-month delay in its receipt of Macmillan's new releases. Amazon responded by removing the option to purchase Macmillan's print and ebook titles from its website.

Sargent, as the district court found, had informed Cue of his intention to confront Amazon before ever leaving for Seattle. *Apple*, 952 F.Supp.2d at 678. On his return, he emailed Cue to inform him about Amazon's decision to remove Macmillan ebooks from Kindle, adding a note to say that he wanted to "make sure you are in the loop." J.A. 640. Sargent also wrote a public letter to Macmillan's authors and agents, describing the Amazon negotiations. Hachette's Arnaud Nourry emailed the CEO of Macmillan's parent company to express his "personal support" for Macmillan's actions and to "ensure [him] that [he was] not going to find [his] company alone in the battle." J.A. 643. A Penguin executive wrote to express similar support for Macmillan's position.

The district court found that while Amazon was "opposed to adoption of the agency model and did not want to cede pricing authority to the Publishers," it knew that it could not prevail in this position against five of the Big Six. *Apple*, 952 F.Supp.2d at 671, 680. When Amazon told Macmillan that it would be willing to negotiate agency terms, Sargent sent Cue an email titled "URGENT!!" that read: "Hi Eddy, I am gonna need to figure out our final agency terms of sale tonight. Can you call me please?" J.A. 642. Cue and Sargent spoke that night and, while Cue denied at trial that the conversation concerned Macmillan's negotiations with Amazon, the district court found that "his denial was not credible." *Apple*, 952 F.Supp.2d at 681 n.52. By February 5, Amazon had agreed to agency terms with Macmillan.

The other publishers who had joined the iBookstore quickly followed Macmillan's lead. *** Once again, Apple closely monitored the negotiations with Amazon. The Publisher Defendants would inform Cue when they had completed agency agreements, and his team monitored price changes on the Kindle. ***

F. Effect on Ebook Prices

As Apple and the Publisher Defendants expected, the iBookstore price caps quickly became the benchmark for ebook versions of new releases and *New York Times* bestsellers. In the five months following the launch of the iBookstore, the publishers who joined the marketplace and switched Amazon to an agency model priced 85.7% of new releases on Kindle and 92.1% of new releases on the iBookstore at, or just below, the price caps. *Apple*, 952 F. Supp. 2d at 682. Prices for *New York Times* bestsellers took a similar leap as publishers began to sell 96.8% of their bestsellers on Kindle and 99.4% of their bestsellers on the iBookstore at, or just below, the Apple price caps *Id.* During that same time period, Random House, which had not switched to an agency model, saw virtually no change in the prices for its new releases or *New York Times* bestsellers.

*** Based on data from February 2010—just before the Publisher Defendants switched Amazon to agency pricing—to February 2011, an expert retained by the Justice Department observed that the weighted average price of the Publisher Defendants' new releases increased by 24.2%, while bestsellers increased by 40.4%, and other ebooks increased by 27.5%, for a total weighted average ebook price increase of 23.9%. Indeed, even Apple's expert agreed, noting that, over a two-year period, the Publisher Defendants increased their average prices for hardcovers, new releases, and other ebooks. ***

II. Apple's Liability Under § 1

This appeal requires us to address the important distinction between "horizontal" agreements to set prices, which involve coordination "between competitors at the same level of [a] market structure," and "vertical" agreements on pricing, which are created between parties "at different levels of [a] market structure." *Anderson News, L.L.C. v. Am. Media, Inc.*, 680 F.3d 162, 182 (2d Cir. 2012) (internal quotation marks omitted). Under § 1 of the Sherman Act, the former are, with limited exceptions, per se unlawful, while the latter are unlawful only if an assessment of market effects, known as a rule-of-reason analysis, reveals that they unreasonably restrain trade. ***

Apple characterizes its Contracts with the Publisher Defendants as a series of parallel but independent vertical agreements, a characterization that forms the basis for its two primary arguments against the district court's decision. *** For the reasons set forth below, we reject these arguments. On this record, the district court did not err in determining that Apple orchestrated an agreement with and among the Publisher Defendants, in characterizing this agreement as a horizontal price fixing-conspiracy, or in holding that the conspiracy unreasonably restrained trade in violation of § 1 of the Sherman Act.

A. The Conspiracy with the Publisher Defendants

Section 1 of the Sherman Act bans restraints on trade "effected by a contract, combination, or conspiracy." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 553 (2007) (internal quotation marks omitted). The first "crucial question in a Section 1 case is therefore whether the challenged conduct 'stem[s] from independent decision or from an agreement, tacit or express.'" *Starr v. Sony BMG*

Music Entm't, 592 F.3d 314, 321 (2d Cir. 2010) (alteration in original) (quoting *Theatre Enters., Inc. v. Paramount Film Distrib. Corp.*, 346 U.S. 537, 540 (1954)).

Identifying the existence and nature of a conspiracy requires determining whether the evidence "reasonably tends to prove that the [defendant] and others had a conscious commitment to a common scheme designed to achieve an unlawful objective." *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984) (internal quotation marks omitted). Parallel action is not, by itself, sufficient to prove the existence of a conspiracy; such behavior could be the result of "coincidence, independent responses to common stimuli, or mere interdependence unaided by an advance understanding among the parties." *Twombly*, 550 U.S. at 556 n.4 (internal quotation marks omitted). Indeed, parallel behavior that does not result from an agreement is not unlawful even if it is anticompetitive. Accordingly, to prove an antitrust conspiracy, "a plaintiff must show the existence of additional circumstances, often referred to as 'plus' factors, which, when viewed in conjunction with the parallel acts, can serve to allow a fact-finder to infer a conspiracy." *Apex Oil Co. v. DiMauro*, 822 F.2d 246, 253 (2d Cir. 1987).

*** Because of the risk of condemning parallel conduct that results from independent action and not from an actual unlawful agreement, the Supreme Court has cautioned against drawing an inference of conspiracy from evidence that is equally consistent with independent conduct as with illegal conspiracy—or, as the Court has called it, "ambiguous" evidence. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 597 n.21 (1986).

*** Apple's basic argument is that because its Contracts with the Publisher Defendants were fully consistent with its independent business interests, those agreements provide only "ambiguous" evidence of a § 1 conspiracy, and the district court therefore erred under *Matsushita* and *Monsanto* in inferring such a conspiracy.

We disagree. At the start, Apple's benign portrayal of its Contracts with the Publisher Defendants is not persuasive—not because those Contracts themselves were independently unlawful, but because, in context, they provide strong evidence that Apple consciously orchestrated a conspiracy among the Publisher Defendants. As explained below, and as the district court concluded, Apple understood that its proposed Contracts were attractive to the Publisher Defendants *only* if they collectively shifted their relationships with Amazon to an agency model—which Apple knew would result in higher consumer-facing ebook prices. In addition to these Contracts, moreover, ample additional evidence identified by the district court established both that the Publisher Defendants' shifting to an agency model with Amazon was the result of express collusion among them and that Apple consciously played a key role in organizing that collusion. The district court did not err in concluding that Apple was more than an innocent bystander.

Apple offered each Big Six publisher a proposed Contract that would be attractive only if the publishers acted collectively. Under Apple's proposed agency model, the publishers stood to make less money per sale than under their wholesale agreements with Amazon, but the Publisher Defendants were willing to stomach this loss because the model allowed them to sell new releases and bestsellers for more than $9.99. Because of the MFN Clause, however, each new release and bestseller sold in the iBookstore would cost only $9.99 as long as Amazon continued to sell ebooks at that price. So in order to receive the perceived benefit of Apple's proposed Contracts, the Publisher Defendants had to switch Amazon to an agency model as well—something no individual publisher had sufficient leverage to do on its own. Thus, each Publisher Defendant would be able to accomplish the shift to agency—and therefore have an incentive to sign Apple's proposed Contracts—only if it acted in tandem with its competitors. By the very act of signing a Contract with Apple containing an MFN Clause, then, each of the Publisher Defendants signaled a clear commitment to move against Amazon, thereby facilitating their collective action. ***

The Supreme Court has defined an agreement for Sherman Act § 1 purposes as "a conscious commitment to a common scheme designed to achieve an unlawful objective." *Monsanto*, 465 U.S. at 764 (internal quotation marks omitted). Plainly, this use of the promise of higher prices as a bargaining chip to induce the Publisher Defendants to participate in the iBookstore constituted a conscious commitment to the goal of raising ebook prices. *** Nor was the Publisher Defendants' joint action against Amazon a result of parallel decisionmaking. *** That the Publisher Defendants were in constant communication regarding their negotiations with both Apple and Amazon can hardly be disputed. Indeed, Apple never seriously argues that the Publisher Defendants were not acting in concert.

*** Apple's involvement in the conspiracy continued even past the signing of its agency agreements. Before Sargent flew to Seattle to meet with Amazon, he told Cue. Apple stayed abreast of the Publisher Defendants' progress as they set coordinated deadlines with Amazon and shared information with one another during negotiations. ***

Apple responds to this evidence—which the experienced judge who oversaw the trial characterized repeatedly as "overwhelming"—by explaining how each piece of evidence standing alone is "ambiguous" and therefore insufficient to support an inference of conspiracy. We are not persuaded. *** Combined with the unmistakable purpose of the Contracts that Apple proposed to the publishers, and with the collective move against Amazon that inevitably followed the signing of those Contracts, the emails and phone records demonstrate that Apple agreed-with the Publisher Defendants, within the meaning of the Sherman Act, to raise consumer-facing ebook prices by eliminating retail price competition. The district court did not err in rejecting Apple's argument that the evidence of its orchestration of the Publisher Defendants' conspiracy was "ambiguous."

*** In short, we have no difficulty on this record rejecting Apple's argument that the district court erred in concluding that Apple "conspir[ed] with the Publisher Defendants to eliminate retail price competition and to raise e-book prices." *Apple*, 952 F. Supp. 2d at 691. Having concluded that the district court correctly identified an agreement between Apple and the Publisher Defendants to raise consumer-facing ebook prices, we turn to Apple's and the dissent's arguments that this agreement did not violate § 1 of the Sherman Act.

B. Unreasonable Restraint of Trade

"Although the Sherman Act, by its terms, prohibits every agreement 'in restraint of trade,' [the Supreme] Court has long recognized that Congress intended to outlaw only unreasonable restraints." *State Oil Co. v. Khan*, 522 U.S. 3, 10 (1997).***

In antitrust cases, "*[p]er se* and rule-of-reason analysis are . . . two methods of determining whether a restraint is 'unreasonable,' *i.e.*, whether its anticompetitive effects outweigh its procompetitive effects." *Atl. Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 342 (1990). *** Horizontal price-fixing conspiracies traditionally have been, and remain, the "archetypal example" of a *per se* unlawful restraint on trade. *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647 (1980). By contrast, the Supreme Court in recent years has clarified that vertical restraints—including those that restrict prices—should generally be subject to the rule of reason.

In this case, the district court held that the agreement between Apple and the Publisher Defendants was unlawful under the *per se* rule; in the alternative, even assuming that a rule-of-reason analysis was required, the district court concluded that the agreement was still unlawful.

1. Whether the *Per Se* Rule Applies

a. Horizontal Agreement

In light of our conclusion that the district court did not err in determining that Apple organized a price-fixing conspiracy among the Publisher Defendants, Apple and the dissent's initial argument against the *per se* rule—that Apple's conduct must be subject to rule-of-reason analysis because it involved merely multiple independent, vertical agreements with the Publisher Defendants—cannot succeed.

"The true test of legality" under § 1 of the Sherman Act "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." *Bd. of Trade of City of Chi. v. United States*, 246 U.S. 231, 238 (1918) (emphasis added). By agreeing to orchestrate a horizontal price-fixing conspiracy, Apple committed itself to "achiev[ing] [that] unlawful objective," *Monsanto*, 465 U.S. at 764 (internal quotation marks omitted): namely, collusion with and among the Publisher Defendants to set ebook prices. This type of agreement, moreover, is a restraint "that would always or almost always tend to restrict competition and decrease output." *Leegin*, 551 U.S. at 886 (internal quotation marks omitted).

The response, raised by Apple and our dissenting colleague, that Apple engaged in "vertical conduct" that is unfit for *per se* condemnation therefore misconstrues the Sherman Act analysis. It is the type of restraint Apple agreed to impose that determines whether the *per se* rule or the rule of reason is appropriate. These rules are means of evaluating "whether [a] *restraint* is unreasonable," not the reasonableness of a particular defendant's role in the scheme. *Atl. Richfield*, 495 U.S. at 342 (emphasis added) (internal quotation marks omitted).

Consistent with this principle, the Supreme Court and our Sister Circuits have held all participants in "hub-and-spoke" conspiracies liable when the objective of the conspiracy was a per se unreasonable restraint of trade. ***

Because the reasonableness of a restraint turns on its anticompetitive effects, and not the identity of each actor who participates in imposing it, Apple and the dissent's observation that the Supreme Court has refused to apply the *per se* rule to certain vertical agreements is inapposite. The rule of reason is unquestionably appropriate to analyze an agreement between a manufacturer and its distributors to, for instance, limit the price at which the distributors sell the manufacturer's goods or the locations at which they sell them. *See Leegin*, 551 U.S. at 881; *Cont'l T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 57 (1977). These vertical restrictions "are widely used in our free market economy," can enhance interbrand competition, and do not inevitably have a "pernicious effect on competition." *Cont'l T.V.*, 433 U.S. at 57-58 (internal quotation marks omitted). But the relevant "agreement in restraint of trade" in this case is not Apple's vertical Contracts with the Publisher Defendants (which might well, if challenged, have to be evaluated under the rule of reason); it is the horizontal agreement that Apple organized among the Publisher Defendants to raise ebook prices. As explained below, horizontal agreements with the purpose and effect of raising prices are *per se* unreasonable because they pose a "threat to the central nervous system of the economy," *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 224 n.59 (1940); that threat is just as significant when a vertical market participant organizes the conspiracy. Indeed, as the dissent notes, the Publisher Defendants' coordination to fix prices is uncontested on appeal. The competitive effects of that *same restraint* are no different merely because a different conspirator is the defendant.

Accordingly, when the Supreme Court has applied the rule of reason to vertical agreements, it has explicitly distinguished situations in which a vertical player organizes a horizontal cartel. ***

A horizontal conspiracy can use vertical agreements to facilitate coordination without the other parties to those agreements knowing about, or agreeing to, the horizontal conspiracy's goals. *** But there is no such possibility for confusion in the hub-and-spoke context, where the vertical organizer has not only committed to vertical agreements, but has also agreed to participate in the horizontal conspiracy. In that situation, the court need not consider whether the vertical agreements restrained trade because all participants agreed to the horizontal restraint, which is "and ought to be, per se unlawful." *Id.*

In short, the relevant "agreement in restraint of trade" in this case is the price-fixing conspiracy identified by the district court, not Apple's vertical contracts with the Publisher Defendants. How the law might treat Apple's vertical agreements in the absence of a finding that Apple agreed to create the horizontal restraint is irrelevant. Instead, the question is whether the vertical organizer of a horizontal conspiracy designed to raise prices has agreed to a restraint that is any less anticompetitive than its co-conspirators, and can therefore escape *per se* liability. We think not. Even in light of this conclusion, however, we must address two additional arguments that Apple raises against application of the *per se* rule.

b. "Enterprise and Productivity"

Apple seeks refuge from the per se rule by invoking a line of cases in which courts have permitted defendants to introduce procompetitive justifications for horizontal price-fixing arrangements that would ordinarily be condemned per se if those agreements "when adopted could reasonably have been believed to promote 'enterprise and productivity.'" Apple Br. at 50 (quoting *In re Sulfuric Acid Antitrust Litig.*, 703 F.3d 1004, 1011 (7th Cir. 2012)) (internal quotation mark omitted). ***

Put differently, a participant in a price-fixing agreement may invoke only certain, limited *kinds* of "enterprise and productivity" to receive the rule of reason's advantages. As the Supreme Court has explained—including in *BMI* itself, *see* 441 U.S. at 8 & n.11—the *per se* rule would lose all the benefits of being "*per se*" if conspirators could seek to justify their conduct on the basis of its purported competitive benefits in every case. Here, there was no joint venture or other similar productive relationship between any of the participants in the conspiracy that Apple joined. Apple also does not claim, nor could it, that creating an ebook retail market is possible only if the participating publishers coordinate with one another on price.

c. Price-Fixing Conspiracy

As noted, the Supreme Court has for nearly 100 years held that horizontal collusion to raise prices is the "archetypal example" of a *per se* unlawful restraint of trade. *Catalano*, 446 U.S. at 647. If successful, these conspiracies concentrate the power to set prices among the conspirators, including the "power to control the market and to fix arbitrary and unreasonable prices." *United States v. Trenton Potteries Co.*, 273 U.S. 392, 397 (1927). And even if unsuccessful or "not . . . aimed at complete elimination of price competition," the conspiracies pose a "threat to the central nervous system of the economy" by creating a dangerously attractive opportunity for competitors to enhance their power at the expense of others. *Socony-Vacuum Oil*, 310 U.S. at 224 n.59 (1940).***

Apple and its amici argue that the horizontal agreement among the publishers was not actually a "price-fixing" conspiracy that deserves *per se* treatment in the first place. But it is well established that *per se* condemnation is not limited to agreements that literally set or restrict prices. Instead, any conspiracy "formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity . . . is illegal per se," and the precise "machinery employed . . . is immaterial." *Socony-Vacuum Oil*, 310 U.S. at 223. The conspiracy among Apple and the Publisher Defendants comfortably qualifies as a horizontal price-fixing conspiracy.

As we have already explained, the Publisher Defendants' primary objective in expressly colluding to shift the entire ebook industry to an agency model (with Apple's help) was to eliminate Amazon's $9.99 pricing for new releases and bestsellers, which the publishers believed threatened their short-term ability to sell hardcovers at higher prices and the long-term consumer perception of the price of a new book. They had grown accustomed to a business in which they rarely competed with one another on price and could, at least partially, control the price of new releases and bestsellers by releasing hardcover copies before paperbacks. Amazon, and the ebook, upset that model, and reduced prices to consumers by eliminating the need to print, store, and ship physical volumes. Its $9.99 price point for new releases and bestsellers represented a small loss on a small percentage of its sales designed to encourage consumers to adopt the new technology.

Faced with downward pressure on prices but unconvinced that withholding books from Amazon was a viable strategy, the Publisher Defendants—their coordination orchestrated by Apple—combined forces to grab control over price. Collectively, the Publisher Defendants accounted for 48.8% of ebook sales in 2010. Once organized, they had sufficient clout to demand control over pricing, in the form of agency agreements, from Amazon and other ebook distributors. This control over pricing facilitated their ultimate goal of raising ebook prices to the price caps. In other words, the Publisher Defendants took by collusion what they could not win by competition. And Apple used the publishers' frustration with Amazon's $9.99 pricing as a bargaining chip in its negotiations and structured its Contracts to coordinate their push to raise prices throughout the industry. A coordinated effort to raise prices across the relevant market was present in every chapter of this story.

This conspiracy to raise prices also had its intended effect. Immediately after the Publisher Defendants switched Amazon to an agency model, they increased the Kindle prices of 85.7% of their new releases and 96.8% of their *New York Times* bestsellers to within 1% of the Apple price caps. They also increased the prices of their other ebook offerings. Within two weeks of the move to agency, the weighted average price of the Publisher Defendants' ebooks—which accounted for just under half of all ebook sales in 2010—had increased by 18.6%, while the prices for Random House and other publishers remained relatively stable.

This sudden increase in prices reduced ebook sales by the Publisher Defendants and proved to be durable. One analysis compared two-week periods before and after the Publisher Defendants took control over pricing and found that they sold 12.9% fewer ebooks after the switch. Another expert for Plaintiffs conducted a regression analysis, which showed that, over a six-month period following the switch, the Publisher Defendants sold 14.5% fewer ebooks than they would have had the price increases not occurred. Nonetheless, ebook prices for the Publisher Defendants over those six months, controlling for other factors, remained 16.8% higher than before the switch. And even Apple's expert produced a chart showing that the Publisher Defendants' prices for new releases, bestsellers, and other offerings remained elevated a full two years after they took control over pricing.

Apple points out that, in the two years following the conspiracy, prices across the ebook market as a whole fell slightly and total output increased. However, when the agreement at issue involves price fixing, the Supreme Court has consistently held that courts need not even conduct an extensive analysis of "market power" or a "detailed market analysis" to demonstrate its anticompetitive character. *FTC v. Ind. Fed'n of Dentists*, 476 U.S. 447, 460 (1986). The district court's assessment of Apple's and the Publisher Defendants' motives, coupled with the unambiguous increase in the prices of their ebooks, was sufficient to confirm that price fixing was the goal, and the result, of the conspiracy.

Moreover, Apple's evidence regarding long-term growth and prices in the ebook industry is not inconsistent with the conclusion that the price-fixing conspiracy succeeded in actually raising prices. *** No court can presume to know the proper price of an ebook, but the long judicial experience applying the Sherman Act has shown that "[a]ny combination which tampers with price structures . . . would be directly interfering with the free play of market forces." *Socony-Vacuum Oil*, 310 U.S. at 221. By setting new, durable prices through collusion rather than competition, Apple and the Publisher Defendants imposed their view of proper pricing, supplanting the market's free play. This evidence, viewed in conjunction with the district court's findings as to and analysis of the conspiracy's history and purpose, is sufficient to support the conclusion that the agreement to raise ebook prices was a *per se* unlawful price-fixing conspiracy.

2. Rule of Reason

As explained above, neither Apple nor the dissent has presented any particularly strong reason to think that the conspiracy we have identified should be spared *per se* condemnation. My concurring colleague would therefore affirm the district court's decision on that basis alone. I, too, believe that *per se* condemnation is appropriate in this case and view Apple's sloganeering references to "innovation" as a distraction from the straightforward nature of the conspiracy proven at trial. Nonetheless, I am mindful of Apple's argument that the nascent ebook industry has some new and unusual features and that the *per se* rule is not fit for "business relationships where the economic impact of certain practices is not immediately obvious." *Leegin*, 551 U.S. at 887 (internal quotation marks omitted). I therefore assume, for the sake of argument, that it is appropriate to apply the rule of reason and to analyze the competitive effects of Apple's horizontal agreement with the Publisher Defendants.

Notably, however, the ample evidence here concerning the purpose and effects of Apple's agreement with the Publisher Defendants affects the scope of the rule-of-reason analysis called for in this case. Under a prototypically robust rule-of-reason analysis, the plaintiff must demonstrate an "*actual* adverse effect" on competition in the relevant market before the "burden shifts to the defendants to offer evidence of the pro-competitive effects of their agreement." *Geneva Pharms. Tech. Corp. v. Barr Labs. Inc.*, 386 F.3d 485, 506-07 (2d Cir. 2004) (internal quotation marks omitted). The factfinder then weighs the competing evidence "to determine if the effects of the challenged restraint tend to promote or destroy competition."*Id.* at 507. ***

Apple's initial argument that its agreement with the Publisher Defendants was procompetitive (an argument presented principally in an amicus brief adopted wholeheartedly by the dissent) is that by eliminating Amazon's $9.99 price point, the agreement enabled Apple and other ebook retailers to enter the market and challenge Amazon's dominance. But this defense—that higher prices enable more competitors to enter a market—is no justification for a horizontal price-fixing conspiracy. ***

From this perspective, the dissent's contention that Apple could not have entered the ebook retail market without the price-fixing conspiracy, because it could not have profited either by charging more than Amazon or by following Amazon's pricing, is a complete non sequitur. The posited dilemma is the whole point of competition: if Apple could not turn a profit by selling new releases and bestsellers at $9.99, or if it could not make the iBookstore and iPad so attractive that consumers would pay more than $9.99 to buy and read those ebooks on its platform, then there was no place for its platform in the ebook retail market. Neither the district court nor Plaintiffs had an obligation to identify a "viable alternative" for Apple's profitable entry because Apple had no entitlement to enter the market on its preferred terms.

*** In actuality, the district court's fact-finding illustrates that Apple organized the Publisher Defendants' price-fixing conspiracy not because it was a necessary precondition to market entry, but because it was a convenient bargaining chip. Apple was operating under a looming deadline and recognized that, by aligning its interests with those of the Publisher Defendants and offering them a way to raise prices across the ebook market, it could gain quick entry into the market on extremely favorable terms, including the elimination of retail price competition from Amazon. But the offer to orchestrate a horizontal conspiracy to raise prices is not a legitimate way to sweeten a deal.

*** To summarize, the district court made no finding that a horizontal conspiracy to eliminate price competition in the ebook retail market was necessary to bring more retailers into the market to challenge Amazon, nor does the record evidence support this conclusion. More importantly, even if there *were* such evidence, the fact that a competitor's entry into the market is contingent on a horizontal conspiracy to raise prices only means (absent monopolistic conduct by the market's dominant firm, which cannot lawfully be challenged by collusion) that the competitor is inefficient, *i.e.*, that its entry will not enhance consumer welfare. For these reasons, I would reject the argument that Apple's entry into the market represented an important pro-competitive benefit of the horizontal price-fixing conspiracy it orchestrated.

*** Accordingly, I agree with the district court's decision that, under the rule of reason, the horizontal agreement to raise consumer-facing ebook prices that Apple orchestrated unreasonably restrained trade. But given the clear applicability of the *per se* rule in this context, the analysis here is largely offered in response to the dissent. I also confidently join with my concurring colleague in affirming the district court's conclusion that Apple committed a *per se* violation of § 1 of the Sherman Act.

CONCLUSION

We have considered the appellants' remaining arguments and find them to be without merit. Because we conclude that Apple violated § 1 of the Sherman Act by orchestrating a horizontal conspiracy among the Publisher Defendants to raise ebook prices, and that the injunctive relief ordered by the district court is appropriately designed to guard against future anticompetitive conduct, the judgment of the district court is AFFIRMED.

LOHIER, CIRCUIT JUDGE, Concurring in part and Concurring in the judgment: I join in the majority opinion except for part II.B.2 relating to the application of the rule of reason. In my view, Apple's appeal rises or falls based on the application of the per se rule. That rule clearly applies to the central agreement in this case (and the only agreement alleged to be unlawful): the publishers' horizontal agreement to fix ebook prices. ***

DENNIS JACOBS, CIRCUIT JUDGE, Dissenting. I respectfully dissent. This appeal is taken by Apple Inc. from a judgment in the United States District Court for the Southern District of New York (Cote, J.), awarding an antitrust injunction in favor of the United States, 31 states, the District of Columbia, and the Commonwealth of Puerto Rico. The plaintiffs' claims are premised on Apple's conduct as a prospective retailer of e-books. I vote to reverse. *** In the course of this litigation, three theories have been offered for how Apple could have entered the e-book market on less restrictive terms. Each theory misapprehends the market or the law, or both. The absence of alternative means bespeaks the reasonableness of the measures Apple took.

Theory 1: Apple could have competed with Amazon on Amazon's terms, using wholesale contracts and below-cost pricing.

This was never an option. The district court found as fact that: a new entrant into the e-book retail market "would run the risk of losing money if it tried or was forced to match Amazon's pricing to remain competitive," *Apple I*, 952 F. Supp. 2d at 658; Apple was "not willing" to engage in below-cost pricing, *Id.* at 657; and Apple could have avoided this money-losing price structure simply by forgoing entry to the market, see *Id.* at 659. Even if Apple had been willing to adopt below-cost pricing, the result at best would have been duopoly, and the hardening of the existing barrier to entry. Antitrust law disfavors a durable duopoly nearly as much as monopoly itself.

Theory 2: Apple could have entered the e-book retail market using the wholesale model and charged higher prices than Amazon's.

The district court foreclosed this theory as well; it found that Apple refused to impair its brand by charging "what it considered unrealistically high prices." *Apple I*, 952 F. Supp. 2d at 659. Even if Apple had been willing to tarnish its brand by offering bad value for money, the notion that customers would actually have bought e-books from Apple at the higher price defies the law of demand. Higher prices may stimulate sales of certain wines and perfumes—not e-books.

Nor could Apple justify higher prices for the e-books by competing on the basis of its new hardware, the iPad, because there is inter-operability among platforms. And if Apple had attempted to pursue this hardware-based competition by programming its iPad to run the iBookstore but to reject Amazon's Kindle application, Apple might have been exposed to an entirely different antitrust peril. See *United States v. Microsoft Corp.*, 253 F.3d 34, 50-80 (D.C. Cir. 2001) (en banc); Google Android, No. 40099 (Eur. Comm'n Apr. 15, 2015) (antitrust proceedings brought by European Commissioner for Competition against Google for favoring Google's own applications on mobile devices that use Google's operating system).

Theory 3: Apple could have asked the Department of Justice to act against Amazon's monopoly.

Counsel for the United States actually proposed this at oral argument. At the same time, however, he conceded that the Department of Justice had already "noticed" Amazon's e-book pricing and had chosen not to challenge it because the government "regarded it as good for consumers." Any request from Apple would therefore have been futile. True, Apple could not have known that the Antitrust Division would have adopted the position that below-cost pricing is not a concern of antitrust policy: who could have guessed that the government would adopt a policy that is primitive as a matter of antitrust doctrine and illiterate as a matter of economics? Nevertheless, hindsight reveals that government antitrust enforcement against Amazon was not an option.

More fundamentally, litigation is not a *market* alternative. This observation has especial force in markets that are undergoing rapid technological advance, where the competitive half-life of a product is considerably more brief than the span of antitrust litigation. A requirement that potential market entrants litigate instead of enter the market on restrictive (but legal and reasonable) terms, would license monopoly for the duration.

Apple took steps to compete with a monopolist and open the market to more entrants, generating only minor competitive restraints in the process. Its conduct was eminently reasonable; no one has suggested a viable alternative. "What could be more perverse than an antitrust doctrine that discouraged new entry into highly concentrated markets?" *In re Text Messaging Antitrust Litig.*, 782 F.3d 867, 874 (7th Cir. 2015).

Application of the rule of reason easily absolves Apple of antitrust liability. That is why at oral argument the government analogized this case to a drug conspiracy, in which every player is a criminal—at every level, on every axis, whether big or small, whether new entrant or recidivist. The government found the analogy useful—and necessary—because in an all-criminal industry there is no justification or harbor under a rule of reason. ***

Ohio v. American Express Co.

585 U.S. 529 (2018)

THOMAS, J., delivered the opinion of the Court. American Express Company and American Express Travel Related Services Company (collectively, Amex) provide credit-card services to both merchants and cardholders. When a cardholder buys something from a merchant who accepts Amex credit cards, Amex processes the transaction through its network, promptly pays the merchant, and subtracts a fee. If a merchant wants to accept Amex credit cards—and attract Amex cardholders to its business—Amex requires the merchant to agree to an anti-steering contractual provision. The anti-steering provision prohibits merchants from discouraging customers from using their Amex card after they have already entered the store and are about to buy something, thereby avoiding Amex's fee. In this case, we must decide whether Amex's anti-steering provisions violate federal antitrust law. We conclude they do not.

I

A

Credit cards have become a primary way that consumers in the United States purchase goods and services. When a cardholder uses a credit card to buy something from a merchant, the transaction is facilitated by a credit card network. The network provides separate but interrelated services to both cardholders and merchants. For cardholders, the network extends them credit, which allows them to make purchases without cash and to defer payment until later. Cardholders also can receive rewards based on the amount of money they spend, such as airline miles, points for travel, or cash back. For merchants, the network allows them to avoid the cost of processing transactions and offers them quick, guaranteed payment. This saves merchants the trouble and risk of extending credit to customers, and it increases the number and value of sales that they can make.

By providing these services to cardholders and merchants, credit-card companies bring these parties together, and therefore operate what economists call a "two-sided platform." As the name implies, a two-sided platform offers different products or services to two different groups who both depend on the platform to intermediate between them. For credit cards, that interaction is a transaction. Thus, credit-card networks are a special type of two-sided platform known as a "transaction" platform. The key feature of transaction platforms is that they cannot make a sale to one side of the platform without simultaneously making a sale to the other. For example, no credit card transaction can occur unless both the merchant and the cardholder simultaneously agree to use the same credit-card network.

Two-sided platforms differ from traditional markets in important ways. Most relevant here, two-sided platforms often exhibit what economists call "indirect network effects." Indirect network effects exist where the value of the two-sided platform to one group of participants depends on how many members of a different group participate. In other words, the value of the services that a two-sided platform provides increases as the number of participants on both sides of the platform increases. A credit card, for example, is more valuable to cardholders when more merchants accept it, and is more valuable to merchants when more cardholders use it. To ensure sufficient participation, two-sided platforms must be sensitive to the prices that they charge each side. Raising the price on side A risks losing participation on that side, which decreases the value of the platform to side B. If participants on side B leave due to this loss in value, then the platform has even less value to side A—risking a feedback loop of declining demand. Two-sided platforms therefore must take these indirect network effects into account before making a change in price on either side.

Sometimes indirect network effects require two-sided platforms to charge one side much more than the other. For two-sided platforms *** [t]he optimal price might require charging the side with more elastic demand a below-cost (or even negative) price. With credit cards, for example, networks often charge cardholders a lower fee than merchants because cardholders are more price sensitive. In fact, the network might well lose money on the cardholder side by offering rewards such as cash back, airline miles, or gift cards. The network can do this because increasing the number of cardholders increases the value of accepting the card to merchants and, thus, increases the number of merchants who accept it. Networks can then charge those merchants a fee for every transaction (typically a percentage of the purchase price). Striking the optimal balance of the prices charged on each side of the platform is essential for two-sided platforms to maximize the value of their services and to compete with their rivals.

B

Amex, Visa, MasterCard, and Discover are the four dominant participants in the credit-card market. Visa, which is by far the largest, has 45% of the market as measured by transaction volume. Amex and MasterCard trail with 26.4% and 23.3%, respectively, while Discover has just 5.3% of the market. Visa and MasterCard have significant structural advantages over Amex. Visa and MasterCard began as bank cooperatives and thus almost every bank that offers credit cards is in the Visa or MasterCard network. This makes it very likely that the average consumer carries, and the average merchant accepts, Visa or MasterCard. As a result, the vast majority of Amex cardholders have a Visa or MasterCard, but only a small number of Visa and MasterCard cardholders have an Amex. Indeed, Visa and MasterCard account for more than 432 million cards in circulation in the United States, while Amex has only 53 million. And while 3.4 million merchants at 6.4 million locations accept Amex, nearly three million more locations accept Visa, MasterCard, and Discover.

Amex competes with Visa and MasterCard by using a different business model. While Visa and MasterCard earn half of their revenue by collecting interest from their cardholders, Amex does not. Amex instead earns most of its revenue from merchant fees. Amex's business model thus focuses on cardholder spending rather than cardholder lending. To encourage cardholder spending, Amex provides better rewards than other networks. Due to its superior rewards, Amex tends to attract cardholders who are wealthier and spend more money. Merchants place a higher value on these cardholders, and Amex uses this advantage to recruit merchants.

Amex's business model has significantly influenced the credit-card market. To compete for the valuable cardholders that Amex attracts, both Visa and MasterCard have introduced premium cards that, like Amex, charge merchants higher fees and offer cardholders better rewards. To maintain their lower merchant fees, Visa and MasterCard have created a sliding scale for their various cards— charging merchants less for low-reward cards and more for high-reward cards. This differs from Amex's strategy, which is to charge merchants the same fee no matter the rewards that its card offers. Another way that Amex has influenced the credit-card market is by making banking and card-payment services available to low-income individuals, who otherwise could not qualify for a credit card and could not afford the fees that traditional banks charge. . . .

Despite these improvements, Amex's business model sometimes causes friction with merchants. To maintain the loyalty of its cardholders, Amex must continually invest in its rewards program. But, to fund those investments, Amex must charge merchants higher fees than its rivals. Even though Amex's investments benefit merchants by encouraging cardholders to spend more money, merchants would prefer not to pay the higher fees. One way that merchants try to avoid them, while still enticing Amex's cardholders to shop at their stores, is by dissuading cardholders from using Amex at the point of sale. This practice is known as "steering."

Amex has prohibited steering since the 1950s by placing anti-steering provisions in its contracts with merchants. These anti-steering provisions prohibit merchants from implying a preference for non-Amex cards; dissuading customers from using Amex cards; persuading customers to use other cards; imposing any special restrictions, conditions, disadvantages, or fees on Amex cards; or promoting other cards more than Amex. The anti-steering provisions do not, however, prevent merchants from steering customers toward debit cards, checks, or cash.

C

In October 2010, the United States and several States (collectively, plaintiffs) sued Amex, claiming that its anti-steering provisions violate §1 of the Sherman Act. After a 7-week trial, the District Court agreed that Amex's anti-steering provisions violate §1. It found that the credit-card market should be treated as two separate markets—one for merchants and one for cardholders. Evaluating the effects on the merchant side of the market, the District Court found that Amex's anti-steering provisions are anticompetitive because they result in higher merchant fees.

The Court of Appeals for the Second Circuit reversed. It concluded that the credit-card market is one market, not two. Evaluating the credit card market as a whole, the Second Circuit concluded that Amex's anti-steering provisions were not anticompetitive and did not violate §1. We granted certiorari and now affirm.

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." 15 U. S. C. §1. This Court has long recognized that, "[i]n view of the common law and the law in this country" when the Sherman Act was passed, the phrase "restraint of trade" is best read to mean "undue restraint." *Standard Oil Co. of N. J. v. United States*, 221 U.S. 1, 59-60 (1911). This Court's precedents have thus understood §1 "to outlaw only *unreasonable* restraints." *State Oil Co. v. Khan*, 522 U.S. 3, 10 (1997) (emphasis added).

Restraints can be unreasonable in one of two ways. A small group of restraints are unreasonable per se because they "always or almost always tend to restrict competition and decrease output." *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717, 723 (1988) [cleaned up]. Typically only "horizontal" restraints—restraints "imposed by agreement between competitors"—qualify as unreasonable per se. Id., at 730. Restraints that are not unreasonable per se are judged under the "rule of reason." Id., at 723. The rule of reason requires courts to conduct a fact-specific assessment of "market power and market structure . . . to assess the [restraint]'s actual effect" on competition. *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 768 (1984). The goal is to "distinguis[h] between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest." *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877, 886 (2007).

In this case, both sides correctly acknowledge that Amex's anti-steering provisions are vertical restraints—i.e., restraints "imposed by agreement between firms at different levels of distribution." *Business Electronics*, supra, at 730. The parties also correctly acknowledge that, like nearly every other vertical restraint, the anti-steering provisions should be assessed under the rule of reason.

To determine whether a restraint violates the rule of reason, the parties agree that a three-step, burden shifting framework applies. Under this framework, the plaintiff has the initial burden to prove that the challenged restraint has a substantial anticompetitive effect that harms consumers in the relevant market. If the plaintiff carries its burden, then the burden shifts to the defendant to show a procompetitive rationale for the restraint. If the defendant makes this showing, then the burden shifts back to the plaintiff to demonstrate that the procompetitive efficiencies could be reasonably achieved through less anticompetitive means.

Here, the parties ask us to decide whether the plaintiffs have carried their initial burden of proving that Amex's anti-steering provisions have an anticompetitive effect. The plaintiffs can make this showing directly or indirectly. Direct evidence of anticompetitive effects would be "'proof of actual detrimental effects [on competition],'" *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 460 (1986), such as reduced output, increased prices, or decreased quality in the relevant market. Indirect evidence would be proof of market power plus some evidence that the challenged restraint harms competition.

Here, the plaintiffs rely exclusively on direct evidence to prove that Amex's anti-steering provisions have caused anticompetitive effects in the credit-card market. To assess this evidence, we must first define the relevant market. Once defined, it becomes clear that the plaintiffs' evidence is insufficient to carry their burden.

A

Because "[l]egal presumptions that rest on formalistic distinctions rather than actual market realities are generally disfavored in antitrust law," *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451, 466–467 (1992), courts usually cannot properly apply the rule of reason without an accurate definition of the relevant market.[7] "Without a definition of [the] market there is no way to measure [the defendant's] ability to lessen or destroy competition." *Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp.*, 382 U.S. 172, 177 (1965). Thus, the relevant market is defined as "the area of effective competition." Ibid. Typically this is the "arena within which significant substitution in consumption or production occurs" [citation omitted]. But courts should "combin[e]" different products or services into "a single market" when "that combination reflects commercial realities." *United States v. Grinnell Corp.*, 384 U.S. at 572.

As explained, credit-card networks are two-sided platforms. Due to indirect network effects, two-sided platforms cannot raise prices on one side without risking a feedback loop of declining demand. And the fact that two-sided platforms charge one side a price that is below or above cost reflects differences in the two sides' demand elasticity, not market power or anticompetitive

[7] The plaintiffs argue that we need not define the relevant market in this case because they have offered actual evidence of adverse effects on competition—namely, increased merchant fees. We disagree. The cases that the plaintiffs cite for this proposition evaluated whether horizontal restraints had an adverse effect on competition. Given that horizontal restraints involve agreements between competitors not to compete in some way, this Court concluded that it did not need to precisely define the relevant market to conclude that these agreements were anticompetitive. Vertical restraints often pose no risk to competition unless the entity imposing them has market power, which cannot be evaluated unless the Court first defines the relevant market. See Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 Antitrust L. J. 135, 160 (1984) ("[T]he possibly anticompetitive manifestations of vertical arrangements can occur only if there is market power").

pricing. Price increases on one side of the platform likewise do not suggest anticompetitive effects without some evidence that they have increased the overall cost of the platform's services. Thus, courts must include both sides of the platform—merchants and cardholders—when defining the credit-card market.

To be sure, it is not always necessary to consider both sides of a two-sided platform. A market should be treated as one sided when the impacts of indirect network effects and relative pricing in that market are minor. Newspapers that sell advertisements, for example, arguably operate a two-sided platform because the value of an advertisement increases as more people read the newspaper. But in the newspaper-advertisement market, the indirect networks effects operate in only one direction; newspaper readers are largely indifferent to the amount of advertising that a newspaper contains. Because of these weak indirect network effects, the market for newspaper advertising behaves much like a one-sided market and should be analyzed as such.

But two-sided transaction platforms, like the credit-card market, are different. These platforms facilitate a single, simultaneous transaction between participants. For credit cards, the network can sell its services only if a merchant and cardholder both simultaneously choose to use the network. Thus, whenever a credit-card network sells one transaction's worth of card-acceptance services to a merchant it also must sell one transaction's worth of card payment services to a cardholder. It cannot sell transaction services to either cardholders or merchants individually. To optimize sales, the network must find the balance of pricing that encourages the greatest number of matches between cardholders and merchants.

Because they cannot make a sale unless both sides of the platform simultaneously agree to use their services, two-sided transaction platforms exhibit more pronounced indirect network effects and interconnected pricing and demand. Transaction platforms are thus better understood as "suppl[ying] only one product"—transactions. [Klein, Lerner, Murphy, & Plache, *Competition in Two-Sided Markets: The Antitrust Economics of Payment Card Interchange Fees*, 73 Antitrust L. J. 571, 580 (2006)]. . . . Tellingly, credit cards determine their market share by measuring the volume of transactions they have sold.[8]

Evaluating both sides of a two-sided transaction platform is also necessary to accurately assess competition. Only other two-sided platforms can compete with a two-sided platform for transactions. A credit-card company that processed transactions for merchants, but that had no cardholders willing to use its card, could not compete with Amex. Only a company that had both cardholders and merchants willing to use its network could sell transactions and compete in the credit card market. Similarly, if a merchant accepts the four major credit cards, but a cardholder only uses Visa or Amex, only those two cards can compete for the particular transaction. Thus, competition cannot be accurately assessed by looking at only one side of the platform in isolation.[9]

For all these reasons, in two-sided transaction markets, only one market should be defined. Any other analysis would lead to "mistaken inferences of the kind that could chill the very conduct the antitrust laws are designed to protect." *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 226 (1993) [cleaned up]. Accordingly, we will analyze the two-sided

[8] Contrary to the dissent's assertion, merchant services and cardholder services are not complements. A two-sided market is different from markets for complementary products, in which both products are bought by the same buyers, who, in their buying decisions, can therefore be expected to take into account both prices. . . .

[9] Non-transaction platforms, by contrast, often do compete with companies that do not operate on both sides of their platform. A newspaper that sells advertising, for example, might have to compete with a television network, even though the two do not meaningfully compete for viewers.

market for credit-card transactions as a whole to determine whether the plaintiffs have shown that Amex's anti-steering provisions have anticompetitive effects.

B

The plaintiffs have not carried their burden to prove anticompetitive effects in the relevant market. The plaintiffs stake their entire case on proving that Amex's agreements increase merchant fees. We find this argument unpersuasive. As an initial matter, the plaintiffs' argument about merchant fees wrongly focuses on only one side of the two-sided credit-card market. As explained, the credit-card market must be defined to include both merchants and cardholders. Focusing on merchant fees alone misses the mark because the product that credit-card companies sell is transactions, not services to merchants, and the competitive effects of a restraint on transactions cannot be judged by looking at merchants alone. Evidence of a price increase on one side of a two-sided transaction platform cannot by itself demonstrate an anticompetitive exercise of market power. To demonstrate anticompetitive effects on the two-sided credit-card market as a whole, the plaintiffs must prove that Amex's anti-steering provisions increased the cost of credit-card transactions above a competitive level, reduced the number of credit-card transactions, or otherwise stifled competition in the credit-card market. They failed to do so.

1

The plaintiffs did not offer any evidence that the price of credit-card transactions was higher than the price one would expect to find in a competitive market. As the District Court found, the plaintiffs failed to offer any reliable measure of Amex's transaction price or profit margins. And the evidence about whether Amex charges more than its competitors was ultimately inconclusive.

Amex's increased merchant fees reflect increases in the value of its services and the cost of its transactions, not an ability to charge above a competitive price. . . . As explained, Amex has historically charged higher merchant fees than these competitors because it delivers wealthier cardholders who spend more money. Amex's higher merchant fees are based on a careful study of how much additional value its cardholders offer merchants. On the other side of the market, Amex uses its higher merchant fees to offer its cardholders a more robust rewards program, which is necessary to maintain cardholder loyalty and encourage the level of spending that makes Amex valuable to merchants. That Amex allocates prices between merchants and cardholders differently from Visa and MasterCard is simply not evidence that it wields market power to achieve anticompetitive ends.

In addition, the evidence that does exist cuts against the plaintiffs' view that Amex's anti-steering provisions are the cause of any increases in merchant fees. Visa and MasterCard's merchant fees have continued to increase, even at merchant locations where Amex is not accepted and, thus, Amex's anti-steering provisions do not apply. This suggests that the cause of increased merchant fees is not Amex's anti-steering provisions, but rather increased competition for cardholders and a corresponding marketwide adjustment in the relative price charged to merchants.

2

The plaintiffs did offer evidence that Amex increased the percentage of the purchase price that it charges merchants by an average of 0.09% between 2005 and 2010 and that this increase was not entirely spent on cardholder rewards. . . . [T]his evidence does not prove that Amex's anti-steering provisions gave it the power to charge anticompetitive prices. . . . This Court will "not infer competitive injury from price and output data absent some evidence that tends to prove that output was restricted or prices were above a competitive level." *Brooke Group Ltd.*, 509 U.S., at 237. There is no such evidence in this case. The output of credit-card transactions grew dramatically from 2008 to 2013, increasing 30%. "Where . . . output is expanding at the same time prices are increasing, rising prices are equally consistent with growing product demand." *Brooke Group Ltd.*, supra, at 237. And, as previously explained, the plaintiffs did not show that Amex charged more than its competitors.

3

The plaintiffs also failed to prove that Amex's anti-steering provisions have stifled competition among credit-card companies. To the contrary, while these agreements have been in place, the credit-card market experienced expanding output and improved quality. Amex's business model spurred Visa and MasterCard to offer new premium card categories with higher rewards. And it has increased the availability of card services, including free banking and card-payment services for low-income customers who otherwise would not be served. Indeed, between 1970 and 2001, the percentage of households with credit cards more than quadrupled, and the proportion of households in the bottom-income quintile with credit cards grew from just 2% to over 38%.

Nor have Amex's anti-steering provisions ended competition between credit-card networks with respect to merchant fees. Instead, fierce competition between networks has constrained Amex's ability to raise these fees and has, at times, forced Amex to lower them. For instance, when Amex raised its merchant prices between 2005 and 2010, some merchants chose to leave its network. And when its remaining merchants complained, Amex stopped raising its merchant prices. In another instance in the late 1980s and early 1990s, competition forced Amex to offer lower merchant fees to "everyday spend" merchants—supermarkets, gas stations, pharmacies, and the like—to persuade them to accept Amex.

In addition, Amex's competitors have exploited its higher merchant fees to their advantage. By charging lower merchant fees, Visa, MasterCard, and Discover have achieved broader merchant acceptance—approximately 3 million more locations than Amex. This broader merchant acceptance is a major advantage for these networks and a significant challenge for Amex, since consumers prefer cards that will be accepted everywhere. And to compete even further with Amex, Visa and MasterCard charge different merchant fees for different types of cards to maintain their comparatively lower merchant fees and broader acceptance. Over the long run, this competition has created a trend of declining merchant fees in the credit-card market. In fact, since the first credit card was introduced in the 1950s, merchant fees—including Amex's merchant fees—have decreased by more than half.

Lastly, there is nothing inherently anticompetitive about Amex's anti-steering provisions. These agreements actually stem negative externalities in the credit-card market and promote interbrand competition. When merchants steer cardholders away from Amex at the point of sale, it undermines the cardholder's expectation of "welcome acceptance"—the promise of a frictionless transaction. A lack of welcome acceptance at one merchant makes a cardholder less likely to use Amex at all other merchants. This externality endangers the viability of the entire Amex network. And it undermines the investments that Amex has made to encourage increased cardholder spending, which discourages investments in rewards and ultimately harms both cardholders and merchants. Perhaps most importantly, anti-steering provisions do not prevent Visa, MasterCard, or Discover from competing against Amex by offering lower merchant fees or promoting their broader merchant acceptance.

In sum, the plaintiffs have not satisfied the first step of the rule of reason. They have not carried their burden of proving that Amex's anti-steering provisions have anticompetitive effects. Amex's business model has spurred robust interbrand competition and has increased the quality and quantity of credit-card transactions. . . . Because Amex's anti-steering provisions do not unreasonably restrain trade, we affirm the judgment of the Court of Appeals.

It is so ordered.

BREYER, J., with whom GINSBURG, SOTOMAYOR, and KAGAN, J., join, dissenting: For more than 120 years, the American economy has prospered by charting a middle path between pure laissez-faire and state capitalism, governed by an antitrust law dedicated to the principle that markets, not individual firms and certainly not political power, produce the optimal mixture of goods and services. By means of a strong antitrust law, the United States has sought to avoid the danger of monopoly capitalism. Long gone, we hope, are the days when the great trusts presided unfettered by competition over the American economy.

This lawsuit is emblematic of the American approach. Many governments around the world have responded to concerns about the high fees that credit-card companies often charge merchants by regulating such fees directly. The United States has not followed that approach. The Government instead filed this lawsuit, which seeks to restore market competition over credit-card merchant fees by eliminating a contractual barrier with anticompetitive effects. The majority rejects that effort. But because the challenged contractual term clearly has serious anticompetitive effects, I dissent.

I

I agree with the majority and the parties that this case is properly evaluated under the three-step "rule of reason" that governs many antitrust lawsuits. Under that approach, a court looks first at the agreement or restraint at issue to assess whether it has had, or is likely to have, anticompetitive effects. In doing so, the court normally asks whether the restraint may tend to impede competition and, if so, whether those who have entered into that restraint have sufficient economic or commercial power for the agreement to make a negative difference. Sometimes, but not always, a court will try to determine the appropriate market (the market that the agreement affects) and determine whether those entering into that agreement have the power to raise prices above the competitive level in that market.

It is important here to understand that in cases under §1 of the Sherman Act (unlike in cases challenging a merger under §7 of the Clayton Act, 15 U. S. C. §18), it may well be unnecessary to undertake a sometimes complex, market power inquiry: "Since the purpose [in a Sherman Act §1 case] of the inquiries into . . . market power is [simply] to determine whether an arrangement has the potential for genuine adverse effects on competition, 'proof of actual detrimental effects, such as a reduction in output,' can obviate the need for an inquiry into market power, which is but a 'surrogate for detrimental effects.'" *Indiana Federation of Dentists*, supra, at 460–461.

Second, if an antitrust plaintiff meets the initial burden of showing that an agreement will likely have anticompetitive effects, normally the burden shifts to the defendant to show that the restraint in fact serves a legitimate objective.

Third, if the defendant successfully bears this burden, the antitrust plaintiff may still carry the day by showing that it is possible to meet the legitimate objective in less restrictive ways, or, perhaps by showing that the legitimate objective does not outweigh the harm that competition will suffer, i.e., that the agreement "on balance" remains unreasonable.

Like the Court of Appeals and the parties, the majority addresses only the first step of that three-step framework.

II

A

This case concerns the credit-card business. As the majority explains, that business involves the selling of two different but related card services. First, when a shopper uses a credit card to buy something from a participating merchant, the credit-card company pays the merchant the amount of money that the merchant's customer has charged to his card and charges the merchant a fee, say 5%, for that speedy-payment service. I shall refer to that kind of transaction as a merchant-related card service. Second, the credit-card company then sends a bill to the merchant's customer, the shopper who holds the card; and the shopper pays the card company the sum that merchant charged the shopper for the goods or services he or she bought. The cardholder also often pays the card company a fee, such as an annual fee for the card or an interest charge for delayed payment. I shall call that kind of transaction a shopper-related card service. The credit card company can earn revenue from the sale (directly or indirectly) of each of these services: (1) speedy payment for merchants, and (2) credit for shoppers. (I say "indirectly" to reflect the fact that card companies often create or use networks of banks as part of the process—but I have found nothing here suggesting that that fact makes a significant difference to my analysis.)

Sales of the two basic card services are related. A shopper can pay for a purchase with a particular credit card only if the merchant has signed up for merchant-related card services with the company that issued the credit card that the shopper wishes to use. A firm in the credit-card business is therefore unlikely to make money unless quite a few merchants agree to accept that firm's card and quite a few shoppers agree to carry and use it. In general, the more merchants that sign up with a particular card company, the more useful that card is likely to prove to shoppers and so the more shoppers will sign up; so too, the more shoppers that carry a particular card, the more useful that card is likely to prove to merchants (as it obviously helps them obtain the shoppers' business) and so the more merchants will sign up. Moreover, as a rough rule of thumb (and assuming constant charges), the larger the networks of paying merchants and paying shoppers that a card firm maintains, the larger the revenues that the firm will likely receive, since more payments will be processed using its cards. Thus, it is not surprising that a card company may offer shoppers incentives (say, points redeemable for merchandise or travel) for using its card or that a firm might want merchants to accept its card exclusively.

B

This case focuses upon a practice called "steering." American Express has historically charged higher merchant fees than its competitors. Hence, fewer merchants accept American Express' cards than its competitors'. But, perhaps because American Express cardholders are, on average, wealthier, higher-spending, or more loyal to American Express than other cardholders, vast numbers of merchants still accept American Express cards. Those who do, however, would (in order to avoid the higher American Express fee) often prefer that their customers use a different card to charge a purchase. Thus, the merchant has a monetary incentive to "steer" the customer towards the use of a different card. A merchant might tell the customer, for example, "American Express costs us more," or "please use Visa if you can," or "free shipping if you use Discover."

Steering makes a difference, because without it, the shopper does not care whether the merchant pays more to American Express than it would pay to a different card company—the shopper pays the same price either way. But if steering works, then American Express will find it more difficult to charge more than its competitors for merchant-related services, because merchants will respond by steering their customers, encouraging them to use other cards. Thus, American Express dislikes steering; the merchants like it; and the shoppers may benefit from it, whether because merchants will offer them incentives to use less expensive cards or in the form of lower retail prices overall.

In response to its competitors' efforts to convince merchants to steer shoppers to use less expensive cards, American Express tried to stop, or at least to limit, steering by placing anti-steering provisions in most of its contracts with merchants. It called those provisions "nondiscrimination provisions." They prohibited steering of the forms I have described above (and others as well). After placing them in its agreements, American Express found it could maintain, or even raise, its higher merchant prices without losing too many transactions to other firms. These agreements—the "nondiscrimination provisions"—led to this lawsuit.

C

In 2010 the United States and 17 States brought this antitrust case against American Express. They claimed that the "nondiscrimination provisions" in its contracts with merchants created an unreasonable restraint of trade. (Initially Visa and MasterCard were also defendants, but they entered into consent judgments, dropping similar provisions from their contracts with merchants). After a 7-week bench trial, the District Court entered judgment for the Government, setting forth its findings of fact and conclusions of law in a 97-page opinion.

Because the majority devotes little attention to the District Court's detailed factual findings, I will summarize some of the more significant ones here. Among other things, the District Court found that beginning in 2005 and during the next five years, American Express raised the prices it charged merchants on 20 separate occasions. In doing so, American Express did not take account of the possibility that large merchants would respond to the price increases by encouraging shoppers to use a different credit card because the nondiscrimination provisions prohibited any such steering. The District Court pointed to merchants' testimony stating that, had it not been for those provisions, the large merchants would have responded to the price increases by encouraging customers to use other, less-expensive cards.

The District Court also found that even though American Express raised its merchant prices 20 times in this 5year period, it did not lose the business of any large merchant. Nor did American Express increase benefits (or cut credit-card prices) to American Express cardholders in tandem with the merchant price increases. Even had there been no direct evidence of injury to competition, American Express' ability to raise merchant prices without losing any meaningful market share, in the District Court's view, showed that American Express possessed power in the relevant market.

The District Court also found that, in the absence of the provisions, prices to merchants would likely have been lower. It wrote that in the late 1990's, Discover, one of American Express' competitors, had tried to develop a business model that involved charging lower prices to merchants than the other companies charged. Discover then invited each "merchant to save money by shifting volume to Discover," while simultaneously offering merchants additional discounts "if they would steer customers to Discover." The court determined that these efforts failed because of American Express' (and the other card companies') "nondiscrimination provisions." These provisions, the court found, "denied merchants the ability to express a preference for Discover or to employ any other tool by which they might steer share to Discover's lower-priced network." Because the provisions eliminated any advantage that lower prices might produce, Discover "abandoned its low-price business model" and raised its merchant fees to match those of its competitors. This series of events, the court concluded was "emblematic of the harm done to the competitive process" by the "nondiscrimination provisions."

The District Court added that it found no offsetting procompetitive benefit to shoppers. Indeed, it found no offsetting benefit of any kind. American Express appealed, and the U. S. Court of Appeals for the Second Circuit held in its favor. The Court of Appeals did not reject any fact found by the District Court as "clearly erroneous." Rather, it concluded that the District Court had erred in step 1 of its rule-of-reason analysis by failing to account for what the Second Circuit called the credit-card business's "two-sided market" (or "two-sided platform").

III

The majority, like the Court of Appeals, reaches only step 1 in its "rule of reason" analysis. To repeat, that step consists of determining whether the challenged "nondiscrimination provisions" have had, or are likely to have, anticompetitive effects. Do those provisions tend to impede competition? And if so, does American Express, which imposed that restraint as a condition of doing business with its merchant customers, have sufficient economic or commercial power for the provision to make a negative difference?

A

Here the District Court found that the challenged provisions have had significant anticompetitive effects. In particular, it found that the provisions have limited or prevented price competition among credit-card firms for the business of merchants. That conclusion makes sense: In the provisions, American Express required the merchants to agree not to encourage customers to use American Express' competitors' credit cards, even cards from those competitors, such as Discover, dissenting that intended to charge the merchants lower prices. By doing so, American Express has "disrupt[ed] the normal price-setting mechanism" in the market. As a result of the provisions, the District Court found, American Express was able to raise merchant prices repeatedly without any significant loss of business, because merchants were unable to respond to such price increases by encouraging shoppers to pay with other cards. The provisions also meant that competitors like Discover had little incentive to lower their merchant prices, because doing so did not lead to any additional market share. . . . Consumers throughout the economy paid higher retail prices as a result, and they were denied the opportunity to accept incentives that merchants might otherwise have offered to use less-expensive cards. I should think that, considering step 1 alone, there is little more that need be said.

The majority, like the Court of Appeals, says that the District Court should have looked not only at the market for the card companies' merchant-related services but also at the market for the card companies' shopper-related services, and that it should have combined them, treating them as a single market. But I am not aware of any support for that view in antitrust law. Indeed, this Court has held to the contrary.

In *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 610 (1953), the Court held that an antitrust court should begin its definition of a relevant market by focusing narrowly on the good or service directly affected by a challenged restraint. The Government in that case claimed that a newspaper's advertising policy violated the Sherman Act's "rule of reason.". . . [The Supreme Court] explained that "every newspaper is a dual trader in separate though interdependent markets; it sells the paper's news and advertising content to its readers; in effect that readership is in turn sold to the buyers of advertising space." We then added:

> "This case concerns solely one of those markets. The Publishing Company stands accused not of tying sales to its readers but only to buyers of general and classified space in its papers. For this reason, dominance in the advertising market, not in readership, must be decisive in gauging the legality of the Company's unit plan."

Here, American Express stands accused not of limiting or harming competition for shopper-related card services, but only of merchant-related card services, because the challenged contract provisions appear only in American Express' contracts with merchants. That is why the District Court was correct in considering, at step 1, simply whether the agreement had diminished competition in merchant-related services.

* * *

C

. . . [A] discussion of market definition was legally unnecessary at step 1. That is because the District Court found strong direct evidence of anticompetitive effects flowing from the challenged restraint. As I said, this evidence included Discover's efforts to break into the credit-card business by charging lower prices for merchant-related services, only to find that the "nondiscrimination provisions," by preventing merchants from encouraging shoppers to use Discover cards, meant that lower merchant prices did not result in any additional transactions using Discover credit cards. The direct evidence also included the fact that American Express raised its merchant prices 20 times in five years without losing any appreciable market share. It also included the testimony of numerous merchants that they would have steered shoppers away from American Express cards in response to merchant price increases (thereby checking the ability of American Express to raise prices) had it not been for the nondiscrimination provisions. It included the factual finding that American Express "did not even account for the possibility that [large] merchants would respond to its price increases by attempting to shift share to a competitor's network" because the nondiscrimination provisions prohibited steering. It included the District Court's ultimate finding of fact, not overturned by the Court of Appeals, that the challenged provisions "were integral to" American Express' "[price] increases and thereby caused merchants to pay higher prices."

As I explained above, this Court has stated that "[s]ince the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, proof of actual detrimental effects . . . can obviate the need for" those inquiries. That statement is fully applicable here. Doubts about the District Court's market-definition analysis are beside the point in the face of the District Court's findings of actual anticompetitive harm.

The majority disagrees that market definition is irrelevant. The majority explains that market definition is necessary because the nondiscrimination provisions are "vertical restraints" and "[v]ertical restraints often pose no risk to competition unless the entity imposing them has market power, which cannot be evaluated unless the Court first determines the relevant market." Ante, at n. 7. The majority thus, in a footnote, seems categorically to exempt vertical restraints from the ordinary "rule of reason" analysis that has applied to them since the Sherman Act's enactment in 1890. The majority's only support for this novel exemption is *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877 (2007). But *Leegin* held that the "rule of reason" applied to the vertical restraint at issue in that case. See id., at 898–899. It said nothing to suggest that vertical restraints are not subject to the usual "rule of reason" analysis.

One critical point that the majority's argument ignores is that proof of actual adverse effects on competition is, a fortiori, proof of market power. Without such power, the restraints could not have brought about the anticompetitive effects that the plaintiff proved. See *Indiana Federation of Dentists*, supra, at 460 ("[T]he purpose of the inquiries into market definition and market power is to determine *whether an arrangement has the potential for* genuine adverse effects on competition" (emphasis added)). The District Court's findings of actual anticompetitive harm from the nondiscrimination provisions thus showed that, whatever the relevant market might be, American Express had enough power in that market to cause that harm. There is no reason to require a separate showing of market definition and market power under such circumstances. And so the majority's extensive discussion of market definition is legally unnecessary.

D

The majority's discussion of market definition is also wrong. . . . [T]he majority agrees with the Court of Appeals that the market for American Express' card services is special because it is a "two-sided transaction platform." The majority explains that credit-card firms connect two distinct groups of customers: First, merchants who accept credit cards, and second, shoppers who use the cards. The majority adds that "no credit-card transaction can occur unless both the merchant and the cardholder simultaneously agree to use to the same credit-card network." And it explains that the credit-card market involves "indirect network effects," by which it means that shoppers want a card that many merchants will accept and merchants want to accept those cards that many customers have and use. From this, the majority concludes that "courts must include both sides of the platform—merchants and cardholders—when defining the credit-card market."

1

Missing from the majority's analysis is any explanation as to why, given the purposes that market definition serves in antitrust law, the fact that a credit-card firm can be said to operate a "two-sided transaction platform" means that its merchant-related and shopper-related services should be combined into a single market. . . . The majority defines the phrase as covering a business that "offers different products or services to two different groups who both depend on the platform to intermediate between them," where the business "cannot make a sale to one side of the platform without simultaneously making a sale to the other" side of the platform. I take from that definition that there are four relevant features of such businesses on the majority's account: they (1) offer different products or services, (2) to different groups of customers, (3) whom the "platform" connects, (4) in simultaneous transactions.

What is it about businesses with those four features that the majority thinks justifies a special market definition approach for them? It cannot be the first two features—that the company sells different products to different groups of customers. Companies that sell multiple products to multiple types of customers are commonplace. . . . I have already explained that, ordinarily, antitrust law will not group the two non-substitutable products together for step 1 purposes.

Neither should it normally matter whether a company sells related, or complementary, products, i.e., products which must both be purchased to have any function, such as ignition switches and tires, or cameras and film. It is well established that an antitrust court in such cases looks at the product where the attacked restraint has an anticompetitive effect. The court does not combine the customers for the separate, non-substitutable goods and see if "overall" the restraint has a negative effect. . . .

The majority disputes my characterization of merchant related and shopper related services as "complements." See ante, n. 8. . . . I agree that two-sided platforms—at least as some academics define them—may be distinct from some types of complements in the respect the majority mentions (even though the services resemble complements because they must be used together for either to have value). But the distinction the majority mentions has nothing to do with the relevant question. The relevant question is whether merchant-related and shopper-related services are substitutes, one for the other, so that customers can respond to a price increase for one service by switching to the other service. As I have explained, the two types of services are not substitutes in this way. . . .

What about the last two features—that the company connects the two groups of customers to each other, in simultaneous transactions? That, too, is commonplace. Consider a farmers' market. It brings local farmers and local shoppers together, and transactions will occur only if a farmer and a shopper simultaneously agree to engage in one. Should courts abandon their ordinary step 1 inquiry if several competing farmers' markets in a city agree that only certain kinds of farmers can participate, or if a farmers' market charges a higher fee than its competitors do and prohibits participating farmers from raising their prices to cover it? Why? If farmers' markets are special, what about travel agents that connect airlines and passengers? What about internet retailers, who, in addition to selling their own goods, allow (for a fee) other goods producers to sell over their networks? Each of those businesses seems to meet the majority's four-prong definition.

Apparently as its justification for applying a special market-definition rule to "two-sided transaction platforms," the majority explains that such platforms "often exhibit" what it calls "indirect network effects." By this, the majority means that sales of merchant-related card services and (different) shopper-related card services are interconnected, in that increased merchant-buyers mean increased shopper-buyers (the more stores in the card's network, the more customers likely to use the card), and vice versa. But this, too, is commonplace. Consider, again, a farmers' market. The more farmers that participate (within physical and esthetic limits), the more customers the market will likely attract, and vice versa. So too with travel agents: the more airlines whose tickets a travel agent sells, the more potential passengers will likely use that travel agent, and the more potential passengers that use the travel agent, the easier it will likely be to convince airlines to sell through the travel agent. And so forth. Nothing in antitrust law, to my knowledge, suggests that a court, when presented with an agreement that restricts competition in any one of the markets my examples suggest, should abandon traditional market-definition approaches and include in the relevant market services that are complements, not substitutes, of the restrained good.

* * *

E

Put all of those substantial problems with the majority's reasoning aside, though. Even if the majority were right to say that market definition was relevant, and even if the majority were right to further say that the District Court should have defined the market in this case to include shopper-related services as well as merchant-related services, that still would not justify the majority in affirming the Court of Appeals. That is because, as the majority is forced to admit, the plaintiffs made the factual showing that the majority thinks is required.

Recall why it is that the majority says that market definition matters: because if the relevant market includes both merchant-related services and card-related services, then the plaintiffs had the burden to show that as a result of the nondiscrimination provisions, "the price of credit card transactions"—considering both fees charged to merchants and rewards paid to cardholders— "was higher than the price one would expect to find in a competitive market.". . .

The problem with this reasoning, aside from it being wrong, is that the majority admits that the plaintiffs did show this: they "offer[ed] evidence" that American Express "increased the percentage of the purchase price that it charges merchants . . . and that this increase was not entirely spent on cardholder rewards.". . .

In the face of this problem, the majority retreats to saying that even net price increases do not matter after all, absent a showing of lower output, because if output is increasing, "'rising prices are equally consistent with growing product demand.'" This argument, unlike the price argument, has nothing to do with the credit-card market being a "two-sided transaction platform," so if this is the basis for the majority's holding, then nearly all of the opinion is dicta. The argument is also wrong. It is true as an economic matter that a firm exercises market power by restricting output in order to raise prices. But the relevant restriction of output is as compared with a hypothetical world in which the restraint was not present and prices were lower. The fact that credit-card use in general has grown over the last decade, as the majority says, says nothing about whether such use would have grown more or less without the nondiscrimination provisions. And because the relevant question is a comparison between reality and a hypothetical state of affairs, to require actual proof of reduced output is often to require the impossible—tantamount to saying that the Sherman Act does not apply at all. In any event, there are features of the credit-card market that may tend to limit the usual relationship between price and output. In particular, merchants generally spread the costs of credit-card acceptance across all their customers (whatever payment method they may use), while the benefits of card use go only to the cardholders. Thus, higher credit-card merchant fees may have only a limited effect on credit card transaction volume, even as they disrupt the marketplace by extracting anticompetitive profits.

IV

A

For the reasons I have stated, the Second Circuit was wrong to lump together the two different services sold, at step 1. But I recognize that the Court of Appeals has not yet considered whether the relationship between the two services might make a difference at steps 2 and 3. That is to say, American Express might wish to argue that the nondiscrimination provisions, while anticompetitive in respect to merchant-related services, nonetheless have an adequate offsetting procompetitive benefit in respect to its shopper-related services. I believe that American Express should have an opportunity to ask the Court of Appeals to consider that matter. American

Express might face an uphill battle. A Sherman Act §1 defendant can rarely, if ever, show that a procompetitive benefit in the market for one product offsets an anticompetitive harm in the market for another.

* * *

B

The majority charts a different path. Notwithstanding its purported acceptance of the three-step, burden-shifting framework I have described, the majority addresses American Express' procompetitive justifications now, at step 1 of the analysis. And in doing so, the majority inexplicably ignores the District Court's factual findings on the subject.

The majority reasons that the challenged nondiscrimination provisions "stem negative externalities in the credit card market and promote interbrand competition." The "negative externality" the majority has in mind is this: If one merchant persuades a shopper not to use his American Express card at that merchant's store, that shopper becomes less likely to use his American Express card at other merchants' stores. The majority worries that this "endangers the viability of the entire [American Express] network," but if so that is simply a consequence of American Express' merchant fees being higher than a competitive market will support. . . . If American Express' merchant fees are so high that merchants successfully induce their customers to use other cards, American Express can remedy that problem by lowering those fees or by spending more on cardholder rewards so that cardholders decline such requests. What it may not do is demand contractual protection from price competition.

In any event, the majority ignores the fact that the District Court, in addition to saying what I have just said, also rejected this argument on independent factual grounds. It explained that American Express "presented no expert testimony, financial analysis, or other direct evidence establishing that without its [nondiscrimination provisions] it will, in fact, be unable to adapt its business to a more competitive market." It further explained that the testimony that was provided on the topic "was notably inconsistent," with some of American Express' witnesses saying only that invalidation of the provisions "would require American Express to adapt its current business model." After an extensive discussion of the record, the District Court found that "American Express possesses the flexibility and expertise necessary to adapt its business model to suit a market in which it is required to compete on both the cardholder and merchant sides of the [credit-card] platform." The majority evidently rejects these factual findings, even though no one has challenged them as clearly erroneous.

Similarly, the majority refers to the nondiscrimination provisions as preventing "free riding" on American Express' "investments in rewards" for cardholders. But as the District Court explained, "[p]lainly . . . investments tied to card use (such as Membership Rewards points, purchase protection, and the like) are not subject to free-riding, since the network does not incur any cost if the cardholder is successfully steered away from using his or her American Express card." This, I should think, is an unassailable conclusion: American Express pays rewards to cardholders only for transactions in which cardholders use their American Express cards, so if a steering effort succeeds, no rewards are paid. As for concerns about free riding on American Express' fixed expenses, including its investments in its brand, the District Court acknowledged that free-riding was in theory possible, but explained that American Express "ma[de] no effort to identify the fixed expenses to which its experts referred or to explain how they are subject to free riding.". . . Finally, the majority reasons that the nondiscrimination provisions "do not prevent Visa, MasterCard, or Discover from competing against [American Express] by offering lower merchant fees or promoting their broader merchant acceptance." But again, the District Court's factual findings were to the contrary. As I laid out above, the District Court found that the nondiscrimination provisions in fact did prevent Discover from pursuing a low merchant-fee business model, by "den[ying] merchants the ability to express a preference for Discover or to employ any other tool by which they might steer share to Discover's lower-priced network." The majority's statements that the nondiscrimination provisions are procompetitive are directly contradicted by this and other factual findings.

+ + +

For the reasons I have explained, the majority's decision in this case is contrary to basic principles of antitrust law, and it ignores and contradicts the District Court's detailed factual findings, which were based on an extensive trial record. I respectfully dissent.

Lorain Journal Co. v. United States

342 U.S. 143 (1951)

MR. JUSTICE BURTON delivered the opinion of the Court: The principal question here is whether a newspaper publisher's conduct constituted an attempt to monopolize interstate commerce, justifying the injunction issued against it under §§ 2 and 4 of the Sherman Antitrust Act. For the reasons hereafter stated, we hold that the injunction was justified.

This is a civil action, instituted by the United States in the District Court for the Northern District of Ohio, against The Lorain Journal Company, an Ohio corporation, publishing, daily except Sunday, in the City of Lorain, Ohio, a newspaper here called the Journal. The complaint alleged that the corporation, together with four of its officials, was engaging in a combination and conspiracy in restraint of interstate commerce in violation of § 1 of the Sherman Antitrust Act, and in a combination and conspiracy to monopolize such commerce in violation of § 2 of the Act, as well as attempting to monopolize such commerce in violation of § 2. The District Court declined to issue a temporary injunction but, after trial, found that the parties were engaging in an attempt to monopolize as charged. Confining itself to that issue, the court enjoined them from continuing the attempt. They appealed to this Court under the Expediting Act of 1903, 15 U.S.C. § 29, and the issues before us are those arising from that finding and the terms of the injunction.

The appellant corporation, here called the publisher, has published the Journal in the City of Lorain since before 1932. In that year it, with others, purchased the Times-Herald which was the only competing daily paper published in that city. Later, without success, it sought a license to establish and operate a radio broadcasting station in Lorain.

The court below describes the position of the Journal, since 1933, as "a commanding and an overpowering one. It has a daily circulation in Lorain of over 13,000 copies and it reaches ninety-nine per cent of the families in the city." 92 F.Supp. at 796. Lorain is an industrial city on Lake Erie with a population of about 52,000 occupying 11,325 dwelling units. The Sunday News, appearing only on Sundays, is the only other newspaper published there.[3]

*** From 1933 to 1948 the publisher enjoyed a substantial monopoly in Lorain of the mass dissemination of news and advertising, both of a local and national character. However, in 1948 the Elyria-Lorain Broadcasting Company, a corporation independent of the publisher, was licensed by the Federal Communications Commission to establish and operate in Elyria, Ohio, eight miles south of Lorain, a radio station whose call letters, WEOL, stand for Elyria, Oberlin and Lorain.[4] Since then it has operated its principal studio in Elyria and a branch studio in

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[3] The Sunday News has a weekly circulation of about 3,000 copies, largely in Lorain. The Chronicle-Telegram is a newspaper published daily, except Sunday, eight miles away in Elyria. It has a daily circulation in that city of about 9,000 but none in Lorain. The Cleveland Plain Dealer, News and Press are metropolitan newspapers published daily, except Sunday, in Cleveland, 28 miles east of Lorain. They have a combined daily circulation in Lorain of about 6,000. The Cleveland Sunday Plain Dealer has a Sunday circulation in Lorain of about 11,000. The Cleveland papers carry no Lorain advertising and little Lorain news. No reference has been made in the record or in the argument here to competition from any radio station other than WEOL.

[4] The license also covers WEOL-FM but the two stations are here treated as one. WEOL operates on a frequency of 930 kilocycles and WEOL—FM of 107.6 megacycles. The station outlines its primary listening or market area on the basis of a half millivolt daytime pattern and a two millivolt nighttime pattern. Its day pattern reaches an area containing all or part of 20 counties and an estimated population of over 2,250,000. Its night pattern reaches an area containing parts of nine of these counties and an estimated population of about 450,000. Lorain County, which includes the communities of Lorain, Elyria and Oberlin, contains about 120,000 people, 52,000 of whom live in the City of Lorain.

Lorain. Lorain has about twice the population of Elyria and is by far the largest community in the station's immediate area. Oberlin is much smaller than Elyria and eight miles south of it.

While the station is not affiliated with a national network it disseminates both intrastate and interstate news and advertising. *** Substantially all of the station's income is derived from its broadcasts of advertisements of goods or services. About 16% of its income comes from national advertising under contracts with advertisers outside of Ohio. This produces a continuous flow of copy, payments and materials moving across state lines.

The court below found that appellants knew that a substantial number of Journal advertisers wished to use the facilities of the radio station as well. For some of them it found that advertising in the Journal was essential for the promotion of their sales in Lorain County. It found that at all times since WEOL commenced broadcasting, appellants had executed a plan conceived to eliminate the threat of competition from the station. Under this plan the publisher refused to accept local advertisements in the Journal from any Lorain County advertiser who advertised or who appellants believed to be about to advertise over WEOL. The court found expressly that the purpose and intent of this procedure was to destroy the broadcasting company.

The court characterized all this as "bold, relentless, and predatory commercial behavior." 92 F.Supp. at 796. To carry out appellants' plan, the publisher monitored WEOL programs to determine the identity of the station's local Lorain advertisers. Those using the station's facilities had their contracts with the publisher terminated and were able to renew them only after ceasing to advertise through WEOL. The program was effective. Numerous Lorain County merchants testified that, as a result of the publisher's policy, they either ceased or abandoned their plans to advertise over WEOL.

*** 1. The conduct complained of was an attempt to monopolize interstate commerce. It consisted of the publisher's practice of refusing to accept local Lorain advertising from parties using WEOL for local advertising. Because of the Journal's complete daily newspaper monopoly of local advertising in Lorain and its practically indispensable coverage of 99% of the Lorain families, this practice forced numerous advertisers to refrain from using WEOL for local advertising. That result not only reduced the number of customers available to WEOL in the field of local Lorain advertising and strengthened the Journal's monopoly in that field, but more significantly tended to destroy and eliminate WEOL altogether. Attainment of that sought-for elimination would automatically restore to the publisher of the Journal its substantial monopoly in Lorain of the mass dissemination of all news and advertising, interstate and national, as well as local. It would deprive not merely Lorain but Elyria and all surrounding communities of their only nearby radio station.

*** It is not necessary, however, to rely on the above suggestions. The findings go further. They expressly and unequivocally state that the publisher's conduct was aimed at a larger target—the complete destruction and elimination of WEOL. The court found that the publisher, before 1948, enjoyed a substantial monopoly in Lorain of the mass dissemination not only of local news and advertising, but of news of out-of-state events transmitted to Lorain for immediate dissemination, and of advertising of out-of-state products for sale in Lorain. WEOL offered competition by radio in all these fields so that the publisher's attempt to destroy WEOL was in fact an attempt to end the invasion by radio of the Lorain newspaper's monopoly of interstate as well as local commerce.

*** 2. The publisher's attempt to regain its monopoly of interstate commerce by forcing advertisers to boycott a competing radio station violated § 2. The findings and opinion of the trial court describe the conduct of the publisher upon which the Government relies. The surrounding circumstances are important. The most illuminating of these is the substantial monopoly which was enjoyed in Lorain by the publisher from 1933 to 1948, together with a 99% coverage of Lorain families. Those factors made the Journal an indispensable medium of advertising for many Lorain concerns. Accordingly, its publisher's refusals to print Lorain advertising for those using WEOL for like advertising often amounted to an effective prohibition of the use of WEOL for that purpose. Numerous Lorain advertisers wished to supplement their local newspaper advertising with local radio advertising but could not afford to discontinue their newspaper advertising in order to use the radio.

WEOL's greatest potential source of income was local Lorain advertising. Loss of that was a major threat to its existence. The court below found unequivocally that appellants' conduct amounted to an attempt by the publisher to destroy WEOL and, at the same time, to regain the publisher's pre-1948 substantial monopoly over the mass dissemination of all news and advertising.

To establish this violation of § 2 as charged, it was not necessary to show that success rewarded appellants' attempt to monopolize. The injunctive relief under § 4 sought to forestall that success. While appellants' attempt to monopolize did succeed insofar as it deprived WEOL of income, WEOL has not yet been eliminated. The injunction may save it. "(W)hen that intent (to monopolize) and the consequent dangerous probability exist, this statute (the Sherman Act), 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.

Assuming the interstate character of the commerce involved, it seems clear that if all the newspapers in a city, in order to monopolize the dissemination of news and advertising by eliminating a competing radio station, conspired to accept no advertisements from anyone who advertised over that station, they would violate §§ 1 and 2 of the Sherman Act. Cf. *Fashion Originators' Guild v. Federal Trade Comm.*, 312 U.S. 457, 465. It is consistent with that result to hold here that a single newspaper, already enjoying a substantial monopoly in its area, violates the "attempt to monopolize" clause of § 2 when it uses its monopoly to destroy threatened competition.

The publisher claims a right as a private business concern to select its customers and to refuse to accept advertisement from whomever it pleases. We do not dispute that general right. "But the word 'right' is one of the most deceptive of pitfalls; it is so easy to slip from a qualified meaning in the premise to an unqualified one in the conclusion. Most rights are qualified." *American Bank & Trust Co. v. Federal Reserve Bank,* 256 U.S. 350, 358. The right claimed by the publisher is neither absolute nor exempt from regulation. Its exercise a purposeful means of monopolizing interstate commerce is prohibited by the Sherman Act. The operator of the radio station, equally with the publisher of the newspaper, is entitled to the protection of that Act. *"In the absence of any purpose to create or maintain a monopoly*, the act does 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". (Emphasis supplied.) *United States v. Colgate & Co.*, 250 U.S. 300, 307. *See Associated Press v. United States*, 326 U.S. 1, 15.

United States v. Aluminum Co. of America

148 F.2d 416 (1945)

L. HAND, CIRCUIT JUDGE: This appeal comes to us by virtue of a certificate of the Supreme Court, under the amendment of 1944 to § 29 of 15 U.S.C.A. The action was brought under § 4 of that title, praying the district court to adjudge that the defendant, Aluminum Company of America, was monopolizing interstate and foreign commerce, particularly in the manufacture and sale of "virgin" aluminum ingot, and that it be dissolved. *** The action came to trial on June 1, 1938, and proceeded without much interruption until August 14, 1940, when the case was closed after more than 40,000 pages of testimony had been taken. The judge took time to consider the evidence, and delivered an oral opinion which occupied him from September 30, to October 9, 1941. Again he took time to prepare findings of fact and conclusions of law which he filed on July 14, 1942; and he entered final judgment dismissing the complaint on July 23rd, of that year. The petition for an appeal, and assignments of error, were filed on September 14, 1942, and the petition was allowed on the next day. On June 12, 1944, the Supreme Court, declaring that a quorum of six justices qualified to hear the case was wanting, referred the appeal to this court under § 29 of Title 15, already mentioned. ***

I.

"Alcoa" is a corporation, organized under the laws of Pennsylvania on September 18, 1888. *** It has always been engaged in the production and sale of "ingot" aluminum, and since 1895 also in the fabrication of the metal into many finished and semi-finished articles. It has proliferated into a great number of subsidiaries, created at various times between the years 1900 and 1929, as the business expanded. Aluminum is a chemical element; it is never found in a free state, being always in chemical combination with oxygen. One form of this combination is known as alumina; and for practical purposes the most available material from which alumina can be extracted is an ore, called, "bauxite." Aluminum was isolated as a metal more than a century ago, but not until about 1886 did it become commercially practicable to eliminate the oxygen, so that it could be exploited industrially. One, Hall, discovered a process by which this could be done in that year, and got a patent on April 2, 1889, which he assigned to "Alcoa," which thus secured a legal monopoly of the manufacture of the pure aluminum until on April 2, 1906, when this patent expired. Meanwhile Bradley had invented a process by which the smelting could be carried on without the use of external heat, as had theretofore been thought necessary; and for this improvement he too got a patent on February 2, 1892. Bradley's improvement resulted in great economy in manufacture, so that, although after April 2, 1906, anyone could manufacture aluminum by the Hall process, for practical purposes no one could compete with Bradley or with his licensees until February 2, 1909, when Bradley's patent also expired. On October 31, 1903, "Alcoa" and the assignee of the Bradley patent entered into a contract by which "Alcoa" was granted an exclusive license under that patent, in exchange for "Alcoa's" promise to sell to the assignee a stated amount of aluminum at a discount of ten per cent below "Alcoa's" published list price, and always to sell at a discount of five per cent greater than that which "Alcoa" gave to any other jobber. Thus until February 2, 1909, "Alcoa" had either, a monopoly of the manufacture of "virgin" aluminum ingot, or the monopoly of a process which eliminated all competition.

The extraction of aluminum from alumina requires a very large amount of electrical energy, which is ordinarily, though not always, most cheaply obtained from water power. Beginning at least as early as 1895, "Alcoa" secured such power from several companies by contracts, containing in at least three instances, covenants binding the power companies not to sell or let power to anyone else for the manufacture of aluminum. "Alcoa"—either itself or by a subsidiary—also entered into four successive "cartels" with foreign manufacturers of aluminum by which, in exchange for certain limitations upon its import into foreign countries, it secured covenants from the foreign producers, either not to import into the United States at all, or to do so under restrictions, which in some cases involved the fixing of prices. These "cartels" and restrictive covenants and certain other practices were the subject of a suit filed by the United States against "Alcoa" on May 16, 1912, in which a decree was entered by consent on June 7, 1912, declaring several of these covenants unlawful and enjoining their performance; and also declaring invalid other restrictive covenants obtained before 1903 relating to the sale of alumina. ("Alcoa" failed at this time to inform the United States of several restrictive covenants in water-power contracts; its justification—which the judge accepted—being that they had been forgotten.) "Alcoa" did not begin to manufacture alumina on its own behalf until the expiration of a dominant patent in 1903. In that year it built a very large alumina plant at East St. Louis, where all of its alumina was made until 1939, when it opened another plant in Mobile, Alabama.

None of the foregoing facts are in dispute, and the most important question in the case is whether the monopoly in "Alcoa's" production of "virgin" ingot, secured by the two patents until 1909, and in part perpetuated between 1909 and 1912 by the unlawful practices, forbidden by the decree of 1912, continued for the ensuing twenty-eight years; and whether, if it did, it was unlawful under § 2 of the Sherman Act, 15 U.S.C.A. § 2. It is undisputed that throughout this period "Alcoa" continued to be the single producer of "virgin" ingot in the United States; and the plaintiff argues that this without more was enough to make it an unlawful monopoly. *** We shall first consider the amount and character of this competition; next, how far it established a monopoly; and finally, if it did, whether that monopoly was unlawful under § 2 of the Act.

From 1902 onward until 1928 "Alcoa" was making ingot in Canada through a wholly owned subsidiary; so much of this as it imported into the United States it is proper to include with what it produced here. In the year 1912 the sum of these two items represented nearly ninety-one per cent of the total amount of "virgin" ingot available for sale in this country. This percentage varied year by year up to and including 1938: in 1913 it was about seventy-two per cent; in 1921 about sixty-eight per cent; in 1922 about seventy-two; with these exceptions it was always over eighty per cent of the total and for the last five years 1934-1938 inclusive it averaged over ninety per cent. The effect of such a proportion of the production upon the market we reserve for the time being, for it will be necessary first to consider the nature and uses of "secondary" ingot, the name by which the industry knows ingot made from aluminum scrap. ***

There are various ways of computing "Alcoa's" control of the aluminum market—as distinct from its production—depending upon what one regards as competing in that market. The judge figured its share—during the years 1929-1938, inclusive—as only about thirty-three percent; to do so he included "secondary," and excluded that part of "Alcoa"s own production which it fabricated and did not therefore sell as ingot. If, on the other hand, "Alcoa's" total production, fabricated and sold, be included, and balanced against the sum of imported "virgin" and "secondary," its share of the market was in the neighborhood of sixty-four per cent for that period. The percentage we have already mentioned—over ninety—results only if we both include all "Alcoa's" production and exclude "secondary". That percentage is enough to constitute a monopoly; it is doubtful whether sixty or sixty-four percent would be enough; and certainly thirty-three per cent is not. Hence it is necessary to settle what he shall treat as competing in the ingot market. That part of its production which "Alcoa" itself fabricates, does not of course ever reach the market as ingot; and we recognize that it is only when a restriction of production either inevitably affects prices, or is intended to do so, that it violates § 1 of the Act. *Apex Hosiery Co. v. Leader,* 310 U.S. 469, 501. However, even though we were to assume that a monopoly is unlawful under Sec. 2 only in case it controls prices, the ingot fabricated by "Alcoa," necessarily had a direct effect upon the ingot market. All ingot—with trifling exceptions—is used to fabricate intermediate or end, products; and therefore all intermediate, or end, products which "Alcoa" fabricates and sell, pro tanto reduce the demand for ingot itself. *** We cannot therefore agree that the computation of the percentage of "Alcoa's" control over the ingot market should not include the whole of its ingot production.

As to "secondary," as we have said, for certain purposes the industry will not accept it at all; but for those for which it will, the difference in price is ordinarily not very great; the judge found that it was between one and two cents a pound, hardly enough margin on which to base a monopoly. *** At any given moment therefore "secondary" competes with "virgin" in the ingot market; further, it can, and probably does, set a limit or "ceiling" beyond which the price of "virgin" cannot go, for the cost of its production will in the end depend only upon the expense of scavenging and reconditioning. It might seem for this reason that in estimating "Alcoa's" control over the ingot market, we ought to include the supply of "secondary," as the judge did. Indeed, it may be thought a paradox to say that anyone has the monopoly of a market in which at all times he must meet a competition that limits his price. We shall show that it is not.

In the case of a monopoly of any commodity which does not disappear in use and which can be salvaged, the supply seeking sale at any moment will be made up of two components: (1) the part which the putative monopolist can immediately produce and sell; and (2) the part which has been, or can be, reclaimed out of what he has produced and sold in the past. By hypothesis he presently controls the first of these components; the second he has controlled in the past, although he no longer does. During the period when he did control the second, if he was aware of his interest, he was guided, not alone by its effect at that time upon the market, but by his knowledge that some part of it was likely to be reclaimed and seek the future market. That consideration will to some extent always affect his production until he decides to abandon the business, or for some other reason ceases to be concerned with the future market. Thus, in the case at bar "Alcoa" always knew that the future supply of ingot would be made up in part of what it produced at the time, and, if it was as far-sighted as it proclaims itself, that consideration must have had its share in determining how much to produce. How accurately it could forecast the effect of present production upon the future market is another matter. Experience, no doubt, would help; but it makes no difference that it had to guess; it is enough that it had an inducement to make the best guess it could, and that it would regulate that part of the future supply, so far as it should turn out to have guessed right. The competition of "secondary" must therefore be disregarded, as soon as we consider the position of "Alcoa" over a period of years; it was as much within "Alcoa's" control as was the production of the "virgin" from which it had been derived. ***

We conclude therefore that "Alcoa's" control over the ingot market must be reckoned at over ninety per cent; that being the proportion which its production bears to imported "virgin" ingot. If the fraction which it did not supply were the produce of domestic manufacture there could be no doubt that this percentage gave it a monopoly—lawful or unlawful, as the case might be.

The producer of so large a proportion of the supply has complete control within certain limits. ***

The case at bar is however different, because, for aught that appears there may well have been a practically unlimited supply of imports as the price of ingot rose. Assuming that there was no agreement between "Alcoa" and foreign producers not to import, they sold what could bear the handicap of the tariff and the cost of transportation. For the period of eighteen years—1920-1937—they sold at times a little above "Alcoa's" prices, at times a little under; but there was substantially no gross difference between what they received and what they would have received, had they sold uniformly at "Alcoa's" prices. While the record is silent, we may therefore assume—the plaintiff having the burden—that, had "Alcoa" raised its prices, more ingot would have been imported. Thus there is a distinction between domestic and foreign competition: the first is limited in quantity, and can increase only by an increase in plant and personnel; the second is of producers who, we must assume, produce much more than they import, and whom a rise in price will presumably induce immediately to divert to the American market what they have been selling elsewhere. It is entirely consistent with the evidence that it was the threat of greater foreign imports which kept "Alcoa's" prices where they were, and prevented it from exploiting its advantage as sole domestic producer; indeed, it is hard to resist the conclusion that potential imports did put a "ceiling" upon those prices. Nevertheless, within the limits afforded by the tariff and the cost of transportation, "Alcoa" was free to raise its prices as it chose, since it was free from domestic competition, save as it drew other metals into the market as substitutes. Was this a monopoly within the meaning of § 2? The judge found that, over the whole half century of its existence, "Alcoa's" profits upon capital invested, after payment of income taxes, had been only about ten per cent, and, although the plaintiff puts this figure a little higher, the difference is negligible. The plaintiff does indeed challenge the propriety of computing profits upon a capital base which included past earnings that have been allowed to remain in the business; but as to that it is plainly wrong. An argument is indeed often made in the case of a public utility, that the "rate-base" should not include earnings re-invested which were greater than a fair profit upon the actual investment outstanding at the time. That argument depends, however, upon the premise that at common law—even in the absence of any commission or other authority empowered to enforce a "reasonable" rate—it is the duty of a public utility to charge no more than such a rate, and that any excess is unlawfully collected. Perhaps one might use the same argument in the case of a monopolist; but it would be a condition that one should show what part of the past earning were extortionate, for not all that even a monopolist may earn is *caput lupinum*. The plaintiff made no such attempt, and its distinction between capital, "contributed by consumers" and capital, "contributed by shareholders," has no basis in law. "Alcoa's" earnings belonged to its shareholders, they were free to withdraw them and spend them, or to leave them in the business. If they chose to leave them, it was no different from contributing new capital out of their pockets. This assumed, it would be hard to say that "Alcoa" had made exorbitant profits on ingot, if it is proper to allocate the profit upon the whole business proportionately among all its products—ingot, and fabrications from ingot. A profit of ten per cent in such an industry, dependent, in part at any rate, upon continued tariff protection, and subject to the vicissitudes of new demands, to the obsolescence of plant and process—which can never be accurately gauged in advance—to the chance that substitutes may at any moment be discovered which will reduce the demand, and to the other hazards which attend all industry; a profit of ten per cent, so conditioned, could hardly be considered extortionate.

There are however, two answers to any such excuse; and the first is that the profit on ingot was not necessarily the same as the profit of the business as a whole, and that we have no means of allocating its proper share to ingot. It is true that the mill cost appears; but obviously it would be unfair to "Alcoa" to take, as the measure of its profit on ingot, the difference between selling price and mill cost; and yet we have nothing else. It may be retorted that it was for the plaintiff to prove what was the profit upon ingot in accordance with the general burden of proof. We think not. Having proved that "Alcoa" had a monopoly of the domestic ingot market, the plaintiff had gone far enough; if it was an excuse, that "Alcoa" had not abused its power, it lay upon "Alcoa" to prove that it had not. But the whole issue is irrelevant anyway, for it is no excuse for "monopolizing" a market that the monopoly has not been used to extract from the consumer more than a "fair" profit. The Act has wider purposes. Indeed, even though we disregard all but economic considerations, it would by no means follow that such concentration of producing power is to be desired, when it has not been used extortionately. Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone. Such people believe that competitors, versed in the craft as no consumer can be, will be quick to detect opportunities for saving and new shifts in production, and be eager to profit by them. In any event the mere fact that a producer, having command of the domestic market, has not been able to make more than a "fair" profit, is no evidence that a "fair" profit could not have been made at lower prices. True, it might have been thought adequate to condemn only those monopolies which could not show that they had exercised the highest possible ingenuity, had adopted every possible economy, had anticipated every conceivable improvement, stimulated every possible demand. No doubt, that would be one way of dealing with the matter, although it would imply constant scrutiny and constant supervision, such as courts are unable to provide. Be that as it may, that was not the way that Congress chose; it did not condone "good trusts" and condemn "bad" ones; it forbad all. Moreover, in so doing it was not necessarily actuated by economic motives alone. It is possible, because of its indirect social or moral effect, to prefer a system of small producers, each dependent for his success upon his own skill and character, to one in which the great mass of those engaged must accept the direction of a few. These considerations, which we have suggested only as possible purposes of the Act, we think the decisions prove to have been in fact its purposes.

It is settled, at least as to § 1, that there are some contracts restricting competition which are unlawful, no matter how beneficent they may be; no industrial exigency will justify them; they are absolutely forbidden. *** Starting, however, with the authoritative premise that all contracts fixing prices are unconditionally prohibited, the only possible difference between them and a monopoly is that while a monopoly necessarily involves an equal, or even greater, power to fix prices, its mere existence might be thought not to constitute an exercise of that power. That distinction is nevertheless purely formal; it would be valid only so long as the monopoly remained wholly inert; it would disappear as soon as the monopoly began to operate; for, when it did—that is, as soon as it began to sell at all—it must sell at some price and the only price at which it could sell is a price which it itself fixed. Thereafter the power and its exercise must needs coalesce. Indeed it would be absurd to condemn such contracts unconditionally, and not to extend the condemnation to monopolies; for the contracts are only steps toward that entire control which monopoly confers: they are really partial monopolies.

But we are not left to deductive reasoning. Although in many settings it may be proper to weigh the extent and effect of restrictions in a contract against its industrial or commercial advantages, this is never to be done when the contract is made with intent to set up a monopoly. *** That concerned a combination of dressmakers who set up a boycott against all retailers who should deal in dresses copied—"pirated"—from the dressmakers' designs. Before the Commission the dressmakers had offered to prove that "the practices of FOGA were reasonable and necessary to protect the manufacturer, laborer, retailer and consumer against devastating evils growing from the pirating of original designs and had in fact benefitted all four." (312 U.S. at page 467). All such evidence the Commission refused to hear, raising as sharply as possible the issue whether the combination could excuse itself as "reasonable" because of the benefits it conferred upon the industry. The court sustained the Commission because "the purpose and object of this combination, its potential power, its tendency to monopoly, the coercion it could and did practice upon a rival method of competition, all brought it within the policy of the prohibition", 312 U.S. 457 at page 467. Moreover, the Clayton Act itself, § § 14 and 18, shows that practices harmless in themselves will not be tolerated when they "tend to create a monopoly." Perhaps, it has been idle to labor the point at length; there can be no doubt that the vice of restrictive contracts and of monopoly is really one, it is the denial to commerce of the supposed protection of competition. To repeat, if the earlier stages are proscribed, when they are parts of a plan, the mere projecting of which condemns them unconditionally, the realization of the plan itself must also be proscribed.

We have been speaking only of the economic reasons which forbid monopoly; but, as we have already implied, there are others, based upon the belief that great industrial consolidations are inherently undesirable, regardless of their economic results. In the debates in Congress Senator Sherman himself *** showed that among the purposes of Congress in 1890 was a desire to put an end to great aggregations of capital because of the helplessness of the individual before them. *** Throughout the history of these statutes it has been constantly assumed that one of their purposes was to perpetuate and preserve, for its own sake and in spite of possible cost, an organization of industry in small units which can effectively compete with each other. We hold that "Alcoa's" monopoly of ingot was of the kind covered by § 2.

It does not follow because "Alcoa" had such a monopoly, that it "monopolized" the ingot market: it may not have achieved monopoly; monopoly may have been thrust upon it. If it had been a combination of existing smelters which united the whole industry and controlled the production of all aluminum ingot, it would certainly have "monopolized" the market. In several decisions the Supreme Court has decreed the dissolution of such combinations, although they had engaged in no unlawful trade practices. *** We may start therefore with the premise that to have combined ninety per cent of the producers of ingot would have been to "monopolize" the ingot market; and, so far as concerns the public interest, it can make no difference whether an existing competition is put an end to, or whether prospective competition is prevented. The Clayton Act itself speaks in that alternative: "to injure, destroy, or prevent competition." § 13(a) 15. Nevertheless, it is unquestionably true that from the very outset the courts have at least kept in reserve the possibility that the origin of a monopoly may be critical in determining its legality; and for this they had warrant in some of the congressional debates which accompanied the passage of the Act. This notion has usually been expressed by saying that size does not determine guilt; that there must be some "exclusion" of competitors; that the growth must be something else than "natural" or "normal"; that there must be a "wrongful intent," or some other specific intent; or that some "unduly" coercive means must be used. At times there has been emphasis upon the use of the active verb, "monopolize," as the judge noted in the case at bar. What engendered these compunctions is reasonably plain; persons may unwittingly find themselves in possession of a monopoly, automatically so to say: that is, without having intended either to put an end to existing competition, or to prevent competition from arising when none had existed; they may become monopolists by force of accident. Since the Act makes "monopolizing" a crime, as well as a civil wrong, it would be not only unfair, but presumably contrary to the intent of Congress, to include such instances. A market may, for example, be so limited that it is impossible to produce at all and meet the cost of production except by a plant large enough to supply the whole demand. Or there may be changes in taste or in cost which drive out all but one purveyor. A single producer may be the survivor out of a group of active competitors, merely by virtue of his superior skill, foresight and industry. In such cases a strong argument can be made that, although the result may expose the public to the evils of monopoly, the Act does not mean to condemn the resultant of those very forces which it is its prime object to foster: finis opus coronat. The successful competitor, having been urged to compete, must not be turned upon when he wins. *** "Alcoa's" size was "magnified" to make it a "monopoly"; indeed, it has never been anything else; and its size, not only offered it an "opportunity for abuse," but it "utilized" its size for "abuse," as can easily be shown.

It would completely misconstrue "Alcoa's" position in 1940 to hold that it was the passive beneficiary of a monopoly, following upon an involuntary elimination of competitors by automatically operative economic forces. Already in 1909, when its last lawful monopoly ended, it sought to strengthen its position by unlawful practices, and these concededly continued until 1912. In that year it had two plants in New York, at which it produced less than 42 million pounds of ingot; in 1934 it had five plants (the original two, enlarged; one in Tennessee; one in North Carolina; one in Washington), and its production had risen to about 327 million pounds, an increase of almost eight-fold. Meanwhile not a pound of ingot had been produced by anyone else in the United States. This increase and this continued and undisturbed control did not fall undesigned into "Alcoa's" lap; obviously it could not have done so. It could only have resulted, as it did result, from a persistent determination to maintain the control, with which it found itself vested in 1912. There were at least one or two abortive attempts to enter the industry, but "Alcoa" effectively anticipated and forestalled all competition, and succeeded in holding the field alone. True, it stimulated demand and opened new uses for the metal, but not without making sure that it could supply what it had evoked. There is no dispute as to this; "Alcoa" avows it as evidence of the skill, energy and initiative with which it has always conducted its business; as a reason why, having won its way by fair means, it should be commended, and not dismembered. We need charge it with no moral derelictions after 1912; we may assume that all it claims for itself is true. The only question is whether it falls within the exception established in favor of those who do not seek, but cannot avoid, the control of a market. It seems to us that that question scarcely survives its statement. It was not inevitable that it should always anticipate increases in the demand for ingot and be prepared to supply them. Nothing compelled it to keep doubling and redoubling its capacity before others entered the field. It insists that it never excluded competitors; but we can think of no more effective exclusion than progressively to embrace each new opportunity as it opened, and to face every newcomer with new capacity already geared into a great organization, having the advantage of experience, trade connections and the elite of personnel. Only in case we interpret "exclusion" as limited to maneuvres not honestly industrial, but actuated solely by a desire to prevent competition, can such a course, indefatigably pursued, be deemed not "exclusionary." So to limit it would in our judgment emasculate the Act; would permit just such consolidations as it was designed to prevent. ***

We disregard any question of "intent." Relatively early in the history of the Act—1905—HOLMES, J., in *Swift & Co. v. United States,* [196 U.S. 375, 396](), explained this aspect of the Act in a passage often quoted. Although the primary evil was monopoly, the Act also covered preliminary steps, which, if continued, would lead to it. These may do no harm of themselves; but, if they are initial moves in a plan or scheme which, carried out, will result in monopoly, they are dangerous and the law will nip them in the bud. For this reason conduct falling short of monopoly, is not illegal unless it is part of a plan to monopolize, or to gain such other control of a market as is equally forbidden. To make it so, the plaintiff must prove what in the criminal law is known as a "specific intent"; an intent which goes beyond the mere intent to do the act. By far the greatest part of the fabulous record piled up in the case at bar, was concerned with proving such an intent. The plaintiff was seeking to show that many transactions, neutral on their face, were not in fact necessary to the development of "Alcoa's" business, and had no motive except to exclude others and perpetuate its hold upon the ingot market. Upon that effort success depended in case the plaintiff failed to satisfy the court that it was unnecessary under § 2 to convict "Alcoa" of practices unlawful of themselves. The plaintiff has so satisfied us, and the issue of intent ceases to have any importance; 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. *** So here, "Alcoa" meant to keep, and did keep, that complete and exclusive hold upon the ingot market with which it started. That was to "monopolize" that market, however innocently it otherwise proceeded. So far as the judgment held that it was not within § 2, it must be reversed.

IV. The Remedies.

Nearly five years have passed since the evidence was closed; during that time the aluminum industry, like most other industries, has been revolutionized by the nation's efforts in a great crisis. That alone would make it impossible to dispose of the action upon the basis of the record as we have it; and so both sides agree; both appeal to us to take "judicial notice" of what has taken place meanwhile, though they differ as to what should be the result. The plaintiff wishes us to enter a judgment that "Alcoa" shall be dissolved, and that we shall direct it presently to submit a plan, whose execution, however, is to be deferred until after the war. *** On the other hand, "Alcoa" argues that, when we look at the changes that have taken place—particularly the enormous capacity of plaintiff's aluminum plants—it appears that, even though we should conclude that it had "monopolized" the ingot industry up to 1941, the plaintiff now has in its hands the means to prevent any possible "monopolization" of the industry after the war, which it may use as it wills; and that the occasion has therefore passed forever which might call for, or justify, a dissolution: the litigation has become moot. *** We do not agree with either side; but, before giving our reasons, we must determine for what purposes we may look outside the record. ***

We may, and we do, accept the figures of aluminum production in the report of the so-called "Truman Committee" as of March, 1944, which showed that the annual production of "Alcoa's" plants was about 828 million pounds; that the production of plants owned by the plaintiff which it had leased to "Alcoa," was about 1293 million pounds; and that the production of the Reynolds and Olin plants was together, 202 million pounds: a total of about 2300 million pounds. *** Even though we took "notice" of these, the report would not be conclusive, or more than evidence. We could not constitutionally substitute it for the findings of a court after a trial: facts which a court may judicially "notice" do not for that reason become indisputable. *** For these reasons we refuse to take "notice" of facts relevant to the correctness of the findings; but we do take "notice" of those relevant to remedies.

After doing so, it is impossible to say what will be "Alcoa's" position in the industry after the war. The plaintiff has leased to it all its new plants and the leases do not expire until 1947 and 1948, though they may be surrendered earlier. No one can now forecast in the remotest way what will be the form of the industry after the plaintiff has disposed of these plants, upon their surrender. It may be able to transfer all of them to persons who can effectively compete with "Alcoa"; it may be able to transfer some; conceivably, it may be unable to dispose of any. The measure of its success will be at least one condition upon the propriety of dissolution, and upon the form which it should take, if there is to be any. It is as idle for the plaintiff to assume that dissolution will be proper, as it is for "Alcoa" to assume that it will not be; and it would be particularly fatuous to prepare a plan now, even if we could be sure that eventually some form of dissolution is not a penalty but a remedy; if the industry will not need it for its protection, it will be a disservice to break up an aggregation which has for so long demonstrated its efficiency. The need for such a remedy will be for the district court in the first instance, and there is a peculiar propriety in our saying nothing to control its decision, because the appeal from any judgment which it may enter, will perhaps be justiciable only by the Supreme Court, if there are then six justices qualified to sit. ***

Aspen Skiing Co. v. Aspen Highlands Skiing Corp.

472 U.S. 585 (1985)

JUSTICE STEVENS delivered the opinion of the Court: In a private treble-damages action, the jury found that petitioner Aspen Skiing Company (Ski Co.) had monopolized the market for downhill skiing services in Aspen, Colorado. The question presented is whether that finding is erroneous as a matter of law because it rests on an assumption that a firm with monopoly power has a duty to cooperate with its smaller rivals in a marketing arrangement in order to avoid violating § 2 of the Sherman Act.

I

Aspen is a destination ski resort with a reputation for "super powder," "a wide range of runs," and an "active night life," including "some of the best restaurants in North America." Tr. 765-767. Between 1945 and 1960, private investors independently developed three major facilities for downhill skiing: Aspen Mountain (Ajax),[2] Aspen Highlands (Highlands),[3] and Buttermilk.[4] A fourth mountain, Snowmass,[5] opened in 1967.

The development of any major additional facilities is hindered by practical considerations and regulatory obstacles. The identification of appropriate topographical conditions for a new site and substantial financing are both essential. Most of the terrain in the vicinity of Aspen that is suitable for downhill skiing cannot be used for that purpose without the approval of the United States Forest Service. That approval is contingent, in part, on environmental concerns. Moreover, the county government must also approve the project, and in recent years it has followed a policy of limiting growth.

Between 1958 and 1964, three independent companies operated Ajax, Highlands, and Buttermilk. In the early years, each company offered its own day or half-day tickets for use of its mountain. In 1962, however, the three competitors also introduced an interchangeable ticket. The 6-day, all-Aspen ticket provided convenience to the vast majority of skiers who visited the resort for weekly periods, but preferred to remain flexible about what mountain they might ski each day during the visit. It also emphasized the unusual variety in ski mountains available in Aspen.

As initially designed, the all-Aspen ticket program consisted of booklets containing six coupons, each redeemable for a daily lift ticket at Ajax, Highlands, or Buttermilk. The price of the booklet was often discounted from the price of six daily tickets, but all six coupons had to be

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[2] Ski Co. developed Ajax in 1946. The runs are quite steep and primarily designed for expert or advanced intermediate skiers.

[3] In 1957, the United States Forest Service suggested that Ajax "was getting crowded, and ... that a ski area ought to be started at Highlands." Tr. 150. Whipple V.N. Jones, who owned an Aspen lodge at the time, discussed the project with Ski Co. officials, but they expressed little interest, telling him that they had "plenty of problems at Aspen now, and we don't think we want to expand skiing in Aspen." Id., at 150-151. Jones went ahead with the project on his own, and laid out a well-balanced set of ski runs: 25% beginner, 50% intermediate, 25% advanced. *** Respondent Aspen Highlands Skiing Corporation provides the downhill skiing services at Highlands Mountain. ***

[4] In 1958, Friedl Pfeiffer and Arthur Pfister began developing the ranches they owned at the base of Buttermilk Mountain into a third ski area. Pfeiffer, a former Olympian, was the director of the ski school for Ski Co., and the runs he laid out were primarily for beginners and intermediate skiers. More advanced runs have since been developed. ***

[5] In the early 1960's William Janss, a former ski racer, and his associates had acquired three ranches in the Snowmass Valley, and had secured Forest Service permits for a ski area. The developer sold the company holding the permits to Ski Co. to allow it to develop a downhill skiing facility for the project, leaving him to develop the land at the base of the site. A fairly balanced mountain was developed with a mixture of beginner, intermediate, and advanced runs.

used within a limited period of time—seven days, for example. The revenues from the sale of the 3-area coupon books were distributed in accordance with the number of coupons collected at each mountain.

In 1964, Buttermilk was purchased by Ski Co., but the interchangeable ticket program continued. In most seasons after it acquired Buttermilk, Ski Co. offered 2-area, 6- or 7-day tickets featuring Ajax and Buttermilk in competition with the 3-area, 6-coupon booklet. Although it sold briskly, the all-Aspen ticket did not sell as well as Ski Co.'s multiarea ticket until Ski Co. opened Snowmass in 1967. Thereafter, the all-Aspen coupon booklet began to outsell Ski Co.'s ticket featuring only its mountains.

In the 1971-1972 season, the coupon booklets were discontinued and an "around the neck" all-Aspen ticket was developed. This refinement on the interchangeable ticket was advantageous to the skier, who no longer found it necessary to visit the ticket window every morning before gaining access to the slopes. Lift operators at Highlands monitored usage of the ticket in the 1971-1972 season by recording the ticket numbers of persons going onto the slopes of that mountain. Highlands officials periodically met with Ski Co. officials to review the figures recorded at Highlands, and to distribute revenues based on that count.

There was some concern that usage of the all-Aspen ticket should be monitored by a more scientific method than the one used in the 1971-1972 season. After a one-season absence, the 4-area ticket returned in the 1973-1974 season with a new method of allocating revenues based on usage. Like the 1971-1972 ticket, the 1973-1974 4-area ticket consisted of a badge worn around the skier's neck. Lift operators punched the ticket when the skier first sought access to the mountain each day. A random-sample survey was commissioned to determine how many skiers with the 4-area ticket used each mountain, and the parties allocated revenues from the ticket sales in accordance with the survey's results.

In the next four seasons, Ski Co. and Highlands used such surveys to allocate the revenues from the 4-area, 6-day ticket. Highlands' share of the revenues from the ticket was 17.5% in 1973-1974, 18.5% in 1974-1975, 16.8% in 1975-1976, and 13.2% in 1976-1977. During these four seasons, Ski Co. did not offer its own 3-area, multi-day ticket in competition with the all-Aspen ticket.[9] By 1977, multiarea tickets accounted for nearly 35% of the total market. Holders of multiarea passes also accounted for additional daily ticket sales to persons skiing with them.

Between 1962 and 1977, Ski Co. and Highlands had independently offered various mixes of 1-day, 3-day, and 6-day passes at their own mountains. In every season except one, however, they had also offered some form of all-Aspen, 6-day ticket, and divided the revenues from those sales on the basis of usage. Nevertheless, for the 1977-1978 season, Ski Co. offered to continue the all-Aspen ticket only if Highlands would accept a 13.2% fixed share of the ticket's revenues.

Although that had been Highlands' share of the ticket revenues in 1976-1977, Highlands contended that that season was an inaccurate measure of its market performance since it had been marked by unfavorable weather and an unusually low number of visiting skiers.[11] Moreover,

[9] In 1975, the Colorado Attorney General filed a complaint against Ski Co. and Highlands alleging, in part, that the negotiations over the 4-area ticket had provided them with a forum for price fixing in violation of § 1 of the Sherman Act and that they had attempted to monopolize the market for downhill skiing services in Aspen in violation of § 2. In 1977, the case was settled by a consent decree that permitted the parties to continue to offer the 4-area ticket provided that they set their own ticket prices unilaterally before negotiating its terms.

[11] The 1976-1977 season was "a no snow year." There were less than half as many skier visits (529,800) in that season as in either 1975-1976 (1,238,500) or 1977-1978 (1,273,400). In addition, Highlands opened earlier than Ski Co.'s mountains and its patrons skied off all the good snow. Ski Co. waited until January and had a better base for the rest of the season.

Highlands wanted to continue to divide revenues on the basis of actual usage, as that method of distribution allowed it to compete for the daily loyalties of the skiers who had purchased the tickets. Fearing that the alternative might be no interchangeable ticket at all, and hoping to persuade Ski Co. to reinstate the usage division of revenues, Highlands eventually accepted a fixed percentage of 15% for the 1977-1978 season. No survey was made during that season of actual usage of the 4-area ticket at the two competitors' mountains.

In the 1970's the management of Ski Co. increasingly expressed their dislike for the all-Aspen ticket. They complained that a coupon method of monitoring usage was administratively cumbersome. They doubted the accuracy of the survey and decried the "appearance, deportment, [and] attitude" of the college students who were conducting it. In addition, Ski Co.'s president had expressed the view that the 4-area ticket was siphoning off revenues that could be recaptured by Ski Co. if the ticket was discontinued. In fact, Ski Co. had reinstated its 3-area, 6-day ticket during the 1977-1978 season, but that ticket had been outsold by the 4-area, 6-day ticket nearly two to one.

In March 1978, the Ski Co. management recommended to the board of directors that the 4-area ticket be discontinued for the 1978-1979 season. The board decided to offer Highlands a 4-area ticket provided that Highlands would agree to receive a 12.5% fixed percentage of the revenue—considerably below Highlands' historical average based on usage. Later in the 1978-1979 season, a member of Ski Co.'s board of directors candidly informed a Highlands official that he had advocated making Highlands "an offer that [it] could not accept."

Finding the proposal unacceptable, Highlands suggested a distribution of the revenues based on usage to be monitored by coupons, electronic counting, or random sample surveys. If Ski Co. was concerned about who was to conduct the survey, Highlands proposed to hire disinterested ticket counters at its own expense—"somebody like Price Waterhouse"—to count or survey usage of the 4-area ticket at Highlands. Ski Co. refused to consider any counterproposals, and Highlands finally rejected the offer of the fixed percentage.

As far as Ski Co. was concerned, the all-Aspen ticket was dead. In its place Ski Co. offered the 3-area, 6-day ticket featuring only its mountains. In an effort to promote this ticket, Ski Co. embarked on a national advertising campaign that strongly implied to people who were unfamiliar with Aspen that Ajax, Buttermilk, and Snowmass were the only ski mountains in the area. For example, Ski Co. had a sign changed in the Aspen Airways waiting room at Stapleton Airport in Denver. The old sign had a picture of the four mountains in Aspen touting "Four Big Mountains" whereas the new sign retained the picture but referred only to three.

Ski Co. took additional actions that made it extremely difficult for Highlands to market its own multiarea package to replace the joint offering. Ski Co. discontinued the 3-day, 3-area pass for the 1978-1979 season,[13] and also refused to sell Highlands any lift tickets, either at the tour operator's discount or at retail. Highlands finally developed an alternative product, the "Adventure Pack," which consisted of a 3-day pass at Highlands and three vouchers, each equal to the price of a daily lift ticket at a Ski Co. mountain. The vouchers were guaranteed by funds on deposit in an Aspen bank, and were redeemed by Aspen merchants at full value. Ski Co., however, refused to accept them.

[13] Highlands' owner explained that there was a key difference between the 3-day, 3-area ticket and the 6-day, 3-area ticket: "with the three day ticket, a person could ski on the ... Aspen Skiing Corporation mountains for three days and then there would be three days in which he could ski on our mountain; but with the six-day ticket, we are absolutely locked out of those people." As a result of "tremendous consumer demand" for a 3-day ticket, Ski Co. reinstated it late in the 1978-1979 season, but without publicity or a discount off the daily rate.

Later, Highlands redesigned the Adventure Pack to contain American Express Traveler's Checks or money orders instead of vouchers. Ski Co. eventually accepted these negotiable instruments in exchange for daily lift tickets.[15] ***

Without a convenient all-Aspen ticket, Highlands basically "becomes a day ski area in a destination resort." Highlands' share of the market for downhill skiing services in Aspen declined steadily after the 4-area ticket based on usage was abolished in 1977: from 20.5% in 1976-1977, to 15.7% in 1977-1978, to 13.1% in 1978-1979, to 12.5% in 1979-1980, to 11% in 1980-1981. ***

II

In 1979, Highlands filed a complaint in the United States District Court for the District of Colorado naming Ski Co. as a defendant. Among various claims, the complaint alleged that Ski Co. had monopolized the market for downhill skiing services at Aspen in violation of § 2 of the Sherman Act, and prayed for treble damages. The case was tried to a jury which rendered a verdict finding Ski Co. guilty of the § 2 violation and calculating Highlands' actual damages at $2.5 million.

In her instructions to the jury, the District Judge explained that the offense of monopolization under § 2 of the Sherman Act has two elements: (1) the possession of monopoly power in a relevant market, and (2) the willful acquisition, maintenance, or use of that power by anticompetitive or exclusionary means or for anticompetitive or exclusionary purposes. Although the first element was vigorously disputed at the trial and in the Court of Appeals, in this Court Ski Co. does not challenge the jury's special verdict finding that it possessed monopoly power.[20] Nor does Ski Co. criticize the trial court's instructions to the jury concerning the second element of the § 2 offense.

On this element, the jury was instructed that it had to consider whether "Aspen Skiing Corporation willfully acquired, maintained, or used that power by anti-competitive or exclusionary means or for anti-competitive or exclusionary purposes." The instructions elaborated: "In considering whether the means or purposes were anti-competitive or exclusionary, you must draw a distinction here between practices which tend to exclude or restrict competition on the one hand and the success of a business which reflects only a superior product, a well-run business, or luck, on the other. The line between legitimately gained monopoly, its proper use and maintenance, and improper conduct has been described in various ways. It has been said that obtaining or maintaining monopoly power cannot represent monopolization if the power was gained and maintained by conduct that was honestly industrial. Or it is said that monopoly power which is thrust upon a firm due to its superior business ability and efficiency does not constitute monopolization. "For example, a firm that has lawfully acquired a monopoly position is not barred from taking advantage of scale economies by constructing a large and efficient factory. These benefits are a consequence of size and not an exercise of monopoly power. Nor is a corporation which possesses monopoly power under a duty to cooperate with its business rivals. Also a company which possesses monopoly power and which refuses to enter into a joint operating agreement with a competitor or otherwise refuses to deal with a competitor in some manner

[15] *** For the 1981-1982 season, Ski Co. set its single ticket price at $22 and discounted the 3-area, 6-day ticket to $114. According to Highlands, this price structure made the Adventure Pack unprofitable.

[20] The jury found that the relevant product market was "[d]ownhill skiing at destination ski resorts," that the "Aspen area" was a relevant geographic submarket, and that during the years 1977-1981, Ski Co. possessed monopoly power, defined as the power to control prices in the relevant market or to exclude competitors.

does not violate Section 2 if valid business reasons exist for that refusal. "In other words, if there were legitimate business reasons for the refusal, then the defendant, even if he is found to possess monopoly power in a relevant market, has not violated the law. We are concerned with conduct which unnecessarily excludes or handicaps competitors. This is conduct which does not benefit consumers by making a better product or service available—or in other ways—and instead has the effect of impairing competition. "To sum up, you must determine whether Aspen Skiing Corporation gained, maintained, or used monopoly power in a relevant market by arrangements and policies which rather than being a consequence of a superior product, superior business sense, or historic element, were designed primarily to further any domination of the relevant market or sub-market." The jury answered a specific interrogatory finding the second element of the offense as defined in these instructions. ***

The Court of Appeals affirmed in all respects. 738 F.2d 1509 (CA10 1984). The court advanced two reasons for rejecting Ski Co.'s argument that "'there was insufficient evidence to present a jury issue of monopolization because, as a matter of law, the conduct at issue was pro-competitive conduct that a monopolist could lawfully engage in.'" First, relying on *United States v. Terminal Railroad Assn. of St. Louis*, 224 U.S. 383 (1912), the Court of Appeals held that the multiday, multiarea ticket could be characterized as an "essential facility" that Ski Co. had a duty to market jointly with Highlands. Second, it held that there was sufficient evidence to support a finding that Ski Co.'s intent in refusing to market the 4-area ticket, "considered together with its other conduct," was to create or maintain a monopoly. ***

III

In this Court, Ski Co. contends that even a firm with monopoly power has no duty to engage in joint marketing with a competitor, that a violation of § 2 cannot be established without evidence of substantial exclusionary conduct, and that none of its activities can be characterized as exclusionary. It also contends that the Court of Appeals incorrectly relied on the "essential facilities" doctrine and that an "anticompetitive intent" does not transform nonexclusionary conduct into monopolization. In response, Highlands submits that, given the evidence in the record, it is not necessary to rely on the "essential facilities" doctrine in order to affirm the judgment.

"The central message of the Sherman Act is that a business entity must find new customers and higher profits through internal expansion—that is, by competing successfully rather than by arranging treaties with its competitors." *United States v. Citizens & Southern National Bank*, 422 U.S. 86, 116 (1975). Ski Co., therefore, is surely correct in submitting that even a firm with monopoly power has no general duty to engage in a joint marketing program with a competitor. Ski Co. is quite wrong, however, in suggesting that the judgment in this case rests on any such proposition of law. For the trial court unambiguously instructed the jury that a firm possessing monopoly power has no duty to cooperate with its business rivals.

The absence of an unqualified duty to cooperate does not mean that every time a firm declines to participate in a particular cooperative venture, that decision may not have evidentiary significance, or that it may not give rise to liability in certain circumstances. The absence of a duty to transact business with another firm is, in some respects, merely the counterpart of the independent businessman's cherished right to select his customers and his associates. The high value that we have placed on the right to refuse to deal with other firms does not mean that the right is unqualified.

In *Lorain Journal Co. v. United States*, 342 U.S. 143 (1951), we squarely held that this right was not unqualified. *** In *Lorain Journal*, the violation of § 2 was an "attempt to monopolize," rather than monopolization, but the question of intent is relevant to both offenses. In the former case it is necessary to prove a "specific intent" to accomplish the forbidden objective—as Judge Hand explained, "an intent which goes beyond the mere intent to do the act." *United States v. Aluminum Co. of America*, 148 F.2d 416, 432 (CA2 1945). In the latter case evidence of intent is merely relevant to the question whether the challenged conduct is fairly characterized as "exclusionary" or "anticompetitive"—to use the words in the trial court's instructions—or "predatory," to use a word that scholars seem to favor. Whichever label is used, there is agreement on the proposition that "no monopolist monopolizes unconscious of what he is doing." ***

The qualification on the right of a monopolist to deal with whom he pleases is not so narrow that it encompasses no more than the circumstances of *Lorain Journal*. In the actual case that we must decide, the monopolist did not merely reject a novel offer to participate in a cooperative venture that had been proposed by a competitor. Rather, the monopolist elected to make an important change in a pattern of distribution that had originated in a competitive market and had persisted for several years. The all-Aspen, 6-day ticket with revenues allocated on the basis of usage was first developed when three independent companies operated three different ski mountains in the Aspen area. It continued to provide a desirable option for skiers when the market was enlarged to include four mountains, and when the character of the market was changed by Ski Co.'s acquisition of monopoly power. Moreover, since the record discloses that interchangeable tickets are used in other multimountain areas which apparently are competitive, it seems appropriate to infer that such tickets satisfy consumer demand in free competitive markets.

Ski Co.'s decision to terminate the all-Aspen ticket was thus a decision by a monopolist to make an important change in the character of the market. *** Since the jury was unambiguously instructed that Ski Co.'s refusal to deal with Highlands "does not violate Section 2 if valid business reasons exist for that refusal," we must assume that the jury concluded that there were no valid business reasons for the refusal. The question then is whether that conclusion finds support in the record.

IV

The question whether Ski Co.'s conduct may properly be characterized as exclusionary cannot be answered by simply considering its effect on Highlands. In addition, it is relevant to consider its impact on consumers and whether it has impaired competition in an unnecessarily restrictive way. If a firm has been "attempting to exclude rivals on some basis other than efficiency,"[33] it is fair to characterize its behavior as predatory. It is, accordingly, appropriate to examine the effect of the challenged pattern of conduct on consumers, on Ski Co.'s smaller rival, and on Ski Co. itself.

Superior Quality of the All-Aspen Ticket

The average Aspen visitor "is a well-educated, relatively affluent, experienced skier who has skied a number of times in the past...." Over 80% of the skiers visiting the resort each year have been there before—40% of these repeat visitors have skied Aspen at least five times. Over the

[33] R. Bork, *The Antitrust Paradox* 138 (1978).

years, they developed a strong demand for the 6-day, all-Aspen ticket in its various refinements. Most experienced skiers quite logically prefer to purchase their tickets at once for the whole period that they will spend at the resort; they can then spend more time on the slopes and enjoying apres-ski amenities and less time standing in ticket lines. The 4-area attribute of the ticket allowed the skier to purchase his 6-day ticket in advance while reserving the right to decide in his own time and for his own reasons which mountain he would ski on each day. It provided convenience and flexibility, and expanded the vistas and the number of challenging runs available to him during the week's vacation.

While the 3-area, 6-day ticket offered by Ski Co. possessed some of these attributes, the evidence supports a conclusion that consumers were adversely affected by the elimination of the 4-area ticket. In the first place, the actual record of competition between a 3-area ticket and the all-Aspen ticket in the years after 1967 indicated that skiers demonstrably preferred four mountains to three. Highlands' expert marketing witness testified that many of the skiers who come to Aspen want to ski the four mountains, and the abolition of the 4-area pass made it more difficult to satisfy that ambition. A consumer survey undertaken in the 1979-1980 season indicated that 53.7% of the respondents wanted to ski Highlands, but would not; 39.9% said that they would not be skiing at the mountain of their choice because their ticket would not permit it.

Expert testimony and anecdotal evidence supported these statistical measures of consumer preference. A major wholesale tour operator asserted that he would not even consider marketing a 3-area ticket if a 4-area ticket were available. During the 1977-1978 and 1978-1979 seasons, people with Ski Co.'s 3-area ticket came to Highlands "on a very regular basis" and attempted to board the lifts or join the ski school. Highlands officials were left to explain to angry skiers that they could only ski at Highlands or join its ski school by paying for a 1-day lift ticket. Even for the affluent, this was an irritating situation because it left the skier the option of either wasting 1 day of the 6-day, 3-area pass or obtaining a refund which could take all morning and entailed the forfeit of the 6-day discount. An active officer in the Atlanta Ski Club testified that the elimination of the 4-area pass "infuriated" him.

Highlands' Ability to Compete

The adverse impact of Ski Co.'s pattern of conduct on Highlands is not disputed in this Court. Expert testimony described the extent of its pecuniary injury. The evidence concerning its attempt to develop a substitute product either by buying Ski Co.'s daily tickets in bulk, or by marketing its own Adventure Pack, demonstrates that it tried to protect itself from the loss of its share of the patrons of the all-Aspen ticket. The development of a new distribution system for providing the experience that skiers had learned to expect in Aspen proved to be prohibitively expensive. As a result, Highlands' share of the relevant market steadily declined after the 4-area ticket was terminated. The size of the damages award also confirms the substantial character of the effect of Ski Co.'s conduct upon Highlands.

Ski Co.'s Business Justification

Perhaps most significant, however, is the evidence relating to Ski Co. itself, for Ski Co. did not persuade the jury that its conduct was justified by any normal business purpose. Ski Co. was apparently willing to forgo daily ticket sales both to skiers who sought to exchange the coupons contained in Highlands' Adventure Pack, and to those who would have purchased Ski Co. daily lift tickets from Highlands if Highlands had been permitted to purchase them in bulk. The jury may well have concluded that Ski Co. elected to forgo these short-run benefits because it was more interested in reducing competition in the Aspen market over the long run by harming its smaller competitor.

That conclusion is strongly supported by Ski Co.'s failure to offer any efficiency justification whatever for its pattern of conduct. In defending the decision to terminate the jointly offered ticket, Ski Co. claimed that usage could not be properly monitored. The evidence, however, established that Ski Co. itself monitored the use of the 3-area passes based on a count taken by lift operators, and distributed the revenues among its mountains on that basis. Ski Co. contended that coupons were administratively cumbersome, and that the survey takers had been disruptive and their work inaccurate. Coupons, however, were no more burdensome than the credit cards accepted at Ski Co. ticket windows. Moreover, in other markets Ski Co. itself participated in interchangeable lift tickets using coupons.

In the end, Ski Co. was pressed to justify its pattern of conduct on a desire to disassociate itself from—what it considered the inferior skiing services offered at Highlands. The all-Aspen ticket based on usage, however, allowed consumers to make their own choice on these matters of quality. Ski Co.'s purported concern for the relative quality of Highlands' product was supported in the record by little more than vague insinuations, and was sharply contested by numerous witnesses. Moreover, Ski Co. admitted that it was willing to associate with what it considered to be inferior products in other markets.

Although Ski Co.'s pattern of conduct may not have been as "'bold, relentless, and predatory'" as the publisher's actions in *Lorain Journal*, the record in this case comfortably supports an inference that the monopolist made a deliberate effort to discourage its customers from doing business with its smaller rival. The sale of its 3-area, 6-day ticket, particularly when it was discounted below the daily ticket price, deterred the ticket holders from skiing at Highlands. The refusal to accept the Adventure Pack coupons in exchange for daily tickets was apparently motivated entirely by a decision to avoid providing any benefit to Highlands even though accepting the coupons would have entailed no cost to Ski Co. itself, would have provided it with immediate benefits, and would have satisfied its potential customers. Thus the evidence supports an inference that Ski Co. was not motivated by efficiency concerns and that it was willing to sacrifice short-run benefits and consumer goodwill in exchange for a perceived long-run impact on its smaller rival.

Because we are satisfied that the evidence in the record,[44] construed most favorably in support of Highlands' position, is adequate to support the verdict under the instructions given by the trial court, the judgment of the Court of Appeals is

Affirmed.

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[44] Given our conclusion that the evidence amply supports the verdict under the instructions as given by the trial court, we find it unnecessary to consider the possible relevance of the "essential facilities" doctrine, or the somewhat hypothetical question whether nonexclusionary conduct could ever constitute an abuse of monopoly power if motivated by an anticompetitive purpose. If, as we have assumed, no monopolist monopolizes unconscious of what he is doing, that case is unlikely to arise.

United States v. AMR

335 F.3d 1109 (10th Cir. 2003)

LUCERO, CIRCUIT JUDGE: This case involves the nature of permissible competitive practices in the airline industry under the antitrust laws of this country, centered around the hub-and-spoke system of American Airlines. The United States brought this suit against AMR Corporation, American Airlines, Inc., and American Eagle Holding Corporation ("American"), alleging monopolization and attempted monopolization through predatory pricing in violation of § 2 of the Sherman Act, 15 U.S.C. § 2. In essence, the government alleges that American engaged in multiple episodes of price predation in four city-pair airline markets, all connected to American's hub at Dallas/Fort Worth International Airport ("DFW"), with the ultimate purpose of using the reputation for predatory pricing it earned in those four markets to defend a monopoly at its DFW hub.[1] At its root, the government's complaint alleges that American: (1) priced its product on the routes in question below cost; and (2) intended to recoup these losses by charging supracompetitive prices either on the four core routes themselves, or on those routes where it stands to exclude competition by means of its "reputation for predation." Finding that the government failed to demonstrate the existence of a genuine issue of material fact as to either of these allegations, the district court granted summary judgment in favor of American, from which the government now appeals. ***

I

Airlines are predominantly organized in a hub-and-spoke system, with traffic routed such that passengers leave their origin city for an intermediate hub airport. Passengers traveling to a concentrated hub tend to pay higher average fares than those traveling on comparable routes that do not include a concentrated hub as an endpoint. This is known as the "hub premium" and a major airline's hub is often an important profit center. Entry of low cost carriers ("LCCs") into a hub market tends to drive down the fares charged by major carriers. Consequently, major carriers generally enjoy higher margins on routes where they do not face LCC competition.

Both American and Delta Airlines ("Delta") maintain hubs at DFW, though Delta's presence is considerably smaller than American's. As of May 2000, American's share of passengers boarded at DFW was 70.2%, Delta's share was roughly 18%, and LCC share was 2.4%. As of mid-2000, there were seven low-cost airlines serving DFW. In the period between 1997 to 2000, five new low-cost airlines entered DFW: American Trans Air, Frontier, National, Sun Country, and Ozark. DFW has more low-fare airlines than any other hub airport and the number of passengers carried by low-fare airlines increased by over 30% from May 1999 to May 2000. Nevertheless, LCCs have a significantly higher market share in some other major U.S. hubs.

LCCs generally enjoy the advantage of having lower costs than major carriers, allowing them to offer lower fares than their major-airline competitors.[3] During the period between 1995 and 1997, a number of LCCs, including Vanguard, Western Pacific, and Sunjet, began to take advantage of these lower costs by entering certain city-pair routes serving DFW and charging lower fares than American. The instant case primarily involves DFW-Kansas City, DFW-Wichita, DFW-Colorado Springs, and DFW-Long Beach.

[1] The four "core" routes are DFW-Kansas City, DFW-Wichita, DFW-Colorado Springs, and DFW-Long Beach.

[3] For example, in 1994, American calculated ValuJet's stage-length adjusted cost per available seat mile to be 4.32 cents, and American's to be 8.54 cents. Southwest has costs that are 30% lower than American's.

American responded to lower LCC fares on these routes with changes in: (1) pricing (matching LCC prices); (2) capacity (adding flights or switching to larger planes); and (3) yield management (making more seats available at the new, lower prices). By increasing capacity, American overrode its own internal capacity-planning models for each route, which had previously indicated that such increases would be unprofitable. In each instance, American's response produced the same result: the competing LCC failed to establish a presence, moved its operations, or ceased its separate existence entirely. Once the LCC ceased or moved its operations, American generally resumed its prior marketing strategy, reducing flights and raising prices to levels roughly comparable to those prior to the period of low-fare competition. Capacity was reduced after LCC exit, but usually remained higher than prior to the alleged episode of predatory activity.[4]

The government filed suit on May 13, 1999, alleging that American participated in a scheme of predatory pricing in violation of § 2 of the Sherman Act. In the government's view, American's combined response of lowering prices, increasing capacity, and altering yield management in response to LCC competition constituted an unlawful, anticompetitive response. After reviewing a voluminous record and receiving extensive briefs the district court granted American's motion for summary judgment on all antitrust claims, concluding that the government failed to demonstrate the existence of a genuine issue of material fact as to (1) whether American had priced below cost and (2) whether American had a dangerous probability of recouping its alleged investment in below-cost prices.

II

*** Monopolization claims under § 2 of the Sherman Act require proof: (1) that a firm has monopoly power in a properly defined relevant market; and (2) that it willfully acquired or maintained this power by means of anticompetitive conduct. *TV Communications Network, Inc. v. Turner Network Television, Inc.,* 964 F.2d 1022, 1025 (10th Cir. 1992). This is to be distinguished from a business that acquired monopoly power by greater skill, efficiency, or by "building a better mousetrap." Claims of attempted monopolization under § 2 of the Sherman Act require four elements of proof: (1) a relevant geographic and product market; (2) specific intent to monopolize the market; (3) anticompetitive conduct in furtherance of the attempt; and (4) a dangerous probability that the firm will succeed in the attempt. *Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal and Prof'l Publ'ns, Inc.,* 63 F.3d 1540, 1550 (10th Cir. 1995).

[4] This pattern is illustrated by the average fares and passengers on the DFW-Wichita route before, during, and after one of the alleged episodes of predation:

	Pre-"predation" 06/94-05/95	"Predatory" Period 10/96-12/96	Post-"predation" 07/97-06/98	Post-"predation" 07/98-06/99
Average fare	$99-108	$58-61	$88-102	$100-123
Average monthly passengers	3,932-5,557	10,076-11,041	7,019-8,373	5,744-8,257
Average monthly seats	21,314-32,109	44,798-47,588	29,939-33,790	25,891-33,790

In the instant case, the anticompetitive conduct at issue is predatory pricing. The crux of the government's argument is that the "incremental" revenues and costs specifically associated with American's capacity additions show a loss. Because American spent more to add capacity than the revenues generated by the capacity additions, such capacity additions made no economic sense unless American intended to drive LCCs out of the market. Under the government's theory, American attempted to monopolize the four city-pair routes in question in order to develop a reputation as an exceedingly aggressive competitor and set an example to all potential competitors. Fearing American's predatory response, the theory goes, future potential competitors will decline to enter other DFW market routes and compete. If American succeeds in preventing or at least forestalling the formation of an LCC hub at DFW, it will then be able to charge higher prices on other DFW routes and thereby recoup the losses it incurred from its "capacity dumping" on the four core routes.

III

Scholars from the Chicago School of economic thought have long labeled predatory pricing as implausible and irrational. *** Commentators viewed below-cost pricing as irrational largely because of the uncertainty of recouping losses through later price increases. In order for a predatory pricing scheme to be successful, two future events had to take place: first, the victim of the alleged predation would have to exit and second, the predator would have to generate profits in excess of its initial losses.

In two seminal antitrust opinions, the Supreme Court adopted the skepticism of Chicago scholars, observing that "there is a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.,* 475 U.S. 574, 589 (1986); *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.,* 509 U.S. 209, 226 (1993). Implausibility of predatory pricing schemes was said to flow from the fact that their success is inherently uncertain. *Matsushita,* 475 U.S. at 598. While "the short-run loss is definite ... the long-run gain depends on successfully neutralizing the competition." *Id.* Moreover, "[t]he success of any predatory scheme depends on *maintaining* monopoly power for long enough both to recoup the predator's losses and to harvest some additional gain." *Id.*

Furthermore, caution in predatory pricing cases is the watchword as "the costs of an erroneous finding are high." *Brooke Group,* 509 U.S. at 227. Because "the mechanism by which a firm engages in predatory pricing—lowering prices—is the same mechanism by which a firm stimulates competition," mistaken inferences may deter the very conduct the antitrust laws were created to protect. *Cargill Inc. v. Monfort of Colo.,* 479 U.S. 104, 122 (1986) (quotation omitted).

Recent scholarship has challenged the notion that predatory pricing schemes are implausible and irrational. *See, e.g.,* Patrick Bolton et al., *Predatory Pricing: Strategic Theory and Legal Policy,* 88 Geo. L.J. 2239, 2241 (2000) ("Modern economic analysis has developed coherent theories of predation that contravene earlier economic writing claiming that predatory pricing conduct is irrational."). Post-Chicago economists have theorized that price predation is not only plausible, but profitable, especially in a multi-market context where predation can occur in one market and recoupment can occur rapidly in other markets.

Although this court approaches the matter with caution, we do not do so with the incredulity that once prevailed.

IV

The Supreme Court has formulated two prerequisites to recovery on a predatory pricing claim, conditions that "are not easy to establish." *Brooke Group,* 509 U.S. at 227. First, the government must prove that "the prices complained of are below an appropriate measure of [American's] costs." *Id.* at 223. While the first element is crucial, "[t]hat below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured." *Id.* at 225. Thus, the second prerequisite to recovery on a predatory pricing claim, a demonstration that American had "a dangerous probability of recouping its investment in below-cost prices," must also be met. *Id.* at 224. Without a dangerous probability of recoupment, competition remains unharmed even if individual competitors suffer. As frequently noted, "the antitrust laws were passed for the protection of *competition,* not *competitors.*" *Id.* (citing *Brown Shoe Co. v. United States,* 370 U.S. 294, 320 (1962)).

Speaking to the first prerequisite to recovery, the Supreme Court stated that "[p]redatory pricing means pricing below some appropriate measure of cost." *Matsushita,* 475 U.S. at 584 n. 8 (quotation omitted). Despite a great deal of debate on the subject, no consensus has emerged as to what the most "appropriate" measure of cost is in predatory pricing cases. Costs can generally be divided into those that are "fixed" and do not vary with the level of output (management expenses, interest on bonded debt, property taxes, depreciation, and other irreducible overhead) and those that are "variable" and do vary with the level of output (materials, fuel, labor used to produce the product). Marginal cost, the cost that results from producing an additional increment of output, is primarily a function of variable cost because fixed costs, as the name would imply, are largely unaffected by changes in output. *See Rebel Oil Co., Inc. v. Atl. Richfield Co.,* 146 F.3d 1088, 1092 (9th Cir. 1998). For predatory pricing cases, especially those involving allegedly predatory production increases, the ideal measure of cost would be marginal cost because "[a]s long as a firm's prices exceed its marginal cost, each additional sale decreases losses or increases profits." *Advo, Inc. v. Phila. Newspapers, Inc.*, 51 F.3d 1191, 1198 (3d Cir. 1995). However, marginal cost, an economic abstraction, is notoriously difficult to measure and "cannot be determined from conventional accounting methods." *Northeastern Tel. Co. v. AT&T,* 651 F.2d 76, 88 (2d Cir. 1981). Economists, therefore, must resort to proxies for marginal cost. A commonly accepted proxy for marginal cost in predatory pricing cases is Average Variable Cost ("AVC"), the average of those costs that vary with the level of output.

The Supreme Court has declined to state which of the various cost measures is definitive. In *Brooke Group,* the Court accepted for the purposes of the case the parties' agreement that the appropriate measure of cost was AVC, but declined to "resolve the conflict among the lower courts over the appropriate measure of cost." 509 U.S. at 223 n. 1. *** Because there may be times when courts need the flexibility to examine both AVC as well as other proxies for marginal cost in order to evaluate an alleged predatory pricing scheme, we again decline to dictate a definitive cost measure for all cases. Sole reliance on AVC as the appropriate measure of cost may obscure the nature of a particular predatory scheme and, thus, contrary to what is suggested by the district court, we do not favor AVC to the exclusion of other proxies for marginal cost. Whatever the proxy used to measure marginal cost, it must be accurate and reliable in the specific circumstances of the case at bar.

Conceding that AVC is a good proxy for marginal cost in most cases, the government nevertheless argues that there may be times when looking only to a market-wide AVC test will disguise the nature of the predatory conduct at issue. Where there is a challenge to well-defined incremental conduct, and where incremental costs may be directly and confidently measured utilizing alternative proxies to AVC, argues the government, the market-wide AVC test is inappropriate.

Considering this to be the situation in the instant case, the government proffers four tests that purport to measure reliably incremental costs—the precise costs associated with the capacity additions at issue. Rather than creating independent measures of the costs associated with American's capacity additions, the government's experts rely on cost measures used in AAIMSPAN, American's internal decisional-accounting system (accounting measures that are used for internal decision making, not financial reporting). The government notes that a range of tests are necessary to rule out false positives and assure confidence in the results. Thus, the tests operate as cross-checks to each other to avoid misleading indications of predation. Due to similarities among the four tests, the district court grouped them as Tests Two and Three, and Tests One and Four for purposes of analysis. We proceed to consider each test to determine whether it is valid as a matter of law.

Two of the tests grouped together by the district court, Tests Two and Three, purport to measure incremental cost by looking to whether certain of American's internal cost-accounting measures became negative following the allegedly predatory capacity additions. Both tests rely on an internal accounting measure known as FAUDNC, or "Fully Allocated earnings plus Upline/Downline contribution Net of Costs." *United States v. AMR Corp.,* 140 F.Supp.2d 1141, 1175 (D. Kan. 2001). As the name would imply, FAUDNC is a fully allocated earnings measure, meaning that general operating expenses are arbitrarily allocated by American's decision accounting system to the flight or route level, and do not necessarily represent the exact costs associated with a particular flight or route. FAUDNC reflects 97-99% of American's total costs, which include fixed costs not affected by the capacity additions at issue. Thus, while FAUDNC includes some costs directly caused by a particular flight or operations on a particular route (such as fuel and landing fees), it also includes many costs that are not related to the operation of a particular flight or route (dispatch, city ticket offices, certain station expenses, certain maintenance expenses, American's flight academy, flight simulator maintenance, general sales and advertising). In other words, FAUDNC includes costs that are not entirely avoidable even if American were to abandon an entire route.

Because Tests Two and Three rely on fully allocated costs and include many fixed costs, the district court held that utilizing these cost measures would be the equivalent of applying an average total cost test, implicitly ruled out by *Brooke Group*'s mention of incremental costs only. The district court therefore concluded that, by relying on FAUDNC, Tests Two and Three were, by definition, not measures of marginal or incremental cost. We agree with this conclusion. While we will accept alternative proxies to marginal cost beyond AVC, Tests Two and Three are simply not proxies for marginal or incremental cost. Moreover, because these tests rely on "arbitrary allocation of costs among different classes of service," they "cannot purport to identify those costs which are *caused* by a product or service, and this is fundamental to economic cost determination." *MCI Communications Corp. v. AT&T,* 708 F.2d 1081, 1116 (7th Cir. 1982). Thus, given that Tests Two and Three rely on cost measures that are not, in large part, variable or avoidable with respect to capacity increases, we conclude that they are invalid as a matter of law as a measure of allegedly predatory capacity increases.[10]

[10] In holding that Tests Two and Three are invalid as a matter of law, we consider the uncontested fact that these tests, by relying on FAUDNC, measure a significant amount of American's fixed costs. As such, Tests Two and Three are inappropriate measures of incremental costs under *Brooke Group,* as they cannot demonstrate that American priced below an "appropriate measure of cost" with respect to the challenged capacity additions.

As to Tests One and Four, the district court grouped them together, labeling them as short-run profit-maximization tests. Test One examines changes in profitability. It employs FAUDNC, discussed above, and an internal measure of American's variable costs know as VAUDNC,[11] as well as a version of VAUDNC that has been modified by the government, VAUDNC-AC.[12] If these measures declined following a capacity addition, this test allegedly demonstrates that adding capacity forced American to forgo better profit performance elsewhere. Test Four relies on VAUDNC-AC to compare the supposed revenue from incremental passengers with the average avoidable cost of adding capacity. Under Test Four, if incremental revenues are below incremental costs, this is "evidence of sacrifice." *AMR Corp.,* 140 F.Supp.2d at 1180.

In rejecting tests One and Four, the district court concluded that they were, in essence, short-run profit-maximization tests that focus on whether a company has sacrificed some level of profit to compete more effectively. Courts and scholars have observed that such a sacrifice test would necessarily involve a great deal of speculation and often result in injury to the consumer and a chilling of competition. Upon closer examination, it is clear that rather than determining whether the added capacity itself was priced below an appropriate measure of cost, Test One effectively treats forgone or "sacrificed" profits as costs, and condemns activity that may have been profitable as predatory.[13] Rather than isolating the costs actually associated with the capacity additions the government purports to measure directly, Test One simply performs a "before-and-after" comparison of the route as a whole, looking to whether profits on the route as a whole decline after capacity was added, not to whether the challenged capacity additions were done below cost. In the end, Test One indicates only that a company has failed to maximize short-run profits on the route as a whole. Such a pricing standard could lead to a strangling of competition, as it would condemn nearly all output expansions, and harm to consumers. We conclude that Test One is invalid as a matter of law. Test Four does not appear to suffer from this flaw, and we do not reject it for being a short-run profit-maximization test.

As with Test One, the district court noted that, in proffering Test Four, the government has not "identif[ied] the actual costs associated with the capacity additions." *AMR Corp.,* 140

[11] VAUDNC refers to "Variable earnings plus Upline/Downline contribution Net of Costs." *AMR Corp.,* 140 F.Supp.2d at 1174. It is a measure of variable costs, calculated over an 18 month planning horizon, and represents 72% of the total costs in American's decision accounting system.

[12] Unlike the other costs measures, which are taken straight out of American's internal accounting system, VAUDNC-AC is a government creation. It represents VAUDNC costs plus the cost of aircraft ownership, which is traditionally considered a fixed cost in the airline industry, not an avoidable cost of changes in capacity on a route. By treating aircraft ownership as a variable expense, this measure reduces the apparent performance of the routes by increasing the costs attributed to operations on a particular flight or route. VAUDNC-AC represents over 79% of the total costs in American's decision accounting system. The district court concluded that VAUDNC-AC overstates short-run cost because it includes fixed, unavoidable aircraft-ownership costs.

[13] For example, if an airline earned $20.6 million on a route that cost $18 million to operate, it would have $2.6 million in profit. If the airline then added a flight to the route that would cost $500,000 to operate, but brought in an additional $1 million in revenue from passengers, the airline would make $500,000 profit. If adding this extra capacity to the route reduced the profitability of other flights on that route, reducing revenue for the rest of the route by $600,000 down to $20 million, under Test One, this conduct would be considered predatory because rather than comparing the additional flight's $1 million in revenue to its $500,000 in costs, Test One looks only to the reduction in profits on the route as a whole from $2.6 million to $2.5 million. Thus, this conduct would be labeled predatory because the profits for the route as a whole declined, even though the capacity additions themselves were profitable and the route as a whole was still profitable. *See* Einer Elhauge, *Why Above-Cost Price Cuts To Drive Out Entrants Are Not Predatory—and the Implications for Defining Costs and Market Power,* 112 Yale L.J. 681, 694 (2003). It is clear, therefore, that, in proffering Test One, the government has not "attempted to identify the actual costs associated with the capacity additions." *AMR Corp.,* 140 F.Supp.2d at 1202.

F.Supp.2d at 1202. We agree with this conclusion as well. Test Four attempts to reveal American's predatory conduct by measuring and comparing the incremental costs incurred by American when it added capacity to the city-pair routes in question to the incremental revenue it received from the additional capacity. The government's expert who developed Test Four, Steven Berry, characterized it as a comparison of the "average revenue from incremental passengers who traveled after the capacity addition with the average avoidable cost of the capacity addition." *See also* William J. Baumol, *Predation and the Logic of the Average Variable Cost Test,* 39 J.L. & Econ. 49, 58 (1996) (opining that average avoidable cost is the proper cost measure for predatory pricing tests). Berry further stated that, when considering an increase in capacity, an avoidable cost test compares, "the *incremental revenue generated by the increment* of capacity to the *avoidable cost of the increment* of capacity." Therefore, the only appropriate costs included in Test Four are those costs that American could have avoided by not adding the challenged capacity to the city-pair routes.

Test Four utilizes VAUDNC-AC, the cost component of which includes both aircraft ownership costs and costs characterized as variable over an eighteen-month planning period by AAIMSPAN. The costs included in VAUDNC-AC include variable costs American incurs with respect to all of its operations at DFW. Because some of those variable costs do not vary proportionately with the level of flight activity, they are allocated arbitrarily to a flight or route by AAIMSPAN. American identifies these variable, non-proportional common costs as: (1) airport ticket agents, (2) arrival agents, (3) ramp workers, and (4) security. Therefore, American argues that because VAUDNC-AC is an allocated variable cost measure, it cannot be used to calculate the *avoidable* cost of the added capacity.

The government first responds to American's criticism by arguing that cost allocation is a key component of managerial accounting and a relevant and sensible method by which to assign costs for decision-making purposes. While the government may be correct, this court is not presented with the question of whether cost allocation is a reasonable *accounting* method or a technique which provides businesses with reliable data to evaluate business decisions. Because the government asserts that Test Four measures average *avoidable* cost, this court must instead determine whether that assertion is correct. Thus, the government's first response is wholly irrelevant.

The government also alleges that there exists a genuine issue of material fact because its expert reworked Test Four so as to omit the contested costs and the results still indicated predation. The government's expert, however, states that when he reworked the numbers in response to criticism from American's expert, he eliminated the following costs from the test: (1) CTO ticketing, (2) direct reservations, (3) reservation communications, (4) cargo reservations, (5) and dispatch. Although the propriety of including these costs in Test Four was also disputed by American, they are not the costs that American disputed on the grounds that they are allocated arbitrarily to a route or flight by AAIMSPAN. Consequently, the expert's revisions to Test Four are not responsive to American's criticism and no genuine issue of material fact exists.

Because the cost component of Test Four includes arbitrarily allocated variable costs, it does not compare incremental revenue to average avoidable cost. Instead, it compares incremental revenue to a measure of both average variable cost and average avoidable cost. Therefore, Test Four does not measure only the avoidable or incremental cost of the capacity additions and cannot be used to satisfy the government's burden in this case.

We conclude that all four proxies are invalid as a matter of law, fatally flawed in their application, and fundamentally unreliable. Because it is uncontested that American did not price below

AVC for any route as a whole, we agree with the district court's conclusion that the government has not succeeded in establishing the first element of *Brooke Group,* pricing below an appropriate measure of cost.[15] Our conclusion that the government has not succeeded in establishing a genuine issue of material fact as to the first prong of *Brooke Group,* pricing below an appropriate measure of cost, renders an examination of whether the government has succeeded in creating a genuine issue of material fact as to the second prong of *Brooke Group,* dangerous probability of recoupment, unnecessary. Given the exceedingly thin line between vigorous price competition and predatory pricing, the balance the Supreme Court has struck in *Brooke Group,* and the fatally flawed nature of the alternative pricing proxies proffered by the government, we conclude that summary judgment in favor of American was appropriate.

V

The order of the district court granting summary judgment to American is **AFFIRMED.**

[15] The district court also stated that even if American had priced below an appropriate measure of cost, it was nevertheless entitled to summary judgment because "American's prices only matched, and never undercut, the fares of the new entrant, low cost carriers on the four core routes." *AMR Corp.,* 140 F.Supp.2d at 1204. In so concluding, the district court essentially imported the statutory "meeting competition" defense from the Robinson-Patman Act, 15 U.S.C. § 13(b). While we have never applied the "meeting competition" defense in a § 2 predatory pricing case, the district court reasoned that "there is strong inferential support for the idea that the defense may be appropriate in a given case." *Id.* at 1204. There may be strong arguments for application of the meeting competition defense in the Sherman Act context by analogy to the Robinson-Patman context. However, unlike in the Robinson-Patman Act, such a defense is not expressly provided for by the terms of the Sherman Act. The Supreme Court has never mentioned the possibility of such a defense under the Sherman Act. We therefore decline to rule that the "meeting competition" defense applies in the § 2 context.

Jefferson Parish Hospital District No. 2 v. Hyde

466 U.S. 2 (1984)

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 because every patient undergoing 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. 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. The Court of Appeals reversed because it was persuaded that the contract was illegal "*per se*." We granted certiorari, 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 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 term of this contract." App. 19.[4]

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 per cent to provide a reserve for uncollectible accounts, the fees are divided equally between Roux and the hospital.

The 1971 contract provided for a one-year term automatically renewable for successive one-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

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

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 per cent 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 Appeals concluded that the relevant geographic market was the East Bank of Jefferson Parish. 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.

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)." 686 F.2d, 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." 686 F.2d, 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 Pac. R. Co. v. United States*, 356 U.S. 1, 11 (1957), the tying arrangement was therefore illegal "*per se*."

II

Certain types of contractual arrangements are deemed unreasonable as a matter of law. 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

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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., at 537.

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." 513 F.Supp., at 541.

which the arrangement may be found. A price fixing agreement between competitors is the classic example of such an arrangement. 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*." The rule was first enunciated in *International Salt Co. v. United States*, 332 U.S. 392, 396 (1947), and has been endorsed by this Court many times since. The rule also reflects congressional policies underlying the antitrust laws. In enacting § 3 of the Clayton Act, 15 U.S.C. § 14, Congress expressed great concern about the anticompetitive character of tying arrangements. See H.R. Rep. No. 63-627, 63d Cong., 2d Sess., 10-13 (1914); Sen. Rep. No. 63-698, 63rd Cong., 2d Sess., 6-9 (1914). While this case does not arise under the Clayton Act, the congressional finding made therein concerning the competitive consequences of tying is illuminating, and must be respected.

It is clear, however, that every refusal to sell two products separately cannot 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, particularly if competing suppliers are free to sell either the entire package or its several parts. 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 if its competitors were ready and able to sell flour by itself." *Northern Pac. R. Co. v. United States*, 356 U.S. 1, 7 (1958). 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.

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.

*** Accordingly, we have condemned tying arrangements 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. See *United States Steel Corp. v. Fortner Enterprises* (*Fortner II*), 429 U.S. 610, 620 (1977). 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. This impairment could either harm existing competitors or create barriers to entry of new competitors in the market for the tied product, and can increase the social costs of market power by facilitating price discrimination, thereby increasing monopoly profits over what they would be absent the tie. 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. 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. Thus, application of the *per se* rule 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. 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. 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.

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, or when the seller offers a unique product that competitors are not able to offer, 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. *** When, however, the 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.

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

[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.

includes the services of the anesthesiologist.[28] Petitioners argue that the package does not involve a tying arrangement at all—that they are merely providing a functionally integrated package of services. 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. 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. In *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. These 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. 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. 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 to identify a distinct product market in which it is efficient to offer anesthesiological services separately from hospital services.

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. The District 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. The Court of Appeals agreed with this finding, and went on to observe that "an 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. The record amply supports the conclusion that consumers differentiate between anesthesiological services and the other hospital services provided by petitioners.

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. Nevertheless, the fact that this case involves a required purchase of two services that would otherwise be purchased separately does not make the Roux contract illegal. As noted above, there is

[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. The issue here is whether the hospital's insistence that its patients purchase anesthesiological services from Roux creates a tying arrangement.

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. The fact that petitioners' patients are required to purchase two separate items is only the beginning of the appropriate inquiry.

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 per cent 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. The fact that a substantial majority of the parish's residents elect not to enter East Jefferson means that the geographic data does 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" 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. 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 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 anesthesioligists 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. The record therefore does not provide a basis for applying the *per se* rule against tying to this arrangement.

[46] As an economic matter, market power exists whenever prices can be raised above the levels that would be charged in a competitive market.

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. 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 competition. The record sheds little light on how this arrangement affected consumer demand for separate arrangements with a specific anesthesiologist. 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.

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. 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 four to five doctors, but the most significant restraints on the patient's freedom to select a specific anesthesiologist will nevertheless remain. 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, 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 anesthesiologists. 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.

It is so ordered.

JUSTICE O'CONNOR, with whom CHIEF JUSTICE BURGER, JUSTICE POWELL, and JUSTICE REHNQUIST join, concurring in the judgment: *** 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 anti-competitive effect. See, *e.g.*, *Northern Pacific R. Co. v. United States*, 356 U.S. 1, 5 (1958). ***

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.*, *supra*, 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. 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 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. 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, or that abet the harmful exercise of market power that the seller possesses in the tying product market. Under the rule of reason tying arrangements should be disapproved only in such instances.

*** 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).

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. The antitrust law is properly concerned with 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.

In a regulated industry a firm with market power may be unable to extract a super-competitive 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.

Tying may also help the seller engage in price discrimination by "metering" the buyer's use of the tying product. 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. *** 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.

First, the seller must have power in the tying product market. Absent such power tying cannot conceivably have any adverse impact in the tied-product market, and can be only pro-competitive in the tying product market. If the seller of flour has no market power over flour, it will gain none by insisting that its buyers take some sugar as well.

*** 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. 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.

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. 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. 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 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.

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.

*** 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. 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, 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 Court's findings on such fact-bound questions, 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.

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, 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 department 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, that has little anti-competitive effect and achieves substantial benefits in the provision of care to patients, is hardly one that the antitrust law should condemn. 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

*** 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. ***

LePage's Inc. v. 3M (Minnesota Mining and Manufacturing Co.)

324 F.3d 141 (3d Cir. 2003) (en banc)

SLOVITER, CIRCUIT JUDGE, with whom BECKER, CHIEF JUDGE, NYGAARD, MCKEE, AMBRO, FUENTES, and SMITH, CIRCUIT JUDGES, join: Minnesota Mining and Manufacturing Company ("3M") appeals from the District Court's order entered March 14, 2000, declining to overturn the jury's verdict for LePage's in its suit against 3M under Section 2 of the Sherman Act ("§ 2"). 3M raises various objections to the trial court's decision but essentially its position is a legal one: it contends that a plaintiff cannot succeed in a § 2 monopolization case unless it shows that the conceded monopolist sold its product below cost. Because we conclude that exclusionary conduct, such as the exclusive dealing and bundled rebates proven here, can sustain a verdict under § 2 against a monopolist and because we find no other reversible error, we will affirm.

I.

FACTUAL BACKGROUND

3M, which manufactures Scotch tape for home and office use, dominated the United States transparent tape market with a market share above 90% until the early 1990s. It has conceded that it has a monopoly in that market. LePage's, founded in 1876, has sold a variety of office products and, around 1980, decided to sell "second brand" and private label transparent tape, *i.e.,* tape sold under the retailer's name rather than under the name of the manufacturer. By 1992, LePage's sold 88% of private label tape sales in the United States, which represented but a small portion of the transparent tape market. Private label tape sold at a lower price to the retailer and the customer than branded tape.

Distribution patterns and consumer acceptance accounted for a shift of some tape sales from branded tape to private label tape. With the rapid growth of office superstores, such as Staples and Office Depot, and mass merchandisers, such as Wal-Mart and Kmart, distribution patterns for second brand and private label tape changed as many of the large retailers wanted to use their "brand names" to sell stationery products, including transparent tape. 3M also entered the private label business during the early 1990s and sold its own second brand under the name "Highland."

LePage's claims that, in response to the growth of this competitive market, 3M engaged in a series of related, anticompetitive acts aimed at restricting the availability of lower-priced transparent tape to consumers. It also claims that 3M devised programs that prevented LePage's and the other domestic company in the business, Tesa Tuck, Inc., from gaining or maintaining large volume sales and that 3M maintained its monopoly by stifling growth of private label tape and by coordinating efforts aimed at large distributors to keep retail prices for Scotch tape high. LePage's claims that it barely was surviving at the time of trial and that it suffered large operating losses from 1996 through 1999.

LePage's brought this antitrust action asserting that 3M used its monopoly over its Scotch tape brand to gain a competitive advantage in the private label tape portion of the transparent tape market in the United States through the use of 3M's multi-tiered "bundled rebate" structure, which offered higher rebates when customers purchased products in a number of 3M's different product lines. LePage's also alleges that 3M offered to some of LePage's customers large lump-sum cash payments, promotional allowances and other cash incentives to encourage them to enter into exclusive dealing arrangements with 3M.

LePage's asserted claims for unlawful agreements in restraint of trade under § 1 of the Sherman Act, monopolization and attempted monopolization under § 2 of the Sherman Act, and exclusive dealing under § 3 of the Clayton Act. After a nine week trial, the jury returned its verdict for LePage's on both its monopolization and attempted monopolization claims under § 2 of the Sherman Act, and assessed damages of $22,828,899 on each. It found in 3M's favor on LePage's claims under § 1 of the Sherman Act and § 3 of the Clayton Act. 3M filed its motions for judgment as a matter of law and for a new trial, arguing that its rebate and discount programs and the other conduct of which LePage's complained did not constitute the basis for a valid antitrust claim as a matter of law and that, in any event, the court's charge to the jury was insufficiently specific and LePage's damages proof was speculative. The District Court granted 3M's motion for judgment as a matter of law on LePage's "attempted maintenance of monopoly power" claim but denied 3M's motion for judgment as a matter of law in all other respects and denied its motion for new trial. The Court subsequently entered a judgment for trebled damages of $68,486,697 to which interest was to be added. LePage's filed a cross appeal on the District Court's judgment dismissing its attempted maintenance of monopoly power claim.

On appeal, the panel of this court before which this case was originally argued reversed the District Court's judgment on LePage's § 2 claim by a divided vote. This court granted LePage's motion for rehearing *en banc* and, pursuant to its practice, vacated the panel opinion. The appeal was then orally argued before the court *en banc.*

III.

MONOPOLIZATION — APPLICABLE LEGAL PRINCIPLES

Section 2 of the Sherman Act provides:

> 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 (2002). A private party may sue for damages for violation of this provision and recover threefold the damages and counsel fees. *Id.* § 15.

Because this section is in sweeping language, suggesting the breadth of its coverage, we look to the Supreme Court decisions for elucidation of the standard to be used in cases alleging monopolization. Elucidation came in *United States v. Grinnell Corp.,* 384 U.S. 563 (1966), where the Court declared that a defendant company which possesses monopoly power in the relevant market will be found in violation of § 2 of the Sherman Act if the defendant willfully acquired or maintained that power. *Id.* at 570-71.

In this case, the parties agreed that the relevant product market is transparent tape and the relevant geographic market is the United States. Moreover, as to the issue of monopoly power, as we noted above, 3M concedes it possesses monopoly power in the United States transparent tape market, with a 90% market share. In fact, the evidence showed that the household penetration of 3M's Scotch-brand tape is virtually 100%. Therefore we need not dwell on the oft-contested issue of market power.

The sole remaining issue and our focus on this appeal is whether 3M took steps to maintain that power in a manner that violated § 2 of the Sherman Act. A monopolist willfully acquires or maintains monopoly power when it competes on some basis other than the merits. *See Aspen Skiing Co. v. Aspen Highlands Skiing Corp.,* 472 U.S. 585, 605 n. 32 (1985).

LePage's argues that 3M willfully maintained its monopoly in the transparent tape market through exclusionary conduct, primarily by bundling its rebates and entering into contracts that expressly or effectively required dealing virtually exclusively with 3M, which LePage's characterizes as *de facto* exclusive. 3M does not argue that it did not engage in this conduct. It agrees that it offered bundled rebates and entered into some exclusive dealing contracts, although it argues that only the few contracts that are expressly exclusive may be considered as such. Instead, 3M argues that its conduct was legal as a matter of law because it never priced its transparent tape below its cost.

This is the most significant legal issue in this case because it underlies 3M's argument. In its brief, 3M states "[a]bove-cost pricing cannot give rise to an antitrust offense as a matter of law, since it is the very conduct that the antitrust laws wish to promote in the interest of making consumers better off." For this proposition it relies on the Supreme Court's decision in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.,* 509 U.S. 209, 222 (1993). It is an argument 3M repeated frequently during its oral argument before the *en banc* court. Counsel stated, "if the big guy is selling above cost, it has done nothing which offends the Sherman Act...." This was the theory upon which 3M's counsel responded to all the questions from the court. When asked whether its theory is that because no one contended that 3M sold below its cost, that is "the end of the story," its counsel responded, "[w]ith the exception of the inconsequential express contract, absolutely."

It is therefore necessary for us, at the outset, to examine whether we must accept 3M's legal theory that after *Brooke Group,* no conduct by a monopolist who sells its product above cost — no matter how exclusionary the conduct — can constitute monopolization in violation of § 2 of the Sherman Act. *** [N]othing that the Supreme Court has written since *Brooke Group* dilutes the Court's consistent holdings that a monopolist will be found to violate § 2 of the Sherman Act if it engages in exclusionary or predatory conduct without a valid business justification.

IV.

MONOPOLIZATION — EXCLUSIONARY CONDUCT

*** B.

Bundled Rebates

In considering LePage's conduct that led to the jury's ultimate verdict, we note that the jury had before it evidence of the full panoply of 3M's exclusionary conduct, including both the exclusive dealing arrangements and the bundled rebates which could reasonably have been viewed as effectuating exclusive dealing arrangements because of the way in which they were structured.

Through a program denominated Executive Growth Fund ("EGF") and thereafter Partnership Growth Fund ("PGF"), 3M offered many of LePage's major customers substantial rebates to induce them to eliminate or reduce their purchases of tape from LePage's. Rather than competing by offering volume discounts which are concededly legal and often reflect cost savings, 3M's rebate programs offered discounts to certain customers conditioned on purchases spanning six of 3M's diverse product lines. The product lines covered by the rebate program were:

Health Care Products, Home Care Products, Home Improvement Products, Stationery Products (including transparent tape), Retail Auto Products, and Leisure Time. In addition to bundling the rebates, both of 3M's rebate programs set customer-specific target growth rates in each product line. The size of the rebate was linked to the number of product lines in which targets were met, and the number of targets met by the buyer determined the rebate it would receive on all of its purchases. If a customer failed to meet the target for any one product, its failure would cause it to lose the rebate across the line. This created a substantial incentive for each customer to meet the targets across all product lines to maximize its rebates.

The rebates were considerable, not "modest" as 3M states. For example, Kmart, which had constituted 10% of LePage's business, received $926,287 in 1997, and in 1996 Wal-Mart received more than $1.5 million, Sam's Club received $666,620, and Target received $482,001. Just as significant as the amounts received is the powerful incentive they provided to customers to purchase 3M tape rather than LePage's in order not to forego the maximum rebate 3M offered. The penalty would have been $264,000 for Sam's Club, $450,000 for Kmart, and $200,000 to $310,000 for American Stores.

3M does not deny that it offered these programs although it gives different reasons for the discounts to each customer. Instead it argues that they were no more exclusive than procompetitive lawful discount programs. And, as it responds to each of LePage's allegations, it returns to its central premise "that it is not unlawful to lower one's prices so long as they remain above cost." Appellant's Br. at 36 (citing *Brooke Group,* 509 U.S. at 222).

However, one of the leading treatises discussing the inherent anticompetitive effect of bundled rebates, even if they are priced above cost, notes that "the great majority of bundled rebate programs yield aggregate prices above cost. Rather than analogizing them to predatory pricing, they are best compared with tying, whose foreclosure effects are similar. Indeed, the 'package discount' is often a close analogy." Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law ¶ 794, at 83 (Supp. 2002).

The treatise then discusses the anticompetitive effect as follows:

> The anticompetitive feature of package discounting is the strong incentive it gives buyers to take increasing amounts or even all of a product in order to take advantage of a discount aggregated across multiple products. In the anticompetitive case, which we presume is in the minority, the defendant rewards the customer for buying its product *B* rather than the plaintiff's *B,* not because defendant's *B* is better or even cheaper. Rather, the customer buys the defendant's *B* in order to receive a greater discount on *A,* which the plaintiff does not produce. In that case the rival can compete in *B* only by giving the customer a price that compensates it for the foregone *A* discount.

Id.

The authors then conclude:

> Depending on the number of products that are aggregated and the customer's relative purchases of each, even an equally efficient rival may find it impossible to compensate for lost discounts on products that it does not produce.

Id. at 83-84.

The 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. We recognized this in our decision in *SmithKline Corp. v. Eli Lilly & Co.,* 575 F.2d

1056 (3d Cir. 1978), where we held that conduct substantially identical to 3M's was anticompetitive and sustained the finding of a violation of § 2. ***

LePage's private-label and second-tier tapes are *** less expensive but otherwise of similar quality to Scotch-brand tape. Indeed, before 3M instituted its rebate program, LePage's had begun to enjoy a small but rapidly expanding toehold in the transparent tape market. 3M's incentive was thus the same as Lilly's in *SmithKline:* to preserve the market position of Scotch-brand tape by discouraging widespread acceptance of the cheaper, but substantially similar, tape produced by LePage's.

3M bundled its rebates for Scotch-brand tape with other products it sold in much the same way that Lilly bundled its rebates ***. In both cases, the bundled rebates reflected an exploitation of the seller's monopoly power. Just as "[cephalosporins] [were] carried in ... virtually every general hospital in the country," *SmithKline,* 575 F.2d at 1062, the evidence in this case shows that Scotch-brand tape is indispensable to any retailer in the transparent tape market. ***

The effect of 3M's rebates were even more powerfully magnified than those in *SmithKline* because 3M's rebates required purchases bridging 3M's extensive product lines. In some cases, these magnified rebates to a particular customer were as much as half of LePage's entire prior tape sales to that customer. For example, LePage's sales to Sam's Club in 1993 totaled $1,078,484, while 3M's 1996 rebate to Sam's Club was $666,620. Similarly, LePage's 1992 sales to Kmart were $2,482,756; 3M's 1997 rebate to Kmart was $926,287. The jury could reasonably find that 3M used its monopoly in transparent tape, backed by its considerable catalog of products, to squeeze out LePage's. 3M's conduct was at least as anticompetitive as the conduct which this court held violated § 2 in *SmithKline.*

C.

Exclusive Dealing

The second prong of LePage's claim of exclusionary conduct by 3M was its actions in entering into exclusive dealing contracts with large customers. 3M acknowledges only the expressly exclusive dealing contracts with Venture and Pamida which conditioned discounts on exclusivity. It minimizes these because they represent only a small portion of the market. However, LePage's claims that 3M made payments to many of the larger customers that were designed to achieve sole-source supplier status.

3M argues that because the jury found for it on LePage's claims under § 1 of the Sherman Act and § 3 of the Clayton Act, these payments should not be relevant to the § 2 analysis. The law is to the contrary. Even though exclusivity arrangements are often analyzed under § 1, such exclusionary conduct may also be an element in a § 2 claim.

3M also disclaims as exclusive dealing any arrangement that contained no express exclusivity requirement. Once again the law is to the contrary. No less an authority than the United States Supreme Court has so stated. In *Tampa Elec. Co. v. Nashville Coal Co.,* 365 U.S. 320, 327 (1961), a case that dealt with § 3 of the Clayton Act rather than § 2 of the Sherman Act, the Court took cognizance of arrangements which, albeit not expressly exclusive, effectively foreclosed the business of competitors.

LePage's introduced powerful evidence that could have led the jury to believe that rebates and discounts to Kmart, Staples, Sam's Club, National Office Buyers and "UDI" were designed to induce them to award business to 3M to the exclusion of LePage's. Many of LePage's former customers refused even to meet with LePage's sales representatives. A buyer for Kmart, LePage's largest customer which accounted for 10% of its business, told LePage's: "I can't talk to you about tape products for the next three years" and "don't bring me anything 3M makes." Kmart switched to 3M following 3M's offer of a $1 million "growth" reward which the jury could have understood to require that 3M be its sole supplier. Similarly, Staples was offered an extra 1% bonus rebate if it gave LePage's business to 3M. 3M argues that LePage's did not try hard enough to retain Kmart, its customer for 20 years, but there was evidence to the contrary. In any event, the purpose and effect of 3M's payments to the retailers were issues for the jury which, by its verdict, rejected 3M's arguments.

The foreclosure of markets through exclusive dealing contracts is of concern under the antitrust laws. As one of the leading treatises states:

> unilaterally imposed quantity discounts can foreclose the opportunities of rivals when a dealer can obtain its best discount only by dealing exclusively with the dominant firm. For example, discounts might be cumulated over lengthy periods of time, such as a calendar year, when no obvious economies result.

3A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 768b2, at 148 (2d Ed. 2002); *see also* 11 Herbert Hovenkamp, *Antitrust Law* ¶ 1807a, at 115-16 (1998) (quantity discounts may foreclose a substantial portion of the market). Discounts conditioned on exclusivity are "problematic" "when the defendant is a dominant firm in a position to force manufacturers to make an all-or-nothing choice." *Id.* at 117 n. 7 (citing *LePage's,* 1997 WL 734005 (E.D. Pa. 1997)).

*** LePage's produced evidence that the foreclosure caused by exclusive dealing practices was magnified by 3M's discount practices, as some of 3M's rebates were "all-or-nothing" discounts, leading customers to maximize their discounts by dealing exclusively with the dominant market player, 3M, to avoid being severely penalized financially for failing to meet their quota in a single product line. Only by dealing exclusively with 3M in as many product lines as possible could customers enjoy the substantial discounts. Accordingly, the jury could reasonably find that 3M's exclusionary conduct violated § 2.

V.

ANTICOMPETITIVE EFFECT

It has been LePage's position in pursuing its § 2 claim that 3M's exclusionary "tactics foreclosed the competitive process by preventing rivals from competing to gain (or maintain) a presence in the market." When a monopolist's actions are designed to prevent one or more new or potential competitors from gaining a foothold in the market by exclusionary, *i.e.* predatory, conduct, its success in that goal is not only injurious to the potential competitor but also to competition in general. It has been recognized, albeit in a somewhat different context, that even the foreclosure of "one significant competitor" from the market may lead to higher prices and reduced output. *Roland Mach. Co. v. Dresser Indus., Inc.,* 749 F.2d 380, 394 (7th Cir. 1984).

*** [I]n this case, the jury could have reasonably found that 3M's exclusionary conduct cut LePage's off from key retail pipelines necessary to permit it to compete profitably.[14] It was only after LePage's entry into the market that 3M introduced the bundled rebates programs. If 3M

[14] In the transparent tape market, superstores like Kmart and Wal-Mart provide a crucial facility to any manufacturer—they supply high volume sales with the concomitant substantially reduced distribution costs. By wielding its monopoly power in transparent tape and its vast array of product lines, 3M foreclosed LePage's from that critical bridge to consumers that superstores provide, namely, cheap, high volume supply lines.

were successful in eliminating competition from LePage's second-tier or private-label tape, 3M could exercise its monopoly power unchallenged, as Tesa Tuck was no longer in the market.

The District Court, recognizing that "this case presents a unique bundled rebate program that the jury found had an anti-competitive effect," *LePage's,* 2000 WL 280350, at *5, denied 3M's motion for judgment as a matter of law ("JMOL"), stating:

> Plaintiff introduced evidence that Scotch is a monopoly product, and that 3M's bundled rebate programs caused distributors to displace LePage's entirely, or in some cases, drastically reduce purchases from LePage's. Under 3M's rebate programs, 3M set overall growth targets for unrelated product lines. *In the distributors' view, 3M set these targets in a manner which forced the distributor to either drop any non-Scotch products, or lose the maximum rebate.* Thus, in order to qualify for the maximum rebate under the EGF/PGF programs, the record shows that most customers diverted private label business to 3M at 3M's suggestion. Similarly, under the newer Brand Mix rebate program, 3M set higher rebates for tape sales which produced a shift from private label tape to branded tape.
>
> *Furthermore, Plaintiff introduced evidence of customized rebate programs that similarly caused distributors to forego purchasing from LePage's if they wished to obtain rebates on 3M's products.* Specifically, the trial record establishes that 3M offered Kmart a customized growth rebate and Market Development Funds payment. In order to reach the $15 million sales target and qualify for the $1 million rebate, however, Kmart had to increase its consumer stationary purchases by $5.5 million. Kmart substantially achieved this "growth" by dropping LePage's and another private label manufacturer, Tesa. Likewise, 3M customized a program with Staples that provided for an extra 1% bonus rebate on Scotch tape sales "if LePage's business is given to 3M." Finally, 3M provided a similar discount on Scotch tape to Venture Stores "based on the contingency of Venture dropping private label." Thus, the jury could have reasonably concluded that 3M's customers were forced to forego purchasing LePage's private label tape in order to obtain the rebates on Scotch tape.

Id. (emphasis added).

In the same opinion, the District Court found that "[LePage's] introduced substantial evidence that the anticompetitive effects of 3M's rebate programs caused LePage's losses." The jury was capable of calculating from the evidence the amount of rebate a customer of 3M would lose if it failed to meet 3M's quota of sales in even one of the bundled products. The discount that LePage's would have had to provide to match the discounts offered by 3M through its bundled rebates can be measured by the discounts 3M gave or offered. For example, LePage's points out that in 1993 Sam's Club would have stood to lose $264,900 and Kmart $450,000 for failure to meet one of 3M's growth targets in a single product line. Moreover, the effect of 3M's rebates on LePage's earnings, if LePage's had attempted to match 3M's discounts, can be calculated by comparing the discount that LePage's would have been required to provide. That amount would represent the impact of 3M's bundled rebates on LePage's ability to compete, and that is what is relevant under § 2 of the Sherman Act.

The impact of 3M's discounts was apparent from the chart introduced by LePage's showing that LePage's earnings as a percentage of sales plummeted to below zero—to negative 10%—during 3M's rebate program. Demand for LePage's tape, especially its private-label tape, decreased significantly following the introduction of 3M's rebates. Although 3M claims that customers participating in its rebate programs continued to purchase tape from LePage's, the evidence does not support this contention. Many distributors dropped LePage's entirely.

Prior to the introduction of 3M's rebate program, LePage's sales had been skyrocketing. Its sales to Staples increased by 440% from 1990 to 1993. Following the introduction of 3M's rebate program which bundled its private-label tape with its other products, 3M's private-label tape sales increased 478% from 1992 to 1997.[15] LePage's in turn lost a proportional amount of sales. It lost key large volume customers, such as Kmart, Staples, American Drugstores, Office Max, and Sam's Club. Other large customers, like Wal-Mart, drastically cut back their purchases.

As a result, LePage's manufacturing process became less efficient and its profit margins declined. In transparent tape manufacturing, large volume customers are essential to achieving efficiencies of scale. As 3M concedes, "'large customers were extremely important to [LePage's], to everyone.' ... Large volumes ... permitted 'long runs,' making the manufacturing process more economical and predictable." Appellant Br. at 10 (quoting trial testimony of Les Baggett, LePage's former president and CEO) (citation omitted).

There was a comparable effect on LePage's share of the transparent tape market. In the agreed upon relevant market for transparent tape in the United States, LePage's market share dropped 35% from 1992 to 1997. In 1992, LePage's net sales constituted 14.44% of the total transparent tape market. By 1997, LePage's sales had fallen to 9.35%. Finally, in March of 1997, LePage's was forced to close one of its two plants. That same year, the only other domestic transparent tape manufacturer, Tesa Tuck, Inc., bowed out of the transparent tape business entirely in the United States. Had 3M continued with its program it could have eventually forced LePage's out of the market.

The relevant inquiry is the anticompetitive effect of 3M's exclusionary practices considered together. As the Supreme Court recognized in *Cont'l Ore Co. v. Union Carbide & Carbon Corp.*, 370 U.S. 690, 699 (1962), the courts must look to the monopolist's conduct taken as a whole rather than considering each aspect in isolation. ***

The effect of 3M's conduct in strengthening its monopoly position by destroying competition by LePage's in second-tier tape is most apparent when 3M's various activities are considered as a whole. The anticompetitive effect of 3M's exclusive dealing arrangements, whether explicit or inferred, cannot be separated from the effect of its bundled rebates. 3M's bundling of its products via its rebate programs reinforced the exclusionary effect of those programs.

3M's exclusionary conduct not only impeded LePage's ability to compete, but also it harmed competition itself, a *sine qua non* for a § 2 violation. LePage's presented powerful evidence that competition itself was harmed by 3M's actions. The District Court recognized this in its opinion, when it said:

> The jury could reasonably infer that 3M's planned elimination of the lower priced private label tape, as well as the lower priced Highland brand, would channel consumer selection to the higher priced Scotch brand and lead to higher profits for 3M. Indeed, Defendant concedes that "3M could later recoup the profits it has forsaken on Scotch tape and private label tape by selling more higher priced Scotch tape ... if there would be no competition by others in the private label tape segment when 3M abandoned that part of the market to sell only higher-priced Scotch tape."

LePage's, 2000 WL 280350, at *7.

3M could effectuate such a plan because there was no ease of entry.

[15] In 1992, 3M's private-label tape sales were $1,142,000. By 1997, its private-label tape sales had increased to $5,464,222.

The District Court found that there was "substantial evidence at trial that significant entry barriers prevent competitors from entering the ... tape market in the United States. Thus, this case presents a situation in which a monopolist remains unchecked in the market." *LePage's,* 2000 WL 280350, at *7. In the time period at issue here, there has never been a competitor that has genuinely challenged 3M's monopoly and it never lost a significant transparent tape account to a foreign competitor.

There was evidence from which the jury could have determined that 3M intended to force LePage's from the market, and then cease or severely curtail its own private-label and second-tier tape lines. For example, by 1996, 3M had begun to offer incentives to some customers to increase purchases of its higher priced Scotch-brand tapes over its own second-tier brand. The Supreme Court has made clear that intent is relevant to proving monopolization, *Aspen Skiing,* 472 U.S. at 602, and attempt to monopolize, *Lorain Journal,* 342 U.S. at 154-55.

3M's interest in raising prices is well-documented in the record. In internal memoranda introduced into evidence by LePage's, 3M executives boasted that the large retailers like Office Max and Staples had no choice but to adhere to 3M's demands. *See* Sealed App. at 2585 ("Either they take the [price] increase ... or we hold orders ...."); *see also* Sealed App. at 2571 (3M's directive when Staples objected to price increase was "orders will be held if pricing is not up to date on 1/1/98"). LePage's expert testified that the price of Scotch-brand tape increased since 1994, after 3M instituted its rebate program. In its opinion, the District Court cited the deposition testimony of a 3M employee acknowledging that the payment of the rebates after the end of the year discouraged passing the rebate on to the ultimate customers. The District Court thus observed, "the record amply reflects that 3M's rebate programs did not benefit the ultimate consumer." *Le Page's,* 2000 WL 280350, at *7.

As the foregoing review of the evidence makes clear, there was sufficient evidence for the jury to conclude the long-term effects of 3M's conduct were anticompetitive. We must therefore uphold its verdict on liability unless 3M has shown adequate business justification for its practices.

VI.

BUSINESS REASONS JUSTIFICATION

It remains to consider whether defendant's actions were carried out for "valid business reasons," the only recognized justification for monopolizing. *See, e.g., Eastman Kodak,* 504 U.S. at 483. However, a defendant's assertion that it acted in furtherance of its economic interests does not constitute the type of business justification that is an acceptable defense to § 2 monopolization. Paraphrasing one corporate executive's well publicized statement, whatever is good for 3M is not necessarily permissible under § 2 of the Sherman Act. As one court of appeals has explained:

> In general, a business justification is valid if it relates directly or indirectly to the enhancement of consumer welfare. Thus, pursuit of efficiency and quality control might be legitimate competitive reasons ..., while the desire to maintain a monopoly market share or thwart the entry of competitors would not.

Data Gen. Corp. v. Grumman Sys. Support Corp., 36 F.3d 1147, 1183 (1st Cir. 1994) (citing *Eastman Kodak,* 504 U.S. at 483; *Aspen Skiing,* 472 U.S. at 608-11).

It can be assumed that a monopolist seeks to further its economic interests and does so when it engages in exclusionary conduct. Thus, for example, exclusionary practice has been defined as "a method by which a firm ... trades a part of its monopoly profits, at least temporarily, for a larger market share, by making it unprofitable for other sellers to compete with it." Richard A. Posner, *Antitrust Law: An Economic Perspective* 28 (1976). Once a monopolist achieves its goal by excluding potential competitors, it can then increase the price of its product to the point at which it will maximize its profit. This price is invariably higher than the price determined in a competitive market. That is one of the principal reasons why monopolization violates the antitrust laws. The fact that 3M acted to benefit its own economic interests is hardly a reason to overturn the jury's finding that it violated § 2 of the Sherman Act.

The defendant bears the burden of "persuad[ing] the jury that its conduct was justified by any normal business purpose." *Aspen Skiing,* 472 U.S. at 608. Although 3M alludes to its customers' desire to have single invoices and single shipments in defense of its bundled rebates, 3M cites to no testimony or evidence in the 55 volume appendix that would support any actual economic efficiencies in having single invoices and/or single shipments. It is highly unlikely that 3M shipped transparent tape along with retail auto products or home improvement products to customers such as Staples or that, if it did, the savings stemming from the joint shipment approaches the millions of dollars 3M returned to customers in bundled rebates.

There is considerable evidence in the record that 3M entered the private-label market only to "kill it." *See, e.g.,* Sealed App. at 809 (statement by 3M executive in internal memorandum that "I don't want private label 3M products to be successful in the office supply business, its distribution or our consumers/end users"). That is precisely what § 2 of the Sherman Act prohibits by covering conduct that maintains a monopoly. Maintaining a monopoly is not the type of valid business reason that will excuse exclusionary conduct. 3M's business justification defense was presented to the jury, and it rejected the claim. The jury's verdict reflects its view that 3M's exclusionary conduct, which made it difficult for LePage's to compete on the merits, had no legitimate business justification. ***

X.

CONCLUSION

Section 2, the provision of the antitrust laws designed to curb the excesses of monopolists and near-monopolists, is the equivalent in our economic sphere of the guarantees of free and unhampered elections in the political sphere. Just as democracy can thrive only in a free political system unhindered by outside forces, so also can market capitalism survive only if those with market power are kept in check. That is the goal of the antitrust laws.

The jury heard the evidence and the contentions of the parties, accepting some and rejecting others. There was ample evidence that 3M used its market power over transparent tape, backed by its considerable catalog of products, to entrench its monopoly to the detriment of LePage's, its only serious competitor, in violation of § 2 of the Sherman Act. We find no reversible error. Accordingly, we will affirm the judgment of the District Court.

GREENBERG, CIRCUIT JUDGE, dissenting: *** As the majority indicates, 3M dominated the United States transparent tape market with a market share above 90% until the early 1990s. LePage's around 1980 decided to sell "second brand" and private label tape, *i.e.,* tape sold under the retailer's, rather than the manufacturer's name, an endeavor successful to the extent that LePage's captured 88% of private label tape sales in the United States by 1992. Moreover, growth of "second brand" and private label tape accounted for a shift of some tape sales from branded tape to private label tape so the size of the private label tape business expanded. In the circumstances, not surprisingly, during the early 1990s, 3M also entered the private label tape business.

As the majority notes, LePage's claims that, in response to the growth of this competitive market, 3M engaged in a series of related, anticompetitive acts aimed at restricting the availability of lower-priced transparent tape to consumers. In particular, it asserts that 3M devised programs that prevented LePage's and the other domestic company in the business, Tesa Tuck, Inc., from gaining or maintaining large volume sales and that 3M maintained its monopoly by stifling growth of private label tape and by coordinating efforts aimed at large distributors to keep retail prices for Scotch tape high. LePage's barely was surviving at the time of trial and suffered large operating losses from 1996 through 1999.

This case centers on 3M's rebate programs that, beginning in 1993, involved offers by 3M of "package" or "bundled" discounts for various items ranging from home care and leisure products to audio/visual and stationery products. Customers could earn rebates by purchasing, in addition to transparent tape, a variety of products sold by 3M's stationery division, such as Post-It Notes and packaging products. There is no doubt but that these programs created incentives for retailers to purchase more 3M products and enabled them to have single invoices, single shipments and uniform pricing programs for various 3M products. 3M linked the size of the rebates to the number of product lines in which the customers met the targets, an aggregate number that determined the rebate percentage the customer would receive on all of its 3M purchases across all product lines. Therefore, if customers failed to meet growth targets in multiple categories, they did not receive any rebate, and if they failed to meet the target in one product line, 3M reduced their rebates substantially. These requirements are at the crux of the controversy here, as LePage's claims that customers could not meet these growth targets without eliminating it as a supplier of transparent tape.

In practice, as 3M's rebate program evolved, it offered three different types of rebates: Executive Growth Fund, Partnership Growth Fund and Brand Mix Rebates. 3M developed a "test program" called Executive Growth Fund ("EGF") for a small number of retailers, 11 in 1993 and 15 in 1994. Under EGF, 3M negotiated volume and growth targets for each customer's purchases from the six 3M consumer product divisions involved in the EGF program. A customer meeting the target in three or more divisions earned a volume rebate of between 0.2-1.25% of total sales.

Beginning in 1995, 3M undertook to end the EGF test program and institute a rebate program called Partnership Growth Fund ("PGF") for the same six 3M consumer products divisions. Under this program, 3M established uniform growth targets applicable to all participants. Customers who increased their purchases from at least two divisions by $1.00 and increased their total purchases by at least 12% over the previous year qualified for the rebate, which ranged from 0.5% to 2%, depending on the number of divisions (between two to five divisions) in which the customer increased its purchases and the total volume of purchases.

In 1996 and 1997, 3M offered price incentives called Brand Mix Rebates to two tape customers, Office Depot and Staples, to increase purchases of Scotch brand tapes. 3M imposed a minimum purchase level for tape set at the level of Office Depot's and Staples's purchases the previous year with "growth" factored in. To obtain a higher rebate, these two customers could increase their percentage of Scotch purchases relative to certain lower-priced orders.

The evidence at trial focused on the parties' dealings with a limited number of customers and demonstrated that LePage's problems were attributed to a number of factors, not merely 3M's rebate programs. *** Notwithstanding the evidence which demonstrates that LePage's lost business for reasons that could not possibly be attributable to any unlawful conduct by 3M, it argues that 3M willfully maintained its monopoly through a "monopoly broth" of anticompetitive and predatory conduct. I would reject LePage's's argument as I agree with 3M that LePage's simply did not establish that 3M's conduct was illegal, as LePage's did not demonstrate that 3M's pricing was below cost (a point that is not in dispute) and, in the absence of such proof, the record does not supply any other basis on which we can uphold the judgment.

There are two elements of a monopolization claim under section 2 of the Sherman Act: "(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. 563, 570-71 (1966). Willful maintenance involves using anticompetitive conduct to "foreclose competition, to gain a competitive advantage, or to destroy a competitor." *Eastman Kodak Co. v. Image Technical Servs.,* 504 U.S. 451, 482-83 (1992) (internal quotation marks omitted). LePage's contends that 3M's bundled rebates were anticompetitive and predatory. It also argues that 3M's other practices, such as exclusionary contracts and the timing of its rebates, were also anticompetitive and predatory. I discuss these claims in the order I have stated them.

LePage's primarily complains of 3M's use of bundled rebates. While, as the majority recognizes, we have held that rebates on volume purchases are lawful, LePage's seeks to avoid that principle by pointing out that 3M offered higher rebates if customers met their target growth rate in different product categories, in effect linking the sale of private label tape with the sale of other products, such as Scotch tape, which customers had to buy from 3M. Thus, LePage's explains:

> 3M understood that, as a practical matter, every retailer in the country had to carry Scotch-brand tape.... It therefore decided to structure its rebates into bundles that linked that product with the product segment in which it did face competition from LePage's (second-line tape).... To increase the leverage on the targeted segment, 3M further linked rebates on transparent tape with those for many other products.... The rival would have to 'compensate' the customer for the amount of rebate it would lose not only on the large volume of Scotch-brand tape it had to buy, but also for rebates on many other products purchased from 3M.

Br. of Appellee at 40.

*** LePage's argues that it does not have to show that 3M's package discounts could prevent an equally efficient firm from matching or beating 3M's package discounts. In its brief, LePage's contends that its expert economist explained that 3M's programs and cash payments have the same anticompetitive impact regardless of the cost structure of the rival suppliers or their efficiency relative to that of 3M. LePage's alleges that the relative efficiency or cost structure of the competitor simply affects how long it would take 3M to foreclose the rival from obtaining the volume of business necessary to survive. "Competition is harmed just the same by the loss of the only existing competitive constraints on 3M in a market with high entry barriers." *Id.* The district court stated that LePage's introduced substantial evidence that the anticompetitive effects of 3M's rebate program caused its losses. *See LePage's Inc. v. 3M,* No. Civ. A. 97-3983, 2000 WL 280350, at *7-*8 (E.D. Pa. Mar. 14, 2000). *** 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, and thus its brief does not point to evidence along such lines.

While I recognize that it is obvious from the size of 3M's rebates as compared to LePage's's sales that LePage's would have had to make substantial reductions in prices to match the rebates 3M paid to particular customers, LePage's did not show the amount by which it lowered its prices in actual monetary figures or by percentage to compete with 3M and how its profitability thus was decreased. Rather, LePage's merely maintains, through the use of an expert, that it would have had to cut its prices drastically to compete and thus would have gone out of business. Furthermore, it is critically important to recognize that LePage's had 67% of the private label business at the time of the trial. Thus, notwithstanding 3M's rebates, LePage's was able to retain most of the private label business. In the circumstances, it is ironical that LePage's complains of 3M's use of monopoly power as the undisputed fact is that LePage's, not 3M, was the dominant supplier of private label tape both before and after 3M initiated its rebate programs. Indeed, the record suggests that inasmuch as LePage's could not make a profit with a 67% share of the private label sales, it must have needed to be essentially the exclusive supplier of such tape for its business to be profitable as it in fact was when it had an 88% share of the private label tape sales business.

*** Without *** pricing information, it is difficult even to begin to estimate how much of the market share LePage's lost was due to 3M's bundled rebates. In fact, the evidence that I described above conclusively demonstrates that LePage's lost private sale tape business for reasons not related to 3M's rebates. Furthermore, some experts have questioned the validity of attributing all the rebates to the one competitive product in situations such as these. *** LePage's does not even attempt to meet that less strict test by calculating how much it would have had to lower its prices to match the rebates, even if they all were aggregated and attributed to private label tape.

One aspect of this method of calculation worth noting is that the volume of the products ordered has a drastic effect on how much the competitor would have to lower its prices to compete. For example, suppose in a similar rebate program, a company was the only producer of products A and B but faced competition in C. If a customer orders 100 units each of A, B, and C at a price of $1.00 each, a 3% rebate would be $9.00 (3% of the total of $300.00). If the rebate on all three products were attributed to product C, then the competitor would have to lower its price to $0.91 in order to compete with it. The results would be starkly different, however, if a customer orders 100 units of A and B but only needs 10 units of C. Then the 3% rebate on the total purchase amount of $210.00 would be $6.30. If the rebate was attributed solely to product C, then a competitor would have to lower its price to $.37 on product C in order to match the company's price.

*** In this case, as the majority acknowledges, LePage's now does not contend that 3M priced its products below average variable cost, an allegation which, if made, in any event would be difficult to prove. Moreover, LePage's's economist conceded that LePage's is not as efficient a tape producer as 3M. Thus, in this case section 2 of the Sherman Act is being used to protect an inefficient producer from a competitor not using predatory pricing but rather selling above cost. While the majority contends that *Brooke Group,* a case on which 3M heavily relies, is distinguishable as none of the defendants there had a monopoly in the market, the fact remains that the Court in describing section 2 of the Sherman Act said flat out in *Brooke Group* that "a plaintiff seeking to establish competitive injury 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. LePage's simply did not do this.

I realize that the majority indicates that "LePage's unlike the plaintiff in *Brooke Group,* does not make a predatory pricing claim." But that circumstance weakens rather than strengthens LePage's's position as it merely confirms the lawfulness of 3M's conduct. Furthermore, the circumstance that 3M is not dealing in an oligopolistic market should not matter as the harm that LePage's claims to have suffered from the bundled rebates would be no less if inflicted by multiple competitors. Moreover, monopolist or not, 3M, even in the absence of LePage's and Tesa from the private label business, would not be the only supplier of private label tape for there are foreign suppliers as is demonstrated plainly by the evidence that both Walgreens and Dollar General dealt with such suppliers.

Contrary to the majority's view, this is not a situation in which there is no business justification for 3M's actions. This point is important inasmuch as it is difficult to distinguish legitimate competition from exclusionary conduct that harms competition, *see United States v. Microsoft Corp.,* 253 F.3d 34, 58 (D.C. Cir. 2001), and some cases suggest that when a company acts against its economic interests and there is no valid business justification for its actions, then it is a good sign that its acts were intended to eliminate competition.

*** Unlike the situation of the defendant in *Aspen,* 3M's pricing structure and bundled rebates were not contrary to its economic interests, as they likely increased its sales. In fact, that is exactly what LePage's is complaining about. Furthermore, other than the obvious reasons such as increasing bulk sales, market share and customer loyalty, there are several other potential "procompetitive" or valid business reasons for 3M's pricing structure and bundled rebates: efficiency in having single invoices, single shipments and uniform pricing programs for various products. Moreover, the record demonstrates that, with the biggest customers, 3M's rebates were not eliminating the competitive process, as LePage's still was able to retain some customers through negotiation, and even though it lost other customers, the losses were attributable to their switching to foreign suppliers or changing suppliers because of quality or service without regard to the rebates. Furthermore, overall LePage's was quite successful in holding its share of the private label sales as it had 67% of the business at the time of the trial.

In sum, I conclude that as a matter of law 3M did not violate section 2 of the Sherman Act by reason of its bundled rebates even though its practices harmed its competitors. The majority decision which upholds the contrary verdict risks curtailing price competition and a method of pricing beneficial to customers because the bundled rebates effectively lowered their costs. I regard this result as a significant mistake which cannot be justified by a fear that somehow 3M will raise prices unreasonably later. In this regard I reiterate that in addition to LePage's there are foreign suppliers of transparent tape so that with or without LePage's there will be constraints on 3M's pricing.

LePage's also claims that, through a variety of other allegedly anticompetitive actions, 3M prevented LePage's from competing. LePage's asserts that 3M foreclosed competition by directly purchasing sole-supplier status. There was some dispute as to whether the contracts were conditioned on 3M being the sole supplier, and 3M claims that there are only two customers for which there is any evidence of a sole supplier agreement. I recognize, however, that although most of 3M's contracts with customers were not conditioned on exclusivity, practically speaking some customers dropped LePage's as a supplier to maximize the rebates that 3M was offering. Moreover, *United Shoe Machinery Corp. v. United States,* 258 U.S. 451, 458 (1922), explained that a contract that does not contain specific agreements not to use the products of a competitor still will come within the Clayton Act as to exclusivity if its practical effect is to prevent such use.

Even assuming, however, that 3M did have exclusive contracts with some of the customers, LePage's has not demonstrated that 3M acted illegally, as one-year exclusive contracts have been held to be reasonable and not unduly restrictive. In *Tampa Electric Co. v. Nashville Coal Co.,* 365 U.S. 320, 327 (1961), the Court stated that even if in practical application a contract is found to be an exclusive-dealing arrangement, it does not violate section 3 of the Clayton Act unless the court believes it probable that performance of the contract will foreclose competition in a substantial share of the line of commerce affected. Using that standard, although LePage's's market share in private label tape has fallen from 88% to 67%, it has not been established that, as a result of the allegedly exclusive contracts, competition was foreclosed in a substantial share of the line of commerce affected. Indeed, in view of LePage's's two-thirds share of the private label business, its attack on exclusivity agreements is attenuated.

There appear to be very few cases supporting liability based on section 2 of the Sherman Act for exclusive dealing, as some cases suggest that if, as is the case here under the jury's findings, there is no liability under section 3 of the Clayton Act, it is more difficult to find liability under the Sherman Act since its scope is more restricted. In any event, the record shows only two allegedly exclusive contracts (with the Venture and Pamida stores), and "[b]ecause an exclusive deal affecting a small fraction of a market clearly cannot have the requisite harmful effect upon competition, the requirement of a significant degree of foreclosure serves a useful screening function." *Microsoft,* 253 F.3d at 69. The *Microsoft* court explained that although exclusive contracts are commonplace, particularly in the field of distribution, in certain circumstances the use of exclusive contracts may give rise to a section 2 violation even though the contracts foreclose less than the roughly 40 to 50% share usually required to establish a section 1 violation. In this case, it cannot be concluded that the two contracts with Venture and Pamida were responsible for the total drop in LePage's's market share. Furthermore, even if all 3M's contracts were considered exclusive, LePage's's total drop in market share was only 21%, and some of this loss was shown in the record to be due to quality or service consistency concerns, as well as foreign competition, rather than to 3M's tactics. Therefore, there was not enough foreclosure of the market to have an anticompetitive effect.

LePage's also claims that by calculating the rebates only once a year, 3M made it more difficult for a purchaser to pass on the savings to its customers, thereby making it harder for companies to switch suppliers and keeping retail prices and margins high. As I discussed above, one-year contracts may be considered standard, and even if they make it more unlikely that rebates are passed on in the form of lower retail prices, the discounts could be applied towards lowering retail prices the following year or towards other costs by companies that are factored into the retail prices (such as advertising). In the circumstances, I am satisfied that this conduct does not qualify as predatory or anticompetitive so as to establish liability under section 2 of the Sherman Act.

LePage's also alleges that 3M entered the retail private label tape portion of the market to destroy the market and thereby increase its sales of branded tape, but the case law does not support liability under section 2 for this type of action. In *Brooke Group,* 509 U.S. at 215, Liggett/Brooke Group alleged that Brown & Williamson Tobacco Corporation ("B&W") sold generic cigarettes in order to decrease losses of sales in its branded cigarettes. B&W sold generic cigarettes at the same list price as Liggett but also offered large volume rebates to certain wholesalers so they would buy their generic cigarettes from B&W. B&W wanted to take a larger part of the generic market from Liggett and drive Liggett to raise prices on generic cigarettes, which B&W would match, thereby encouraging consumers to switch back to branded cigarettes. The

Court held that because B&W had no reasonable prospect of recouping its predatory losses and could not inflict the injury to competition that antitrust laws prohibit, it did not violate the Robinson-Patman Act or the Sherman Act. In this case, however, 3M did not use below average variable cost pricing (LePage's does not charge predatory pricing) and therefore 3M did not have predatory costs to recoup.

I recognize that LePage's attempts to distinguish *Brooke Group* on the ground that "3M used other techniques [*i.e.,* techniques other than predatory pricing] to extinguish the private-label category subjecting itself to different legal standards," but I nevertheless cannot accept LePage's's argument on this point. While LePage's does not contend that 3M engaged in predatory pricing, it does contend that the goal of 3M's other conduct was "to extinguish the private-label category, subjecting itself to different legal standards" than those applicable in *Brooke Group*. Moreover, though 3M denies that it was attempting to eliminate the private label category of transparent tape, the record supports a finding that it had that intent. I am satisfied, however, that its efforts to eliminate the private label aspect of the transparent tape market are not unlawful as, "examined without reference to its effects on competitors," it is evident that in view of 3M's dominance in brand tape, that it was rational for it to want the sale of tape to be concentrated in that category of the market. Thus, we should not uphold the verdict on that basis.

Accordingly, I conclude that 3M's actions in the record, including the bundled rebates and other elements of the "monopoly broth," were not anticompetitive and predatory as to violate section 2 of the Sherman Act. Thus, I would reverse the judgment of the district court and remand the case for entry of judgment in favor of 3M. Judge Scirica and Judge Alito join in this opinion.

Cascade Health Solutions v. PeaceHealth

502 F.3d 895 (9th Cir. 2007)

GOULD, CIRCUIT JUDGE

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., 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. . . . .

B

. . . 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. . . . .

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. . . 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). . . .

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. 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. . . .

Bundled discounts generally benefit buyers because the discounts allow the buyer to get more for less. . . .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. . . .

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 competition."). Consistent with that principle, we should not be too quick to condemn price-reducing bundled discounts as anticompetitive, 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).

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.

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). . . .

As the bipartisan Antitrust Modernization Commission ("AMC") 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 monopolist are anticompetitive with respect to its competitors who do not manufacture an equally diverse product line. Anti-trust 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 pro-competitive bundled discounts from antitrust scrutiny. The AMC proposed that:

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

In addition, the Supreme Court has forcefully suggested that we should not condemn prices that are above some measure of incremental cost. . . .

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. . . .

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).

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. Accordingly, we hold that the exclusionary 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. . . .

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

[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.

one-good rivals were foreclosed."). Under a discount aggregation rule, anticompetitive bundled discounting schemes that harm competition may too easily escape liability. . . .

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. . . .

[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. . . .

Instead, as our cost-based rule, we adopt what amici refer to as a "discount attribution" standard. 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]

[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 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.

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]. . .

6. 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.

[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.