# ANTITRUST LAW

## Unit 16: Introduction to Unilateral Conduct Offenses

Preliminary--Lacks Seminal Cases

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[1] The Section 2 Report was issued by the Bush administration on Sept. 11, 2008, and was withdrawn by the Obama administration on May 11, 2009).

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# Unilateral Conduct Offenses

# UNILATERAL CONDUCT OFFENSES
## The Sherman Act

### Section 2. Monopolizing trade a felony; penalty

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 $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court. [15 U.S.C. § 2]

## AN INTRODUCTION TO THE LAW OF MONOPOLIZATION

Section 2 of the Sherman Act prohibits monopolization, attempted monopolization, and conspiracies to monopolize. Section 2 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 $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.[1]

Section 2 is violated only when there is "conduct which unfairly tends to destroy competition itself."[2] Unlike Section 1, which requires no fundamental alteration of market structure, Section 2 is "aimed primarily not at improper conduct but at a pernicious market structure in which the concentration of power saps the salubrious influence of competition."[3] Section 2 is primarily directed to unilateral action, which Section 1 does not reach, although Section 2 can reach concerted action as well. By its terms, Section 2 specifies three separate offenses: monopolization, attempted monopolization, and conspiracy to monopolize.

### Monopolization

Originally, the offense of monopolization focused on the acquisition by the defendant of the *power* to exclude actual and potential competitors from a substantial portion of the market or as to be able to raise prices, independently of whether that power was in fact exercised.[4] This is in keeping with the historical idea of a monopoly as a prerogative grant with the power to exclude competitors. The evil was the power to exclude; the power to raise prices was important but more secondary and in the absence of anticompetitive exclusionary conduct is not actionable under Section 2. A firm that has lawfully acquired a monopoly—say, through competition on the merits or innovation resulting in a patent grant—is free under the antitrust laws to charge a monopoly price.

1. 15 U.S.C. § 2.

2. Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993); *see* Mumford v. GNC Franchising LLC, 437 F. Supp. 2d 344, 354 (W.D. Pa. 2006) ("[A] practice is not 'anticompetitive' simply because it harms competitors . . . . Rather, a practice is 'anticompetitive' only if it harms the competitive process.") (citations omitted).

3. Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 272 (2d Cir. 1979).

4. *See* American Tobacco Co. v. United States, 328 U.S. 781, 811 (1946) ("[T]he material consideration in determining whether a monopoly exists is not that prices are raised and that competition actually is excluded but that power exists to raise prices or to exclude competition when it is desired to do so.").

Following *DuPont*, monopoly power is often defined as "the power to control prices or exclude competition" within a relevant market,[5] but this is a little loose. More precisely, monopoly power exists when the firm profitably can maintain price substantially above the competitive level for a significant period of time.[6] The idea is that a monopolist is able to charge higher prices by restricting output and creating an artificial scarcity in the market, so that customers that value the product the most bid up the market-clearing price. The cases require that this power be durable in the long run, so that the power to effect a short run price increase that quickly subsides due to entry is not sufficient to predicate a Section 2 monopolization violation.[7]

The offense of monopolization has two elements: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."[8]

*The relevant market.* The monopoly power of the alleged monopolist must be located in a relevant market.[9] "Without a definition of that market there is no way to measure [the defendant's] ability to lessen or destroy competition."[10] As a result, proof of the relevant market is generally regarded as an essential element of the plaintiff's prima facie case.[11] Moreover, a firm can possess monopoly power only in a market in which it competes.[12]

5. United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 391 (1956) ("Monopoly power is the power to control prices or exclude competition."); *see id*. at 389 ("Our cases determine that a party has monopoly power if it has, over 'any part of the trade or commerce among the several states', a power of controlling prices or unreasonably restricting competition.") (quoting Standard Oil Co. v. United States, 221 U.S. 1, 85 (1911)); *accord* United States v. Grinnell Corp., 384 U.S. 563, 571 (1966).

6. *See* Sheridan v. Marathon Petroleum Co., 530 F.3d 590 (7th Cir. 2008); Port Dock & Stone Corp. v. Oldcastle Northeast, Inc., 507 F.3d 117, 123 (2d Cir. 2007); United States v. Microsoft Corp., 253 F.3d 34, 51 (D.C. Cir. 2001) (en banc) (per curiam); AD/SAT v. Associated Press, 181 F.3d 216, 227 (2d Cir. 1999); *see also* Rio Grande Royalty Co., Inc. v. Energy Transfer Partners, L.P., 786 F. Supp. 2d 1190, 1197 (S.D. Tex. 2009) (citing, among other things, lack of allegations as to duration of defendants' market power in dismissing a monopolization claim).

7. *See, e.g.*, United States v. Syufy Enters., 903 F.2d 659, 666-67 (9th Cir. 1990) ("In evaluating monopoly power, it is not market share that counts, but the ability to maintain market share."); *accord* United States v. Dentsply Int'l., Inc., 399 F.3d 181, 189 (3d Cir. 2005).

8. United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966); *accord* Pacific Bell Tel. Co. v. Linkline Commc'ns, Inc., 555 U.S. 438, 447-48 (2009); Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004); Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 595-96 (1985).

9. *Grinnell*, 384 U.S. at 570-71; *see* Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993) (reversing finding of attempted monopolization in part because of lack of proof of any relevant market).

10. Walker Process Equip., Inc. v. Food Mach. & Chem. Corp., 382 U.S. 172, 177 (1965).

11. *See, e.g.*, IGT v. Alliance Gaming Corp., 702 F.3d 1338, 1344 (Fed. Cir. 2012); Heerwagen v. Clear Channel Commc'ns, 435 F.3d 219, 229 (2d Cir. 2006); M.A.P. Oil Co. v. Texaco Inc., 691 F.2d 1303, 1306 (9th Cir. 1982); *but cf.* E.I. du Pont de Nemours & Co. v. Kolon Indus., Inc., 637 F.3d 435, 441 (4th Cir. 2011) (noting that in analyzing Section 2 claims "courts begin with a *preliminary* inquiry into market definition, which serves as a tool to determine the defendant's

The product and geographic dimensions of a relevant antitrust market for Section 2 purposes are determined in the same way and using the same standards as proof of relevant markets under Section 7 of the Clayton Act or Section 1 of the Sherman Act, namely, reasonable interchangeability of use and high cross-elasticity of demand.

*Monopoly power*. As noted above, monopoly power is often defined as "the power to control prices or exclude competition" within a relevant market for a significant period of time. "If a firm can profitably raise prices without causing competing firms to expand output and drive down prices, that firm has monopoly power."[13] The possession of monopoly power can be proved either through direct evidence of the defendant's control over prices or exclusion of competitors or through circumstantial evidence of a sufficiently high market share in a relevant market with meaningful barriers to entry.[14]

First, monopoly power may be proved through direct evidence of supracompetitive prices, often accompanied by evidence of restricted market output.[15] Monopoly power may also be proved through direct evidence of actual exclusion of competitors from the relevant market. But proving prices are above (and output below) the competitive level can be challenging even when true since there is no ready standard for determining competitive prices or output levels. In *Radio Music License Committee, Inc. v. SESAC, Inc.*,[16] for example, the district court found the complaint sufficient on the element of monopoly power where the plaintiffs alleged that SESAC had "profitably and sustainably maintained exorbitant prices that are far greater than those charged by ASCAP and BMI, and has done so without suffering a loss of sales" and that SESAC had raised prices from 8% to 20% each year since 2009 without any contemporaneous increase in the size or popularity of its repertory.[17] Still, courts are demanding in the direct proof required for showing monopoly power, especially in the context of a plaintiff's motion for summary judgment. A mere showing of prices significantly in excess of marginal costs and a drop in price in the wake of new entry is not sufficient, at least not without an

market power") (emphasis added); Campfield v. State Farm Mut. Auto. Ins. Co., 532 F.3d 1111, 1117 (10th Cir. 2008).

12. *See, e.g.*, Discon, Inc. v. NYNEX Corp., 93 F.3d 1055, 1061-62 (2d Cir. 1996), *rev'd on other grounds*, 525 U.S. 128 (1998); Official Airline Guides, Inc. v. FTC, 630 F.2d 920, 926 (2d Cir. 1980); Olde Monmouth Stock Transfer Co., Inc. v. Depository Trust & Clearing Corp., 485 F. Supp. 2d 387, 392-93 (S.D.N.Y. 2007).

13. Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 307 (3d Cir. 2007).

14. *See, e.g.*, *Broadcom*, 501 F.3d at 307.

15. *Broadcom*, 501 F.3d at 307; United States v. Microsoft Corp., 253 F.3d 34, 51 (D.C. Cir. 2001) (en banc); Rebel Oil Co. v. Atlantic Richfield Co., 51 F.3d 1421, 1434 (9th Cir. 1995); *In re* Neurontin Antitrust Litig., MDL No. 1479, No. 02–1390 (FSH), 2013 WL 4042460, at *2 (D.N.J. Aug. 8, 2013).

16. Radio Music License Comm., Inc. v. SESAC, Inc., No. 12-CV-5807-CDJ, 2014 WL 2892391, at *9-10 (E.D. Pa. June 26, 2014).

17. *Id*. at *10.

analysis of price in relation to total costs (including any fixed development costs)[18] and perhaps without evidence of restricted output.[19]

Notably, some modern courts have held that market definition is not strictly an element of monopolization but rather only an element of a circumstantial evidence case, and that where direct evidence of monopoly power exists there is no need to define a relevant market.[20] Still other courts have taken more of a middle ground, so that plaintiffs in a direct evidence case need not prove the dimensions of the relevant market with the same degree of rigor as they would in a circumstantial evidence case but still have to prove at least roughly the boundaries of the relevant market.[21]

Second, and much more commonly, market power may be proved through circumstantial evidence that the defendant possesses a "dominant" market share along with evidence of barriers that prevent other firms in the market from expanding their output or new firms from entering.[22] The idea here is that the dominant market share allows the defendant to supply a large fraction of the output—so that an output reduction by the defendant could have a significant effect on price—and that other existing firms and new entrants cannot respond to the resulting supracompetitive prices by expanding output and reducing the market-clearing price.

In *United States v. Aluminum Co. of America*,[23] Judge Learned Hand set out what has become the seminal rule of when market share is large enough to infer monopoly power: "[O]ver ninety . . . percentage is enough to constitute a monopoly; it is

18. *See, e.g.*, *In re* Remeron Direct Purchaser Antitrust Litig., 367 F. Supp. 2d 675, 682 (D.N.J. 2005) (denying summary judgment for plaintiffs on element of monopoly power where they "provided no evidence of excessive price-cost margins or restricted output but merely [relied] on the fact that later generic manufacturers could enter the market more cheaply than Remeron's price in order to establish monopoly power").

19. *See, e.g.*, Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 307 (3d Cir. 2007) ("The existence of monopoly power may be proven through direct evidence of supracompetitive prices and restricted output."); *Neurontin*, 2013 WL 4042460, at *4 n.5, *5.

20. *See* Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 307 n.3 (3d Cir. 2007) ("Because market share and barriers to entry are merely surrogates for determining the existence of monopoly power, direct proof of monopoly power does not require a definition of the relevant market."); *accord* Behrend v. Comcast Corp., 655 F.3d 182, 192 (3d Cir. 2011); Radio Music License Comm., Inc. v. SESAC, Inc., No. 12-CV-5807-CDJ, 2014 WL 2892391, at *9-10 (E.D. Pa. June 26, 2014); *see* PepsiCo, Inc. v. Coca-Cola Co., 315 F.3d 101, 107-08 (2d Cir. 2002); Conwood Co., L.P. v. U.S. Tobacco Co., 290 F.3d 768, 783 n.2 (6th Cir. 2002).

21. *See, e.g.*, *In re* Comp. of Managerial, Prof. and Technical Employees Antitrust Litig., No. 02–2924, 2008 WL 3887619, at *8 (D.N.J. Aug. 20, 2008) ("The Third Circuit [in *Broadcom* ] did not state that the direct evidence could be completely untethered or unmoored from a roughly identified relevant market . . . . Although Plaintiffs may not need to define the relevant market with the same level of precision that is required under the traditional method of demonstrating market power, Plaintiffs are required to prove, at least roughly, the parameters of the relevant [ ] markets.") (internal citation omitted); *Neurontin*, 2013 WL 4042460, at *3.

22. Diaz Aviation Corp. v. Airport Aviation Servs., Inc., 716 F.3d 256, 265 (1st Cir. 2013); *Broadcom*, 501 F.3d at 307; Harrison Aire, Inc. v. Aerostar Int'l, Inc., 423 F.3d 374, 380 (3d Cir. 2005); *Neurontin*, 2013 WL 4042460, at *5.

23. 148 F.2d 416 (2d Cir. 1945).

doubtful whether sixty or sixty-four percent would be enough; and certainly thirty-three percent is not."[24] Following *Alcoa*, courts have usually held that a market share in excess of 70% is sufficient to prove a prima facie case of monopoly power.[25] A lower share may suffice when other evidence shows that other firms in the market either cannot or will not expand output and new firms cannot or will not enter.[26] Some circuits set a minimum share threshold below which market share evidence is insufficient as a matter of law to prove monopoly power. Generally, a firm with a market share of less than 50% cannot possess monopoly power for Section 2 purposes,[27] although the Ninth Circuit has a 65% threshold.[28]

On the other hand, courts have held that when barriers to expansion or entry are nonexistent, so that firms cannot maintain supracompetitive prices without attracting countervailing output expansions by other competitors in the market, then even evidence of high market share is insufficient to establish monopoly power.[29] In this

24. *Id*. at 424.

25. *See, e.g.*, American Tobacco Co. v. United States, 328 U.S. 781, 797 (1946) (holding that "over two-thirds of the entire domestic field of cigarettes and over 80% of the field of comparable cigarettes" constituted a "substantial monopoly"); United States v. Grinnell Corp., 384 U.S. 563, 571 (1966) (finding that "87% of the accredited central station service business leaves no doubt that the congeries of these defendants have monopoly power"); International Boxing Club, Inc. v. United States, 358 U.S. 242 (1959) (81% of championship fights); Spirit Airlines, Inc. v. Northwest Airlines, Inc., 431 F.3d 917, 935-36 (6th Cir. 2005) (finding shares of 70% and 89% sufficient to support a finding of monopoly power); see generally Byars v. Bluff City News Co., 609 F.2d 843, 850 (6th Cir. 1979 (noting that "courts have been quick to find monopoly power where the market share is 75-80% or greater").

26. *See, e.g.*, Syufy Enters. v. American Multicinema, Inc., 793 F.2d 990, 995 (9th Cir. 1986) (finding sufficient a the summary judgment stage a share of 60-69% accompanied by a fragmentation of competition with the next largest competitor having at best only a 24.7% share in a market with high barriers to entry); Pacific Coast Agricultural Export Ass'n v. Sunkist Growers, Inc., 526 F.2d 1196 (9th Cir. 1975) (finding sufficient a 45–70% market share where competitors were highly fragmented and Sunkist controlled the supply market).

27. *See, e.g.*, United States v. United States Steel Corp., 251 U.S. 417 (1920) (holding 50% market share insufficient to constitute monopoly); Ideal Dairy Farms v. John Labatt, Ltd., 90 F.3d 737, 749 (3d Cir. 1996) (finding control of 47% of the New Jersey market, "without concrete evidence of anticompetitive behavior," insufficient to show monopoly power); Domed Stadium Hotel, Inc. v. Holiday Inns, Inc., 732 F.2d 480, 489 (5th Cir. 1984) (stating "absent special circumstances, a defendant must have a market share of at least fifty percent before he can be guilty of monopolization"); *In re* Southeastern Milk Antitrust Litig., 801 F. Supp. 2d 705, 727 (E.D. Tenn. 2011) (finding a market shares in the low 40% insufficient, especially where existing competitors have expanded and new rivals have entered); Rio Grande Royalty Co., Inc. v. Energy Transfer Partners, L.P., 786 F. Supp. 2d 1190, 1197 (S.D. Tex. 2009); Yeager's Fuel v. Pennsylvania Power & Light Co., 953 F. Supp. 617, 654 (E.D. Pa. 1997) (holding "market share of 31% is insufficient as a matter of law to establish monopoly power").

28. *See* Image Tech. Servs., Inc. v. Eastman Kodak Co., 125 F.3d 1195, 1206 (9th Cir. 1997) ("Courts generally require a 65% market share to establish a prima facie case of market power.") (citing American Tobacco Co. v. United States, 328 U.S. 781, 797 (1946)).

29. *See* United States v. Dentsply Int'l, Inc., 399 F.3d 181, 188-89 (3d Cir. 2005) ("In evaluating market power, it is not market share that counts, but the ability to maintain market share.") (citing United States v. Syufy Enters., 903 F.2d 659, 665-55 (9th Cir. 1990)).

sense, barriers to entry "are factors, such as regulatory requirements, high capital costs, or technological obstacles, that prevent new competition from entering a market in response to a monopolist's supracompetitive prices."[30] In the Second Circuit, for example, even a share as high as 64% is insufficient to infer monopoly power in the absence of additional evidence showing an ability to control prices or exclude competition, such as large barriers to entry or a lack of strong competition.[31] While some courts (mistakenly) have held that a declining market share indicates the lack of monopoly power even if the absolute levels of the share remain high,[32] other courts recognize that a declining share could mean that the firm has monopoly power albeit that power is being dissipated by expansion or entry.[33] Still, a sufficiently rapid decline indicates a lack of barriers to expansion and entry and so suggests the lack of monopoly power.[34]

*Willful maintenance through exclusionary acts*. It is not enough that the defendant possess monopoly power; that power must be accompanied by some anticompetitive exclusionary conduct to obtain or maintain that power.[35] The "willful acquisition or maintenance" element of monopolization is proved through a showing that the defendant's monopoly power was created as the result of, or maintained by, exclusionary conduct, that is, conduct that excludes competitors from the relevant market. This exclusionary conduct must be anticompetitive in the sense that it reduces consumer welfare by intentionally impairing competition on the merits.[36] The Third Circuit described anticompetitively exclusionary acts as follows:

30. Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 307 (3d Cir. 2007).

31. *See* Bookhouse of Stuyvesant Plaza, Inc. v. Amazon.com, Inc., 985 F. Supp. 2d 612, 622 (S.D.N.Y. 2013) (citing PepsiCo, Inc. v. Coca-Cola Co., 315 F.3d 101, 109 (2d Cir. 2002)).

32. *See, e.g.*, Richter Concrete Corp. v. Hilltop Concrete Corp., 691 F.2d 818, 826 (6th Cir. 1982) ("The fact that [defendant's] share of the market was declining also belies whatever inference of capacity to monopolize that may be drawn from the size of its market share."); Advaanced Health–Care Servs. v. Giles Memorial Hosp., 846 F. Supp. 488, 494 (W.D. Va. 1994) ("If the defendants' market share is declining and/or other competitors' market shares are rising, then the defendants can hardly possess monopoly power."); *see also* Greyhound Computer Corp. v. IBM Corp., 559 F.2d 488, 496 n.18 (9th Cir. 1977) (noting that declining market share "may reflect an absence of market power").

33. *See, e.g.*, Oahu Gas Serv., Inc. v. Pacific Res., Inc., 838 F.2d 360, 366 (9th Cir. 1988) (finding that a decrease in the defendant's market share from 100% to 68.2% did not foreclose a conclusion that the defendant possessed monopoly power); *In re* Ductile Iron Pipe Fittings (DIPF) Direct Purchaser Antitrust Litig., Civ. No. 12–711, 2013 WL 812143, at *17 (D.N.J. Mar. 5, 2013) (finding that the decline in the defendants' market share from 100% to 90% does not foreclose a conclusion that the plaintiffs adequately pled monopoly power).

34. *See, e.g.*, United States v. Syufy Enters., 903 F.2d 659, 666-67 (9th Cir. 1990) (finding a lack of monopoly power where shares were declining rapidly and significantly).

35. *See, e.g.*, Verizon Commcn's Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004); Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 308 (3d Cir. 2007).

36. *See* Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985) ("Thus, 'exclusionary' comprehends at the most behavior that not only (1) tends to impair the opportunities of rivals, but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way.") (quoting 3 P. AREEDA & D. TURNER, ANTITRUST LAW 78 (1978);

> Broadly speaking, a firm engages in anticompetitive conduct when it attempts to exclude rivals on some basis other than efficiency or when it competes on some basis other than the merits. Conduct that impairs the opportunities of rivals and either does not further competition on the merits or does so in an unnecessarily restrictive way may be deemed anticompetitive. The line between anticompetitive conduct and vigorous competition is sometimes blurry, but distinguishing between the two is critical, because the Sherman Act directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself.[37]

Simply put, "[c]onduct that impairs the opportunities of rivals and either does not further competition on the merits or does so in an unnecessarily restrictive way may be deemed anticompetitive."[38] On the other hand, conduct that merely harms competitors, while not harming the competitive process itself, is not anticompetitive and cannot predicate a monopolization claim.[39] In analyzing Section 2 claims, the totality of the conduct should be considered and not each individual act on its own without reference to other conduct.[40]

Exclusionary conduct can come in many different forms.[41] Some types of conduct are obviously exclusionary, at least in the sense that they exclude some competitors from doing business with a particular firm. The most common example is an exclusive dealing contract that obligates the contracting firm to deal only with the defendant.[42] Likewise, tying arrangements can foreclose competitors from the

*Broadcom*, 501 F.3d at 308 ("Anticompetitive conduct may take a variety of forms, but it is generally defined as conduct to obtain or maintain monopoly power as a result of competition on some basis other than the merits.").

37. West Penn Allegheny Health Sys., Inc. v. UPMC, 627 F.3d 85, 108-09 (3d Cir. 2010) (internal quotation marks and citations omitted).

38. *Broadcom*, 501 F.3d at 308; *see* Port Dock & Stone Corp. v. Oldcastle Northeast., Inc., 507 F.3d 117, 124 (2d Cir. 2007) ("[A]nticompetitive conduct is conduct without a legitimate business purpose that makes sense only because it eliminates competition."); United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001) (en banc) (per curiam) ("[T]o be condemned as exclusionary, a monopolist's act must have 'anticompetitive effect.' That is, it must harm the competitive process and thereby harm consumers. In contrast, harm to one or more competitors will not suffice.").

39. Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 224 (1993).

40. Continental Ore Co. v. Union Carbide & Carbon Corp., 370 U.S. 690, 699 (1962) (observing that Section 2 plaintiffs "should be given the full benefit of their proof without tightly compartmentalizing the various factual components and wiping the slate clean after scrutiny of each.").

41. *See* LePage's Inc. v. 3M, 324 F.3d 141, 152 (3d Cir. 2003) ("'Anticompetitive conduct' can come in too many different forms, and is too dependent upon context, for any court or commentator ever to have enumerated all the varieties.").

42. Unit 20 deals with exclusive contracts.

market for the tied product.[43] In some circumstances, below-cost ("predatory") pricing[44] and mixed bundling[45] can foreclose competitors.

But it is not enough that the conduct be exclusionary; it must be *anticompetitively* exclusionary, that is, the conduct must not have an efficiency justification and its value to the defendant must lie primarily in the exclusion of its competitors. For this reason, conduct that excludes competitors by drawing away customers through a superior value proposition, such as a better product, the exercise of superior business judgment, lower prices (as long as they are not predatory), or the development of a superior brand reputation, is not exclusionary and cannot predicate a monopolization violation, even if, as a result, the firm gains a monopoly market share. Anticompetitive exclusionary conduct is the key to a monopolization violation. As the Supreme Court recognized in *Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP*,[46] "[t]o safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct."[47] Indeed, "[a] monopolist, no less than any other competitor, is permitted and indeed encouraged to compete aggressively on the merits, and any success it may achieve solely through 'the process of invention and innovation' is necessarily tolerated by the antitrust laws."[48]

Although courts are very skeptical about monopolization claims predicated on a dominant firm's product design decisions, there are circumstances in which design decisions can be anticompetitively exclusionary. The most well-known case is *United States v. Microsoft Corp.*,[49] where the government showed that Microsoft engaged in anticompetitive exclusionary conduct when it integrated its web browser (Internet Explorer) into its Windows 98 operating system, for which Microsoft provided no procompetitive justification and which had the effect of excluding competitive web browsers. The court concluded that, since web browsers were the most likely source of future competition to Microsoft's operating system, Microsoft's design decision served no purpose other than protecting its operating system

43. The canonical form of a tying arrangement is that the seller will only sell Product A (the desired or "tying" product) to the buyer if the buyer also buys Product B (the unwanted or "tied" product) from the seller. Unit 22 deals with tying arrangements.

44. Unit 17 deals with predatory pricing.

45. In mixed bundling, the seller sells bundles consisting of products over which the seller has market power and competitive products and prices the bundles in way that makes the bundles attractive and so draws customers away from competitors in the competitive products. In a sense, mixed bundling is a more generalized form of tying arrangement and we will treat it as well in Unit 22.

46. 540 U.S. 398, 407 (2004).

47. *Id*. at 407; *accord Adderall*, 754 F.3d at 133.

48. Foremost Pro Color, Inc. v. Eastman Kodak Co., 703 F.2d 534, 544-45 (9th Cir. 1983) (quoting Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 281 (2d Cir. 1979)); *accord* Allied Orthopedic Appliances Inc. v. Tyco Health Care Group LP, 592 F.3d 991, 998 (9th Cir. 2010).

49. 253 F.3d 34, 65 (D.C. Cir. 2001).

monopoly.[50] By contrast, in *California Computer Prods., Inc. v. IBM Corp.*,[51] a competitor-manufacturer of peripheral computer devices alleged that IBM made design changes on its CPUs, disk drives and controllers that had no technological benefit and were designed solely for the purpose of foreclosing peripheral device competitors. The court, however, found uncontroverted evidence that IBM's changes allowed it to reduce manufacturing costs and prices to the consumer and also improved performance of the product and so affirmed a directed verdict for IBM. The test for design decisions is one-sided: if the design decision confers a customer benefit or a manufacturing cost reduction, the conduct is permissible under the antitrust laws without any balancing of the benefits of the improvement against its anticompetitive effects. As the Ninth Circuit observed in *Allied Orthopedic Appliances Inc. v. Tyco Health Care Group LP*:[52]

> To weigh the benefits of an improved product design against the resulting injuries to competitors is not just unwise, it is unadministrable. There are no criteria that courts can use to calculate the "right" amount of innovation, which would maximize social gains and minimize competitive injury. A seemingly minor technological improvement today can lead to much greater advances in the future. The balancing test proposed by plaintiffs would therefore require courts to weigh as-yet-unknown benefits against current competitive injuries. Our precedents and the precedents we have relied upon strongly counsel against such a test. Although one federal court of appeals has nominally included a balancing component in its test, it has not yet attempted to apply it. *See United States v. Microsoft Corp.*, 253 F.3d 34, 59, 66-67 (D.C. Cir. 2001) (including balancing as the last step of its test but not applying that step, either because the defendant had provided no justification for its product change or because the plaintiff had not rebutted the justification provided). Absent some form of coercive conduct by the monopolist, the ultimate worth of a genuine product improvement can be adequately judged only by the market itself.[53]

The challenged conduct must also be *effective* in excluding competitors. Conduct that appears unfair will not rise to the level of being anticompetitively exclusionary unless competitors are materially threatened by it and lack the means of defending themselves in the marketplace. False advertising is a common example. False advertising is typically rejected as an anticompetitively exclusionary act, since the targets usually can defend themselves through counteradvertising or other means.[54] On the other hand, the enforcement of a patent obtained by fraud on the Patent Office can be an effective anticompetitive exclusionary act, at least when there is no

50. *Id*. at 66-67.

51. 613 F.2d 727, 735 (9th Cir. 1979).

52. 592 F.3d 991 (9th Cir. 2010).

53. *Id*. at 1000 (internal citations omitted).

54. *See, e.g.*, Innovation Ventures, LLC v. N.V.E., Inc., 694 F.3d 723, 741 (6th Cir. 2012); *see also* Houser v. Fox Theatres Mgmt. Corp., 845 F.2d 1225, 1230-31 (3d Cir. 1988) (rejecting a Section 2 claim regarding defendant's disparagement of plaintiff's box office potential because defendant's conduct was "consistent with legitimate competitive conduct").

reasonable means of “inventing around” the patent and entering the relevant market through an alternative technology. An allegation of a Section 2 violation predicated on the enforcement of a fraudulently obtained patent is known as a *Walker Process* claim, which is commonly asserted as a counterclaim in patent infringement suits.[55] In general, courts recognized fraud as an anticompetitively exclusionary act if it is effective in foreclosing competitors and securing a monopoly for the defendant.[56]

Finally, the challenged conduct must be the *proximate cause* of the foreclosure of competitors from the market. *Rambus Inc. v. FTC*[57] provides a good example. Between 1991 and 1996, Rambus participated in a standard-setting process conducted by the Joint Electron Device Engineering Council, the leading standard-setting organization (SSO) for the computer industry. The FTC found that Rambus deceptively failed to disclose its patent interests in four technologies in dynamic random access memory (DRAM) when JEDEC was setting standards that included these technologies. In 1999, after the standards were set and the industry was locked into them, Rambus informed the major DRAM and chipset manufacturers that it held patent rights over technologies included in the JEDEC standards, and that the manufacture, sale, or use of products compliant with those standards infringed Rambus’ patent rights. Some manufacturers then obtained a license from Rambus for those technologies (presumably at royalty rates reflecting the market power conferred on Rambus through the adopted standards), and those that did not faced patent infringement litigation from Rambus. The FTC found that “but for Rambus’s deceptive course of conduct, JEDEC either [1] would have excluded Rambus’s patented technologies from the JEDEC DRAM standards, or [2] would have demanded RAND [reasonable and nondiscriminatory] assurances, with an opportunity for ex ante licensing negotiations.”[58] The Commission held that Rambus’ conduct constituted monopolization under Sherman Act § 2 of the markets for four technologies in issue and hence violated FTC Act § 5.[59] In a separate opinion on the appropriate remedy, the FTC prohibited Rambus from making misrepresentations or omissions to standard-setting organizations, required Rambus

55. *See* Walker Process Equip., Inc. v. Food Mach. & Chem. Corp., 382 U.S. 172 (1965).

56. *See, e.g.*, United States ex rel. Krahling v. Merck & Co., Civ. A. Nos. 10-4374, 12-3555, 2014 WL 4407969, at *12 (E.D. Pa. Sept. 5, 2014) (finding allegation that defendant’s representation to the government that its mumps vaccine had a 95% efficacy rate effectively foreclosed potential competitors from entering the market).

57. 522 F.3d 456 (D.C. Cir. 2008), *setting aside In re* Rambus Inc., 2006-2 Trade Cas. (CCH) ¶ 75,364 (F.T.C. Aug. 2, 2006) (No. 9302) (opinion on liability).

58. 2006-2 Trade Cas. (CCH) ¶ 75,364, at *40.

59. For other cases where courts have allowed a relevant market to be defined by the technologies that were competing for inclusion in an SSO-adopted standard, see, for example, Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 315 (3d Cir. 2007); ChriMar Sys., Inc v. Cisco Sys., Inc., 2014 WL 5477666, at *3 (N.D. Cal. Oct. 29, 2014); Apple Inc. v. Samsung Elecs. Co., 2012 WL 1672493, at *5 (N.D. Cal. May 14, 2012).

to license the technologies in dispute to users, and set limits on the royalty rates Rambus could charge under these mandatory licenses.[60]

The D.C. Circuit set aside the Commission's orders, finding that the Commission failed to find that Rambus' conduct had an actionable exclusionary effect. In reaching this conclusion, the court assumed without finding that Rambus' failure to disclose its patent would have been exclusionary if JEDEC would have excluded the Rambus technology in its standard had it known about Rambus' ownership interests.[61] However, the court found that if the outcome of Rambus' failure to disclose was simply higher prices—when in the "but for" world the JEDEC would have negotiated lower prices for its members to use the Rambus technology as a condition to including the Rambus technologies in the JEDEC standards—then the conduct was not exclusionary, since the charging of higher prices does not impair rivals in a manner tending to bring about or protect a defendant's monopoly power.[62] Since the Commission explicitly left open this second possibility as a consequence of Rambus' conduct, the court of appeals concluded that the Commission's finding of liability was not supported by the evidence.[63]

As a general rule the antitrust laws do not impose a duty to deal with third parties. As a result, a refusal to deal with a competitor is not deemed to be an anticompetitive exclusionary act.[64] As the *Trinko* Court explained:

> Firms may acquire monopoly power by establishing an infrastructure that renders them uniquely suited to serve their customers. Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities.[65]

There may be an exception, however, when a firm terminates a prior voluntary and profitable course of dealing with a competitor in order to enhance its market share and market power in the market.[66]

60. *In re* Rambus Inc., 2006-2 Trade Cas. (CCH) ¶ 75, 364 (F.T.C. Feb. 5, 2007) (No. 9302) (opinion on remedy).

61. *Rambus*, 522 F.3d at 463.

62. *Id*. at 464.

63. *Id*. at 466-67.

64. *See, e.g.*, Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 408 (2004) ("[A]s a general matter, the Sherman Act 'does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.'") (quoting United States v. Colgate & Co., 250 U.S. 300, 307 (1919)); *see* Christy Sports, LLC v. Deer Valley Resort Co., Ltd., 555 F.3d 1188, 1194 (10th Cir. 2009) ("Deer Valley is not required to invite competitors onto its property to rent skis to its patrons, even if a failure to do so would mean it is the sole supplier of rental skis at the ski area."); Bookhouse of Stuyvesant Plaza, Inc. v. Amazon.com, Inc., 985 F. Supp. 2d 612, 623 (S.D.N.Y. 2013).

65. *Trinko*, 540 U.S. at 407-08.

66. *See Trinko,* 540 U.S. at 409; *In re* Adderall XR Antitrust Litig., 754 F.3d 128, 133 (2d Cir. 2014); *In re* Elevator Antitrust Litig., 502 F.3d 47, 52, 53 (2d Cir. 2007) (per curiam). The source

Significantly, monopolization is a conduct offense, not a structural offense. As a result, the mere existence of a structural monopoly does not constitute monopolization.[67] At the same time, high prices are not exclusionary and so cannot predicate a monopolization offense. In *Trinko,* the Supreme Court was emphatic on both points:

> The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly prices—at least for a short period—is what attracts "business acumen" in the first place; it induces risk taking that produces innovation and economic growth. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive *conduct*.[68]

This is different in Europe, where the charging of excessively high prices by a dominant firm may be an abuse of a dominant position in violation of Article 82 of the EC Treaty.[69]

**Attempted monopolization**

Attempted monopolization has three elements: (1) the defendant must have engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power.[70]

Predatory or anticompetitive conduct is the same as exclusionary conduct that would predicate a monopolization violation.[71]

A specific intent to monopolize is the intent to destroy competition in the market in order to achieve a monopoly.[72] However, "no monopolist monopolizes

for this exception is Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985). Unilateral duties to deal in general, and *Aspen* in particular, are examined in Unit 18.

67. Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004); Rambus Inc. v. FTC, 522 F.3d 456, 463 (D.C. Cir. 2008); United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001) (en banc) (per curiam).

68. *Trinko*, 540 U.S. at 407 (2004); *see* Pacific Bell Tel. Co. v. Linkline Commc'ns, Inc., 555 U.S. 438, 447-48 (2009) (observing that "[s]imply possessing monopoly power and charging monopoly prices does not violate § 2"); Coalition For ICANN Transparency, Inc. v. VeriSign, Inc., 611 F.3d 495, 503-04 (9th Cir. 2010); Alaska Airlines, Inc. v. United Airlines, Inc., 948 F.2d 536 (9th Cir. 1991); Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 294 (2d Cir. 1979).

69. *See, e.g.*, Case 110/88, Lucazeau v. SACEM, 1989 E.C.R. 2811 (Eur. Ct. Justice); Case 30/87, Bodson v. Pompes Funebres des Regions Liberees SA, 1988 E.C.R. 2479 (Eur. Ct. Justice); Case 27/76, United Brands Co. v. Comm'n, 1978 E.C.R. 207 (Eur. Ct. Justice); Case 26/75, Gen. Motors Cont'l NV v. Comm'n, 1975 E.C.R. 1367 (Eur. Ct. Justice); Case 40/70, Sierna S.r.l. v. Eda S.r.l., 1971 E.C.R. 69 (Eur. Ct. Justice). *See generally* Organisation for Economic Co-operation and Development, Directorate for Financial and Enterprise Affairs Competition Committee, Roundtable on Excessive Prices (DAF/COMP(2011)18, Feb. 7, 2012).

70. Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 456 (1993).

71. *See, e.g.*, Kolon Indus. Inc. v. E.I. du Pont de Nemours & Co., 748 F.3d 160, 178 (4th Cir. 2014); *see also* Spectrum Sports, 506 U.S. at 459 (Section 2 "makes the conduct of a single firm unlawful only when it actually monopolizes or dangerously threatens to do so.").

unconscious of what he is doing," and so "[i]mproper exclusion (exclusion not the result of superior efficiency) is always deliberately intended."[73] Specific intent may be proved through direct or circumstantial evidence, although a bad intent without accompanying evidence of exclusionary conduct cannot support a finding of attempted monopolization. Specific intent is often inferred circumstantially from evidence of a firm's exclusionary conduct coupled with the firm's market power,[74] although some cases indicate that specific intent can be inferred from significantly anticompetitive conduct alone.[75] An intent to drive a competitor out of business through legitimate means is not probative of a specific intent to monopolize.[76]

Finally, a "dangerous probability of success" is present when the defendant's conduct is sufficiently likely to enable the firm to achieve monopoly power in the relevant market.[77] The Supreme Court first addressed the meaning of attempt to monopolize in 1905 in *Swift & Co. v. United States*.[78] Justice Holmes, writing for the Court, observed:

> Where acts are not sufficient in themselves to produce a result which the law seeks to prevent—for instance, the monopoly—but require further acts in addition to the mere forces of nature to bring that result to pass, an intent to bring it to pass is necessary in order to produce a dangerous probability that it will happen. But when that intent and the consequent dangerous probability exist, this statute, like many others and like the common law in some cases, directs itself against that dangerous probability as well as against the completed result.[79]

72. *See, e.g.*, Spirit Airlines, Inc. v. Northwest Airlines, Inc., 431 F.3d 917, 932 (6th Cir. 2005); Conwood Co., L.P. v. U.S. Tobacco Co., 290 F.3d 768, 782 (6th Cir. 2002); Tops Markets, Inc. v. Quality Markets, Inc., 142 F.3d 90, 101 (2d Cir. 1998).

73. Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 602, 603 (1985).

74. *See, e.g.*, Lenox MacLaren Surgical Corp. v. Medtronic, Inc., 762 F.3d 1114, 1130 (10th Cir. 2014); Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 318 (3d Cir. 2007).

75. *See, e.g.*, M & M Med. Supplies & Serv., Inc. v. Pleasant Valley Hosp., Inc., 981 F.2d 160, 166 (4th Cir. 1992); Thurman Indus., Inc. v. Pay 'N Pak Stores, Inc., 875 F.2d 1369, 1378 (9th Cir. 1989) (holding that specific intent may be inferred from conduct, "but only if the conduct is predatory or clearly in restraint of competition such as a per se violation under section 1"); Volvo North America Corp. v. Men's Int'l. Prof'l Tennis Council, 857 F.2d 55, 74 (2d Cir. 1988); General Indus. Corp. v. Hartz Mountain Corp., 810 F.2d 795, 802 (8th Cir. 1987); Pennsylvania Dental Ass'n v. Medical Serv. Ass'n of Pa., 745 F.2d 248, 261 (3d Cir.1984)

76. *See, e.g.*, Abcor Corp. v. AM Int'l, Inc., 916 F.2d 924, 927 (4th Cir. 1990); *Pennsylvania Dental*, 745 F.2d at 260-61 ("Even an intent to perform acts that can be objectively viewed as tending toward the acquisition of monopoly power is insufficient, unless it also appears that the acts were not predominantly motivated by legitimate business aims.") (internal quotations and citation omitted).

77. *See* Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993) ("We hold that petitioners may not be liable for attempted monopolization under § 2 of the Sherman Act absent proof of a dangerous probability that they would monopolize a particular market and specific intent to monopolize.").

78. 196 U.S. 375 (1905).

79. *Id*. at 396 (internal citation omitted).

The Court went on to explain, however, that not every act done with intent to produce an unlawful result constitutes an attempt. "It is a question of proximity and degree."[80] Under *Swift*, intent is necessary but not sufficient to prove the dangerous probability of success.[81] Holmes confirmed his interpretation in *Swift* several years later in *Hyde v. United States*.[82] In dissenting on other grounds, Holmes stated:

> An attempt, in the strictest sense, is an act expected to bring about a substantive wrong by the forces of nature. With it is classed the kindred offense where the act and the natural conditions present or supposed to be present are not enough to do the harm without a further act, but where it is so near to the result that, if coupled with an intent to produce that result, the danger is very great. *Swift & Co. v. United States*, 196 U. S. 375, 396 [(1906).] But combination, intention, and overt act may all be present without amounting to a criminal attempt,-as if all that were done should be an agreement to murder a man 50 miles away, and the purchase of a pistol for the purpose. There must be dangerous proximity to success.[83]

A "dangerous probability of success" is usually proved through an inference from a suitably high market share in the relevant market, the idea being that a high market share, coupled with exclusionary conduct and a bad intent, creates a sufficient likelihood that the defendant will achieve a monopoly share position in the marketplace. The usual rule of thumb is that an inference of a dangerous probability of success from market share alone requires a market share of 50% or more;[84] allegations of market shares between 30% and 50% shares should usually be rejected as sufficient to infer a dangerous probability, except when conduct is shown by other evidence very likely to achieve monopoly;[85] and allegations of market shares less than 30% market shares should presumptively be rejected as sufficient to infer a dangerous probability.[86] But as the Fourth Circuit explained:

80. *Id*. at 402.

81. *See Spectrum Sports*, 506 U.S. at 455.

82. 225 U.S. 347 (1912) (Holmes, J., dissenting).

83. *Id*. at 387-88; *see Spectrum Sports*, 506 U.S. at 455 n.7.

84. *See, e.g.*, Iris Wireless LLC v. Syniverse Techs., No. 8:14-cv-1741-T-30TGW, 2014 WL 4436021, at *6 (M.D. Fla. Sept. 8, 2014) (finding allegation of a market share of "50% or more" in the relevant market sufficient to support a dangerous probability of success and overcome a motion to dismiss); SSS Enters., Inc. v. Nova Petroleum Suppliers, LLC, No. 1:11–cv–1134, 2012 WL 3866490, at *2 (E.D. Va. Aug. 30, 2012).

85. *See, e.g.*, *In re* Pool Prods. Distrib. Mkt. Antitrust Litig., 940 F. Supp. 2d 367, 385-86 (E.D. La. 2013) (finding a share of 33% sufficient to infer dangerous probability on a motion to dismiss the complaint, where the complaint also alleged a pattern of acquisitions that suggest that Pool's market share has been increasing, Pool's competitors are fragmented and much smaller and likely unable to expand production significantly, and Pool's exclusionary agreements with manufacturers have created an entry barrier).

86. *See, e.g.*, H.L. Hayden Co. of N.Y. v. Siemens Med. Systs., Inc., 879 F.2d 1005, 1018 (2d Cir. 1989) (finding a market share of 20 percent, standing alone, presumptively inadequate to permit a finding of dangerous probability of success and that even a share of 30 percent might be insufficient).

> Market share is relevant, but its relevance is tempered by evidence of the other two elements of the claim. Compelling evidence of an intent to monopolize or of anticompetitive conduct reduces the level of market share that need be shown. Conversely, weak evidence of the other two elements requires a showing of significant market share. A rising share may show more probability of success than a falling share. Other factors must be considered, such as ease of entry, which heralds slight chance of success, or exclusionary conduct without the justification of efficiency, which enhances the likelihood of success.[87]

Where the defendant has been engaged in the challenged conduct for some time and its market share has not increased, courts usually will find no dangerous probability of success.[88] Likewise, where a defendant's market power is insignificant, it is unlikely that a plaintiff will be able to show a dangerous probability that the defendant will be able to gain monopoly power.[89]

In any event, proof of the dimensions of the relevant market are an essential part of establishing a dangerous probability of success and hence attempted monopolization.[90] Ease of entry, whether analyzed as part of market definition (high cross-elasticity of supply) or ease of entry per se, will negate a dangerous probability of success.[91] As in the case of monopolization, a firm cannot attempt to monopolize a relevant market in which the firm does not compete and does not intend to compete.[92]

87. M & M Med. Supplies & Serv., Inc. v. Pleasant Valley Hosp., Inc., 981 F.2d 160, 168 (4th Cir. 1992).

88. *See, e.g.*, Kolon Indus. Inc. v. E.I. du Pont de Nemours & Co., 748 F.3d 160, 178 (4th Cir. 2014); *but see* Multiflex, Inc. v. Samuel Moore & Co. , 709 F.2d 980, 991 (5th Cir. 1983) (finding adequate evidence of support for the jury’s implicit finding that there was a "dangerous probability of success" of monopolization by a competitor manufacturer even though during the period in question, defendant's share of the relevant market plummeted from over 80% to approximately 38%; other evidence showed a clear intent to freeze plaintiff out of the market through disparagement to plaintiff's bankers and potential customers).

89. *See, e.g.*, Surgical Care Ctr. of Hammond, L.C. v. Hosp. Serv. Dist. No. 1 of Tangipahoa Parish, 309 F.3d 836, 840 (5th Cir. 2002).

90. *See Spectrum Sports*, 506 U.S. at 456 (“In order to determine whether there is a dangerous probability of monopolization, courts have found it necessary to consider the relevant market and the defendant’s ability to lessen or destroy competition in that market.”); Gulf States Reorganization Group, Inc. v. Nucor Corp., 721 F.3d 1281, 1285 (11th Cir. 2013) (“A plaintiff can show this dangerous probability of success only if it can properly define the relevant market, which has both product and geographic dimensions.”); Rebel Oil Co. v. Atlantic Richfield Co., 51 F.3d 1421, 1434-35 (9th Cir. 1995).

91. *See, e.g.*, *Nucor*, 721 F.3d at 1286-87 (affirming summary judgment for defendant where there was a high cross-elasticity of supply with firms outside of the plaintiff’s alleged relevant market); Morgan, Strand, Wheeler & Biggs v. Radiology, Ltd., 924 F.2d 1484, 1490 (9th Cir.1991).

92. Discon, Inc. v. NYNEX Corp., 93 F.3d 1055, 1062 (2d Cir. 1996), *rev’d on other grounds*, 525 U.S. 128 (1998); Official Airline Guides, Inc. v. FTC, 630 F.2d 920, 921 (2d Cir. 1980); Olde Monmouth Stock Transfer Co., Inc. v. Depository Trust & Clearing Corp., 485 F. Supp. 2d 387, 392-93 (S.D.N.Y. 2007).

### Conspiracy to monopolize

Conspiracy to monopolize has three elements: (1) the existence of a combination or conspiracy, (2) an overt act in furtherance of the conspiracy, and (3) specific intent to monopolize.[93] Combination or conspiracy is proved in the same way as concerted action under Section 1 of the Sherman Act. An overt act in furtherance of the conspiracy is proved in the same way as an exclusionary act in the proof of monopolization, and may include the making of the agreement itself.[94] Specific intent is proved in the same way as specific intent in attempted monopolization.

The cases are mixed on whether the plaintiff, as part of its prima facie case, must plead and prove the dimensions of the relevant market that is the target of the conspiracy to monopolize.[95] Likewise, the cases are mixed as to whether a dangerous probability of success of achieving a monopoly is an element of the plaintiff's prima facie case of conspiracy to monopolize.[96] A dangerous probability of success should not be required, since the gravamen of the offense is the conspiracy itself and not the attainment of its objective.[97] To cabin the offense, however, some courts properly have required that the conspiracy, if successfully implemented, would result in

93. *See, e.g.*, United States v. Yellow Cab Co., 332 U.S. 218, 224-25 (1947); Am. Tobacco Co. v. United States, 328 U.S. 781, 788, 809 (1946); Howard Hess Dental Labs. Inc. v. Dentsply Int'l, Inc., 602 F.3d 237, 253 (3d Cir. 2010); Paladin Assocs., Inc. v. Montana Power Co., 328 F.3d 1145, 1158 (9th Cir. 2003); Lantec, Inc. v. Novell, Inc., 306 F.3d 1003, 1028 (10th Cir. 2002); Stewart Glass & Mirror, Inc. v. U.S. Auto Glass Discount Ctrs., Inc., 200 F.3d 307, 316 (5th Cir. 2000); Electronics Commc'ns Corp. v. Toshiba Am. Consumer Prods., Inc., 129 F.3d 240, 246 (2d Cir. 1997); TV Commc'ns Network, Inc. v. Turner Network Television, Inc., 964 F.2d 1022, 1026 (10th Cir. 1992); Gerlinger v. Amazon.Com, Inc., 311 F. Supp. 2d 838, 851 (N.D. Cal. 2004), *aff'd on other grounds*, 526 F.3d 1253 (9th Cir. 2008).

94. *See* McArthur Dairy, LLC v. McCowtree Bros. Dairy, Inc., No. 09–62033–CIV, 2011 WL 2118701, at *7 (S.D. Fla. May 27, 2011).

95. For cases requiring proof of a relevant market, see Fraser v. Major League Soccer, LLC, 284 F.3d 47, 67-68 (1st Cir. 2002); Doctor's Hosp. of Jefferson, Inc. v. S.E. Med. Alliance, Inc., 123 F.3d 301, 311 (5th Cir. 1997); Bill Beasley Farms, Inc. v. Hubbard Farms, 695 F.2d 1341, 1343 (11th Cir. 1983); Alexander v. Nat'l Farmers Org., 687 F.2d 1173, 1182 (8th Cir. 1982); Big River Indus., Inc. v. Headwaters Resources, Inc., 971 F. Supp. 2d 609, 621 ((M.D. La. 2013). For cases not requiring proof of a relevant market, see Salco Co. v. Gen. Motors Co., 517 F.2d 567, 576 (10th Cir. 1975).

96. For cases requiring proof of a dangerous probability of success, see Gulf States Reorganization Group, Inc. v. Nucor Corp., 822 F. Supp. 2d 1201, 1237 (N.D. Ala. 2011); Carpet Group Int'l v. Oriental Rug Imps. Ass'n, 256 F. Supp. 2d 249, 283 (D.N.J. 2003); Urdinaran v. Aarons, 115 F. Supp. 2d 484, 491 (D.N.J. 2000). For cases not requiring proof of a dangerous probability of success, see U.S. Anchor Mfg., Inc. v. Rule Indus., Inc., 7 F.3d 986, 1001 (11th Cir. 1993); Hunt-Wesson Foods, Inc. v. Ragu Foods, Inc., 627 F.2d 919, 926 (9th Cir. 1980); International Distrib. Ctrs., Inc. v. Walsh Trucking Co., 812 F.2d 786, 795 n.8 (2d Cir. 1987); Rheumatology Diagnostics Laboratory, Inc. v. Aetna, Inc., No. 12–cv–05847–JST, 2013 WL 3242245, at *14 (N.D. Cal. June 25, 2013); Rome Ambulatory Surgical Ctr. v. Rome Mem'l Hosp., 349 F. Supp. 2d 389, 420 (N.D.N.Y. 2004).

97. *See* American Tobacco Co. v. United States, 328 U.S. 781, 789 (1946).

monopolization.[98] Accordingly, although not part of the black letter law, in a conspiracy to monopolize case the plaintiff should plead and prove facts that the conspiracy would resulted in an illegal monopolization of the market if successful.[99]

Conspiracy to monopolize is largely a superfluous violation and is seldom invoked, since all conspiracies to monopolize also violate Section 1 of the Sherman Act.[100]

### Applying Section 2 to monopoly leveraging

Monopoly leveraging is the effort by a monopolist to extend its monopoly in one relevant market into a separate relevant market. Using monopoly power in one market to monopolize or attempt to monopolize a second market is a straightforward violation of Section 2.[101] But what if the firm uses its monopoly power in one market to obtain only a competitive advantage in the second market without any dangerous probability of success to achieve monopoly power? Led by the Second Circuit, some courts held that the "competitive advantage" version of monopoly leverage was a separate species of Section 2 violation that did not require a showing of the elements of either monopolization or attempted monopolization.[102] In 2004, the Supreme Court in *Trinko* resolved the issue by rejecting the idea that monopoly leveraging could constitute a Section 2 offense apart from monopolization or attempted monopolization.[103]

### Separability of offenses

In *American Tobacco Co. v. United States*,[104] the Supreme Court held that although attempted monopolization merges into monopolization (so that the same defendant cannot be convicted of both offenses for the same acts), conspiracy to

98. *See* Dickson v. Microsoft Corp., 309 F.3d 193, 211 (4th Cir. 2002); Black Box Corp. v. Avaya, Inc., No. 07-6161 (GEB)(JJH), 2008 WL 4117844, at *8 (D.N.J. Aug. 29, 2008); Avaya, Inc. v. Telecom Labs, Inc., No. 06-2490 (GEB)(JJH), 2008 WL 4117957, at *9 (D.N.J. Aug. 29, 2008); *see also* Big River Indus., Inc. v. Headwaters Resources, Inc., 971 F. Supp. 2d 609, 621 (M.D. La. 2013) ("In order for a plaintiff to show that there was intent to monopolize, the plaintiff must demonstrate that the monopoly was plausible, or, economically feasible.").

99. *See Dickson*, 309 F.3d at 211 (affirming the dismissal on the pleadings of a conspiracy to monopolize claim where the plaintiff failed to plead allegations regarding market power or share to show that the conspiracy would have had an anticompetitive effect if successful).

100. *See* West Penn Allegheny Health Sys., Inc. v. UPMC, 627 F.3d 85, 99 n.7 (3d Cir. 2010); Fraser v. Major League Soccer, LLC, 284 F.3d 47, 67 (1st Cir. 2002).

101. United States v. Griffith, 334 U.S. 100 (1948).

102. *See* Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 275 (2d Cir. 1979) (holding that "a firm violates § 2 by using its monopoly power in one market to gain a competitive advantage in another, albeit without an attempt to monopolize the second market"); *but see* Alaska Airlines v. United Airlines, 948 F.2d 536, 547 (9th Cir. 1991) (rejecting *Berkey Photo* and requiring the elements of monopolization or attempted monopolization to be shown).

103. Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 415 n.4 (2004).

104. 328 U.S. 781 (1946).

monopolize is a separate offense from either monopolization or attempted monopolization under Section 2 as well from conspiracy to restrain trade under Section 1. In that case, the Court rejected defendants' arguments that criminal convictions under multiple counts constituted double jeopardy since multiple punishments were imposed for the same price-fixing conduct and it sustained convictions for monopolization, conspiracy to monopolize, and conspiracy to restrain trade.[105]

In reaching this result, the *American Tobacco* court applied the rule in *Blockburger v. United States*[106] to determine whether Congress has provided that two statutory offenses are separate and may be punished cumulatively:

> The applicable rule is that where the same act or transaction constitutes a violation of two distinct statutory provisions, the test to be applied to determine whether there are two offenses or only one, is whether each provision requires proof of a fact which the other does not.[107]

Accordingly, if each statutory element of the offense "requires proof of a fact that the other does not, the *Blockburger* test is satisfied, notwithstanding a substantial overlap in the proof offered to establish the crimes."[108] The Court explained that where the offenses are reciprocally distinguishable, "[t]he fact that an offender violates by a single transaction several regulatory controls devised by Congress as means for dealing with a social evil as deleterious as it is difficult to combat does not make the several different regulatory controls single and identic."[109]

*American Tobacco* concluded that a conspiracy to restrain trade under Section 1 and a conspiracy to monopolize were separate offenses because "we have here separate statutory offenses, one a conspiracy in restraint of trade that may stop short of monopoly, and the other a conspiracy to monopolize that may not be content with restraint short of monopoly."[110] That is, a conspiracy to monopolize requires a specific intent to obtain a monopoly in the relevant market by excluding competitors, while a conspiracy to restrain trade is actionable if its objective is to fix prices even if there is no intent to exclude competitors or obtain monopoly control over the market.[111] There are criminal antitrust cases where the jury found both a Section 1

105. *Id*. at 787-89; *see* H.I. Hayden Co. of New York, Inc. v. Siemens Med. Sys., Inc., 879 F.2d 1005, 1019 (2d Cir. 1989) (finding that plaintiffs' conspiracy allegations were "reciprocally distinguishable" and hence separate offenses where the Section 1 claim was directed at the elimination of a specific competitor, whereas the Section 2 claim was directed to attaining a monopoly over sale of the relevant equipment to dentists in the United States).

106. 284 U.S. 299 (1932).

107. *Id*. at 304.

108. Iannelli v. United States, 420 U.S. 770, 785, n.17 (1975).

109. Gore v. United States, 357 U.S. 386, 389 (1958).

110. *American Tobacco*, 328 U.S. at 788.

111. *Id*. ("In the present cases, the court below has found that there was more than sufficient evidence to establish a conspiracy in restraint of trade by price fixing and other means, and also a conspiracy to monopolize trade with the power and intent to exclude actual and potential competitors from at least a part of the tobacco industry."); *see, e.g.*, International Distrib. Ctrs., Inc.

conspiracy and a Section 2 conspiracy and sentence the defendant to separate (and even consecutive) sentences for the two violations.[112]

Similarly, the *American Tobacco* Court held that a conspiracy to monopolize and monopolization are separate offenses. Conspiracy to monopolize requires both a multiplicity of actors acting in concert with the specific intent to obtain a monopoly in the relevant market, but the offense is committed even if the conspirators have yet to acquire the monopoly they seek.[113] Monopolization, on the other hand, requires only a single actor but that actor must actually have obtained a monopoly.

**Applying Section 2 in private actions**

The Clayton Act provides private parties with a private cause of action in connection with an actual or threatened violation of the antitrust laws, including Section 2 of the Sherman Act. As in private actions for violations of Section 1, a private plaintiff seeking relief from a Section 2 violation must plead and prove it has antitrust standing, including proximate causation and actual antitrust injury for treble damages and actual or threatened antitrust injury for injunctive relief.[114]

v. Walsh Trucking Co., 812 F.2d 786, 793-94 (2d Cir. 1987); Rome Ambulatory Surgical Center, LLC v. Rome Memorial Hosp., Inc., 349 F. Supp. 2d 389, 413 n.9 (N.D.N.Y. 2004).

112. *See, e.g.*, Montrose Lumber Co. v. United States, 124 F.2d 573, 575-76 (10th Cir. 1941); United States v. Shapiro, 103 F.2d 775, 776 (2d Cir. 1939); United States v. Buchalter, 88 F.2d 625, 628 (2d Cir. 1937); United States v. MacAndrews & Forbes Co., 149 F. 836, 838 (C.C.S.D.N.Y. 1907).

113. *American Tobacco*, 328 U.S. at 789.

114. *See, e.g.*, Paladin Assocs., Inc. v. Montana Power Co., 328 F.3d 1145, 1158 (9th Cir. 2003) (conspiracy to monopolize); General Indus. Corp. v. Hartz Mountain Corp., 810 F.2d 795, 801 (9th Cir. 1987) (attempt to monopolize).

# The Seminal Monopolization Cases

# DOJ Section 2 Report

# Department of Justice

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## JUSTICE DEPARTMENT ISSUES REPORT ON ANTITRUST MONOPOLY LAW

***Report Provides Consumers, Businesses, and Policy Makers With Analysis of Single-Firm Conduct Under the Antitrust Laws***

WASHINGTON — The Department of Justice today issued a report informing consumers, businesses and policy makers about issues relating to monopolization offenses under the antitrust laws. The report, “Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act,” examines whether and when specific types of single-firm conduct may or may not violate Section 2 of the Sherman Act by harming competition and consumer welfare.

The Department’s report draws extensively on a series of joint hearings, involving more than100 participants, that the Department and the Federal Trade Commission (FTC) held from June 2006 to May 2007 to explore in depth the antitrust treatment of single-firm conduct. The 213-page report also incorporates commentary found in scholarly literature and the jurisprudence of the U.S. Supreme Court and lower courts.

Section 2 of the Sherman Act prohibits a firm from illegally acquiring or maintaining a monopoly, meaning the ability to exclude competitors and profitably raise price significantly above competitive levels for a sustained period of time. Unlike antitrust laws that prohibit anticompetitive mergers or other agreements among firms, Section 2 particularly targets single-firm conduct, such as decisions regarding whether and on what terms to sell to or buy from others. Although possessing monopoly power is not unlawful, using an improper means to seek or maintain monopoly power is unlawful where it can harm competition and consumers.

“Single-firm conduct offers some of the greatest challenges in antitrust enforcement today,” said Thomas O. Barnett, Assistant Attorney General in charge of the Department’s Antitrust Division. “While we need to identify and prohibit conduct that harms the competitive process, we also need to avoid interfering in the rough and tumble of beneficial competition that drives innovation and economic growth. This report draws on the rich body of commentary created during the hearings, judicial precedent, and scholarly research to help us better achieve both objectives. With standards that are more clear and administrable, businesses are more likely to comply with the law, violations will be easier to identify and remedy, and consumers will be better served.”

The report discusses the important role that Section 2 plays in antitrust enforcement and the principles that guide that enforcement today. The report identifies and discusses a number of areas of consensus with respect to the proper treatment of single-firm conduct and highlights and examines those areas in which there is not yet consensus. The report seeks to make progress toward the goal of developing sound, clear, objective, effective and administrable standards for Section 2 analysis. It addresses the following specific issues: monopoly power; conduct standards; predatory pricing and bidding; tying; bundled and single-product loyalty discounts; unilateral, unconditional refusals to deal with rivals; exclusive dealing; remedies; and international perspectives.

Among the observations in the report:

- Enforcement of Section 2 has been and should continue to be a key component of antitrust enforcement;

- While market share does not itself prove the existence of monopoly power, it is an important factor. When a firm has maintained a market share in excess of two-thirds for a significant period and its market position would not likely be eroded in the near future, the Department normally will presume that the firm possesses monopoly power, absent convincing evidence to the contrary;

- No single test for determining whether conduct is anticompetitive–such as the effects-balancing, profit-sacrifice, no-economic-sense, equally efficient competitor, or disproportionality tests–works well in all cases. The Department encourages the continuing development of conduct-specific tests and safe harbors;

- Vague or overly inclusive prohibitions against single-firm conduct are particularly likely to undermine economic growth and to harm consumers.

- In contrast, Section 2 prohibitions that are based on clear and objective criteria, and that are carefully tailored to conduct likely to harm the competitive process, are likely to increase economic growth and to benefit consumers. Businesses are better able to comply with the law and avoid violations; antitrust enforcers can more easily identify and prove violations; effective and administrable remedies are more likely to be available; and aggressive but beneficial competition is less likely to be deterred;

- The appropriate measure of cost in relation to predatory-pricing claims should identify loss-creating sales that could force an equally efficient rival out of the market, and such a measure should be administrable by businesses and the courts. In most cases, the best cost measure likely will be average avoidable cost;

- The historical hostility of the law to the practice of tying is unjustified, and the qualified rule of per se illegality applicable to tying is inconsistent with the U.S. Supreme Court's modern antitrust decisions and should be abandoned;

- Bundled discounting, although a common practice that frequently benefits consumers, can potentially harm competition in two different ways. Accordingly, depending on particular facts, either an analysis similar to predatory pricing is appropriate or an analysis similar to tying is appropriate;

- Antitrust liability for mere unilateral, unconditional refusals to deal with rivals should not play a meaningful role in Section 2 enforcement because compelling access is likely to harm long-term competition and courts are ill suited to be market regulators;

- Exclusive-dealing arrangements foreclosing less than 30 percent of existing customers or effective distribution should not be illegal;

- Remedies for conduct that is found to violate Section 2 should re-establish the opportunity for competition without unnecessarily chilling competitive practices or undermining incentives to invest and innovate;

- Further consideration of monetary damages and penalties for Section 2 violations may be useful; and

- The Department will continue to explore ways of strengthening cooperation with counterparts in foreign jurisdictions and to encourage further convergence on sound enforcement policies in this important area.

An Executive Summary of the Department's report is attached. The full report can be found on the Department of Justice's web site at www.usdoj.gov/atr/public/reports/236681.pdf

**Background on Section 2 Hearings:**

The enforcement challenge involving Section 2 of the Sherman Act led the Department of Justice and FTC in June 2006 to embark on a year-long series of joint public hearings to study issues relating to enforcement of Section 2 against different types of single-firm conduct. The "Hearings on Section 2 of the Sherman Act: Single Firm Conduct as Related to Competition" took place over 19 days and featured 29 separate panels, in which 119 different panelists participated. The hearings covered a wide range of general topics, such as monopoly power, remedies, and international issues, as well as specific types of conduct, including predatory pricing and bidding, bundled and single-product loyalty discounts, tying and refusals to deal. Participants included members of the bar, economists and academics and representatives of the business community. The agencies also received numerous written submissions from participants and non-participants.

Complete information on the hearings, including transcripts, submissions and lists of participants, can be found at www.usdoj.gov/atr/public/hearings/single_firm/sfchearing.htm

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08-787

**STATEMENT OF COMMISSIONERS HARBOUR, LEIBOWITZ AND ROSCH ON THE ISSUANCE OF THE SECTION 2 REPORT BY THE DEPARTMENT OF JUSTICE**[1]

Today the Department of Justice ("the Department") issued a Report that, if adopted by the courts, would be a blueprint for radically weakened enforcement of Section 2 of the Sherman Act.[2] We recognize that, in response to our concerns, today's Report includes more balanced discussion sections than earlier drafts we reviewed. Nevertheless, the final Report's descriptions and conclusions respecting how Section 2 is and should be enforced cannot be said to represent the consensus, or even the prevailing, view of the myriad of stakeholders interested in Section 2 enforcement. The Report also goes beyond the holdings of the Supreme Court cases upon which it relies. The Federal Trade Commission ("FTC") does not endorse the Department's Report.

We have two overarching concerns with the Department's Report. First, the U.S. Supreme Court has declared that the welfare of *consumers* is the primary goal of the antitrust laws.[3] However, the Department's Report is chiefly concerned with firms that enjoy monopoly or near-monopoly power, and prescribes a legal regime that places these firms' interests ahead of the interests of consumers. At almost every turn, the Department would place a thumb on the scales in favor of firms with monopoly or near-monopoly power and against other equally significant stakeholders.

Second, the Report seriously overstates the level of legal, economic, and academic consensus regarding Section 2. For example, the witnesses who participated on the hearing panels were far from unanimous in their opinions about what the settled law was, much less what it should be.[4] Indeed, in hindsight, we are concerned that the testimony gathered during the hearings was not representative of the views of all Section 2 stakeholders, despite the best efforts of the two agencies to assemble balanced witness panels. In particular, we are concerned that voices representing the interests of consumers were not adequately heard. And insofar as the Report relies on economic

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[1] Chairman William E. Kovacic does not join this statement and writes separately.

[2] U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT (2008), *available at* http://www.usdoj.gov/atr/public/reports/236681.pdf [hereinafter REPORT]. Section 2 prohibits, among other things, monopolization and attempts to monopolize.

[3] Reiter v. Sonotone Corp., 442 U.S. 330, 342 (1979).

[4] We express our appreciation to Commission and Department staff members who labored long and hard to put together the Section 2 hearings. We are equally appreciative of the time and effort invested by all of the witnesses who testified at the hearings (identified in an Appendix to the Department's Report), and we join the Department in saluting them for their contributions.

theory, the recent warning of Justice Breyer bears repeating: while economic theory is an important consideration in applying antitrust law, economic theory is not tantamount to the law itself.[5]

We envisioned a Report that would identify outstanding issues in Section 2 enforcement; provide neutral and balanced illustrations of the conflicting positions that have been taken on those issues; and suggest topics for further study to help resolve the debate. Such a Report would carefully distinguish between Supreme Court holdings and *dicta* in terms of their precedential value. Additionally, it would take special care not to imply that the testimony at the hearings was representative of the views of all of the Section 2 stakeholders. Such a Report would have made a significant contribution to Section 2 jurisprudence.

## I. The Report's Premises

The Department's descriptions of its Section 2 enforcement intentions are based on four fundamental premises. First, the Report embraces the theory that the promise of monopoly profits drives firms to innovate and compete.[6] Anticipated financial rewards certainly drive innovation and competition. But this does not guarantee that profits resulting from monopoly power will have the same beneficial market effects as profits resulting from competition. Monopolies have been appropriately criticized because they tend toward inefficiency and have reduced incentives to

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5 Leegin Creative Leather Prods. v. PSKS, Inc., 127 S. Ct. 2705, 2729 (2007) (Breyer, J., dissenting) ("[A]ntitrust 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.").

6 *See, e.g.,* REPORT, Chapter 1 at 7-8; Chapter 2 at 1; Chapter 4 at 49 (low prices); Chapter 7 at 119 (refusals to deal with rivals).

innovate.[7] Monopolies also have been criticized because monopoly power in one market (even where legitimately acquired or maintained) may be used to leverage power in other markets.[8]

Second, the Report concludes that the risk of over-enforcement of Section 2 is greater than the risk of under-enforcement, contending that fear of liability leads firms to compete less aggressively.[9] The Report notes that it is often difficult to distinguish between aggressive competition and exclusionary conduct.[10] This may be true in some cases, but that challenge also exists in other areas of antitrust law and is not unique to Section 2. Regardless of the underlying theory of potential liability, antitrust counseling and enforcement decisions require an in-depth, context-specific assessment of the facts. We believe that the federal antitrust enforcement agencies and the private antitrust bar are (and will remain) up to that task, in the Section 2 realm and elsewhere.

At the same time, the Report downplays the risks of under-enforcement. The Report espouses the economic theory that monopoly power is self-destructive and that markets are self-correcting.[11] In other words, it is said that a firm with monopoly power (however that power was obtained or maintained) will not have that power forever; thus, the risks of under-enforcement are outweighed by the risks of over-enforcement. Even if correct, however, this hypothesis does not

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7 Standard Oil Co. v. United States, 221 U.S. 1, 52 (1911) (citing the danger that a monopoly will "fix the price," impose a "limitation on production," or cause a "deterioration in the quality of the monopolized product"); United States v. Aluminum Co. of Am., 148 F.2d 416, 427 (2d Cir. 1945) (Hand, J.) ("unchallenged economic power deadens initiative, discourages thrift and depresses energy"); *Federal Trade Commission and Department of Justice Hearings on Section 2 of the Sherman Act: Single-Firm Conduct As Related to Competition*, Sept. 26, 2006 Hr'g Tr., Empirical Perspectives at 13 (Scherer), *available at* http://www.ftc.gov/os/sectiontwohearings/docs/transcripts/sept26EmpiricalPerspectivestrans.pdf (observing that reluctance to "cannibalize the rents that they are earning on the products that they already have marketed" may make monopolists "sluggish innovators").

8 Town of Concord v. Boston Edison Co., 915 F.2d 17, 23-24 (1st. Cir. 1990); *compare* REPORT, Chapter 5 at 77, 90 (declaring that tying is ubiquitous, typically benefits consumers, and is often procompetitive, with no exception for situations where engaged in by a firm with monopoly or near-monopoly power).

9 *See, e.g.,* REPORT, Chapter 1 at 14-15; Chapter 3 at 46-47; Chapter 4 at 49, 69 (low prices); Chapter 5 at 88, 90 (tying); Chapter 6, section 1 at 102 (bundled discounts); Chapter 6, section 2 at 116 (loyalty discounts); Chapter 7 at 126, 129 (refusals to deal with rivals).

10 *See, e.g.,* REPORT, Chapter 1 at 9, 12-13, 18; Chapter 3 at 33-34, 43; Chapter 4 at 49 (predatory pricing); Chapter 5 at 88 (tying); Chapter 6, section 1 at 102, 104-05 (bundled discounts); Chapter 6, section 2 at 116-17 (loyalty discounts); Chapter 7 at 125-26 (refusals to deal with rivals).

11 *See, e.g.,* REPORT, Chapter 2 at 25.

adequately consider the harm consumers will suffer while waiting for the correction to occur. Markets can and do take years, even decades, to correct themselves. For one reason or another, it may take a long time for rivals to surmount entry barriers or other impediments to effective competition. Indeed, the monopolist's own deliberate conduct may further delay a market correction and prolong the duration of consumer harm.

Third, the Department repeatedly cites the "costs of administration" as a factor weighing against enforcement of Section 2.[12] Of course those costs must be considered, by the federal antitrust enforcement agencies as well as by the courts. For example, if it would be impossible to fashion a meaningful remedy for an alleged violation, arguably it is not worth challenging the suspect conduct in the first place. But no one – including the Department – has yet provided a methodology for weighing the costs and benefits of Section 2 enforcement (including potential remedies), or for comparing the relative costs and benefits to businesses versus consumers. Therefore, we do not agree that any category of conduct can be excluded from the scope of Section 2 based on the difficulty of devising an appropriate remedy.

Fourth, the Report emphasizes a need for clear and administrable rules, asserting that this need has motivated courts to fashion "bright line" tests.[13] While clear rules are desirable in the abstract, the benefits of clarity must be balanced against the benefits of effective and reasonable law enforcement, lest the interests of consumers be compromised.[14] Drawing an analogy to Section 1 enforcement, rules of *per se* illegality largely have been tempered by rule of reason analysis, despite the clear guidance afforded by earlier *per se* rules. Similarly, the Report overstates the extent to which the Supreme Court has embraced bright-line rules of *per se* legality. The only "safe harbors" blessed by the Supreme Court relate to alleged predatory pricing and bidding;[15] they were adopted because of the unique threat to consumer welfare that otherwise might result from challenges to low

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[12] *See, e.g.,* REPORT, Chapter 1 at 9, 16; Chapter 2 at 4; Chapter 3 at 45; Chapter 6, section 1 at 102 (bundled discounts); Chapter 7 at 123, 126-27 (refusals to deal with rivals).

[13] *See, e.g.*, REPORT, Introduction at 2; Chapter 1 at 13-15, 17-18; Chapter 3 at 34-35; Chapter 4 at 49-50, 61, 73 (predatory pricing); Chapter 6, section 1 at 97-98, 105 (bundled discounts); Chapter 6, section 2 at 116 (loyalty discounts); Chapter 8 at 141 (exclusive dealing).

[14] We recognize that businesses are key stakeholders interested in Section 2 enforcement. Firms that enjoy monopoly or near-monopoly power are among these stakeholders, as are their rivals and customers. To the extent the federal antitrust enforcement agencies can provide detailed and transparent guidance to the business community regarding our interpretation of Section 2 and our enforcement priorities – without compromising the interests of consumers – of course we should do so.

[15] Brooke Group v. Brown & Williamson Tobacco Corp, 509 U.S. 209 (1993); Weyerhauser Co. v. Ross-Simmons Hardwood Lumber Co., 127 S.Ct. 1069 (2007). The Court has not, however, adopted the "average avoidable cost" safe harbor set forth in the Report. REPORT, Chapter 4 at 65-67.

prices.[16] The Report incorrectly suggests that the Court in *Trinko* adopted a rule of *per se* legality for refusals to deal with rivals, ignoring both the context of the case and the Court's express language to the contrary.[17]

This is not to say that the Department's premises are entirely without merit. These premises are not totally lacking in support from some of the witnesses at the Section 2 hearings, Supreme Court *dicta* in some cases, and additional scholarship. But these premises do not represent the consensus, or even the prevailing, views of the section 2 stakeholders. They do not reflect the conclusions of those who enacted Section 2 and its counterparts, who decided that, on balance, the negatives associated with the acquisition or maintenance of monopoly power outweigh the positives. Nor do these premises represent the views of the Supreme Court, as those views have been expressed by the Court in its holdings in Section 2 cases. As law enforcement agencies, the Department and the Commission must respect existing law. Of course, the agencies have an equally important obligation to encourage the development of the law – a role that the Commission, in particular, has always taken quite seriously. But with respect to Section 2 enforcement policy, neither the views of the many stakeholders, nor the Supreme Court's holdings, provide clear guidance regarding whether the drastic changes proposed by the Department are necessary. Therefore, we strongly distance ourselves from the enforcement positions stated in the Report.

## II. The Report's Law Enforcement Standards

The Department's premises lead it to adopt law enforcement standards that would make it nearly impossible to prosecute a case under Section 2 of the Sherman Act. For example, the Department's baseline test for Section 2 liability would only condemn conduct if the demonstrable anticompetitive effects are "disproportionately" greater than the procompetitive potential.[18] The disproportionality test distorts the rule of reason standard, which simply asks whether the anticompetitive harm "outweighs" the procompetitive effects. The existing rule of reason standard already poses a significant hurdle to liability, unless care is taken to ensure that a Section 2 plaintiff does not bear a prohibitively high burden of proof.[19]

The Department also adopts specific tests for a variety of conduct such as predatory pricing, loyalty discounts, price bundling, tying, refusals to deal with rivals, and exclusive dealing. In almost every case, the Department adopts standards that are tougher – and in some cases much tougher – than existing standards as defined by Section 2 case law.

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16 *Brooke Group*, 509 U.S. at 226-27.

17 Verizon Comms. Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004).

18 REPORT, Chapter 3 at 45.

19 *See, e.g.*, United States v. Microsoft, 253 F.3d 34 (D.C. Cir. 2001).

1. Predatory Pricing

With respect to predatory pricing, the Department states that as long as prices are above a firm's "average avoidable costs" (which would not include any costs incurred before the alleged predatory pricing occurs), the firm's pricing is legal.[20] The Department adopts this broad rule of legality despite acknowledging that the rule could enable a firm with monopoly or near-monopoly power to exclude a rival who otherwise could constrain the firm's exercise of monopoly power. This would occur, for example, where the firm and its rival must incur large up-front costs but the "avoidable costs" of producing each unit are *de minimis*.[21] Moreover, in the event that a firm's pricing falls outside this price-cost safe harbor, the Department would allow proof of "efficiencies" as a "defense even in a setting where there is existing monopoly power."[22] No Supreme Court decision has embraced either the Department's "average avoidable cost" safe harbor or the proof of "efficiencies" as an extra defense of conduct that could facilitate foreclosure effects.[23] Indeed, the Department acknowledges that the latter defense "received little attention" at the Section 2 hearings.[24]

2. Loyalty Discounts

Similarly, in the case of loyalty discounts, the Department states that it "would likely apply a standard predatory pricing test."[25] That price-cost "safe harbor" would apply even when the loyalty discounts are so-called "first dollar" or "non-linear" discounts.[26] The Department again adopts this price-cost "safe harbor" despite recognizing that this legal standard could permit a firm with monopoly or near-monopoly power to foreclose a weaker rival from the minimum viable scale

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[20] REPORT, Chapter 4 at 65-67.

[21] *Id.* at 63-64.

[22] *Id.* at 71-72.

[23] In *Brooke Group*, the Court stated only that "an appropriate measure of cost" should be used. *Brooke Group*, 509 U.S. at 222-24. The Court did not say it would be "appropriate" to use a price-cost test that could facilitate foreclosure of rivals in a market where monopoly power exists, and the Court has never blessed an additional "efficiencies" defense in those circumstances.

[24] REPORT, Chapter 4 at 71.

[25] REPORT, Chapter 6, section 2 at 116.

[26] "First dollar" or "non-linear" discounts are discounts offered not only on the "contestable" portion of sales made to customers (sales for which the firm and its rival can both compete) but also on "uncontestable" sales (sales for which a rival cannot compete because, for example, the rival lacks the economies of scale or scope to do so). *See* REPORT, Chapter 6, section 2 at 111-12.

it would need to constrain the exercise of monopoly power.[27] In an even more striking declaration, the Department says that if a rival "remains in the market" (no matter how crippled the rival may be), the rival's existence will be treated as evidence that the loyalty discounts are legal, even if the practices fall outside the ambit of the price-cost "safe harbor."

There is no authority for these law enforcement prescriptions in the holdings of the Supreme Court or, for that matter, the holdings of the "lower court" invoked by the Department.[28] Moreover, the Department's use of the "standard" price-cost "safe harbor" (or any kind of price-cost "safe harbor"), rather than using an exclusive dealing analysis for these kinds of loyalty discounts, is inconsistent with the Report's recognition that these practices represent a form of exclusive dealing.[29]

3. Bundled Discounts

The Department acknowledges that bundled discounts can be used by a firm with monopoly or near-monopoly power to foreclose a rival from the scale it needs to constrain the firm's exercise of monopoly power, especially when the rival cannot offer all of the products in the bundle.[30] Yet the Department declares that if the rival can offer all of the products in the bundle, the "standard" price-cost safe harbor will be used.[31] If the rival cannot do so, the price-cost "safe harbor" will still be used, modified only to attribute the discount at which the bundle is sold to the products sold in common by the firm and the rival.[32] Additionally, even if the bundled discount falls outside of these price-cost "safe harbors," the Department will nevertheless consider it legal, unless a public or private plaintiff demonstrates that the practice has "no procompetitive benefit" or that the harm is "disproportionate" to the benefit.[33]

Again, no Supreme Court decision has ever blessed the use of any price-cost rules of legality for any practice except predatory pricing, and the Department is the sole author and authority for

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27 *Id.* at 107, 111-12.

28 The Supreme Court has never blessed the use of any price-cost rules of *per se* legality for any practice except predatory pricing. It is not clear that any of the lower court decisions cited in the Report involved "first dollar" or "non-linear" discounts granted by a firm with monopoly or near-monopoly power. In any event, even if such discounts were involved, the lower courts did not address their exclusionary potential.

29 REPORT, Chapter 6, section 2 at 114-15.

30 REPORT, Chapter 6 at 105-06.

31 *Id.* at 105.

32 *Id.*

33 *Id.* at 117.

use of the "disproportionality" safety net.[34] Moreover, the Report does not mention the possibility of analyzing bundled discounts as a form of exclusive dealing instead of affording them the protection of price-cost "safe harbors" and requiring proof of "disproportionality," despite the Department's recognition of the kinship between bundled discounts and "first dollar" loyalty discounts (the latter having been identified by the Department as a form of exclusive dealing).

4. Tying

The Department declares that tying is ubiquitous.[35] Contrary to existing Supreme Court case law,[36] the Department says that tying (presumably even by a firm with monopoly or near-monopoly power) "typically benefits consumers" and is "often procompetitive."[37] Tying surely benefits consumers in some instances, but the Department draws no distinction between the use of tying by a firm with monopoly power or near-monopoly power and the use of the practice by other firms.[38] Additionally, lest the practice of tying be challenged despite these admonitions, the Department would require public and private plaintiffs to prove that the anticompetitive consequences of a tying scheme are "significantly disproportionate" to any benefits.[39] As previously stated, the disproportionality test is of the Department's own making.[40] The Department's position enjoys no support in the law, and it is so ill-defined that it will be hard, if not impossible, for any public or private plaintiff to satisfy it.

5. Unilateral Refusals to Deal with Rivals

The Report flatly declares that unilateral refusals to deal with rivals "should not play a meaningful role in antitrust enforcement," regardless of a firm's monopoly power or the potential for foreclosure.[41] The Department incorrectly implies[42] that the Commission subscribed to this

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34 REPORT, Chapter 3 at 45-46.

35 REPORT, Chapter 5 at 77.

36 Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2 (1984).

37 REPORT, Chapter 5 at 90.

38 *Id.*

39 *Id.*

40 *See* REPORT, Chapter 3 at 45-46.

41 REPORT, Chapter 7 at 127, 129.

42 *Id.* at 124 and n. 71.

position in the agencies' joint April 2007 report on intellectual property issues ("IP Report").[43] The IP Report concluded that "mere unilateral, unconditional refusals to license will not play a meaningful part in the interface between patent rights and antitrust protection."[44] That statement reflected the agencies' view that the simple act of refusing to license intellectual property may not constitute a violation of the antitrust laws. That view is consistent with the Supreme Court's holding in *Illinois Tool Works* that intellectual property may or may not confer monopoly power.[45]

If a patent does confer monopoly power, however, then denial of access to the patented technology may not be a "mere" unilateral refusal to license intellectual property. A firm with monopoly power or near-monopoly power may violate Section 2 if it refuses to license to, or otherwise refuses to deal with, a rival. The Commission has never itself, or in conjunction with the Department, said otherwise. Indeed, the Supreme Court repeatedly has held, as it stated long ago in its *Colgate* decision, that when there is a "purpose to create or maintain a monopoly" there may be a duty to deal with a rival.[46] Although the Court held in *Trinko*[47] that a firm with monopoly power had no duty to deal with rivals when the public was protected by regulation of the firm's practices, the Court declared in *Trinko* that the right to refuse to deal with rivals is not unqualified.[48] The Department acknowledges this aspect of *Trinko* in its Report but fails to apply such a standard to the conclusions in this chapter.[49]

6. Exclusive Dealing

Finally, with respect to exclusive dealing, the Department adopts another "safe harbor," declaring that the practice is legal if no more than thirty percent of the market is foreclosed to a

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43 U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, ANTITRUST ENFORCEMENT AND INTELLECTUAL PROPERTY RIGHTS: PROMOTING INNOVATION AND COMPETITION (Apr. 2007), *available at* http://www.ftc.gov/reports/innovation/P040101PromotingInnovationandCompetitionrpt0704.pdf.

44 *Id.* at 6, 32.

45 Illinois Tool Works Inc. v. Independent Ink, Inc., 547 U.S. 28 (2006).

46 United States v. Colgate & Co., 250 U.S. 300 (1919) (*dictum*); Otter Tail Power Co. v. United States, 410 U.S. 366 (1973); Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 602 (1985); Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 466-467 (1992).

47 *Trinko*, 540 U.S. 398.

48 *Id.* at 408 (*citing Aspen Skiing*, 472 U.S. at 601).

49 REPORT, Chapter 7 at 122, 125.

rival.[50] According to the Report, that rule applies despite the Department's acknowledgment that a rival may need greater access to the market in order to achieve sufficient scope and scale to constrain the exercise of monopoly power.[51] The Department further declares that exclusive dealing will be considered legal, even if outside the "safe harbor," unless the public or private plaintiff can establish that the conduct has no procompetitive effects or that its anticompetitive effects are "disproportionate" to its benefits under the Department's newly-created "disproportionality" requirement.[52]

## III. <u>Conclusion</u>

The Department's Report does not consider all of the exclusionary practices that may be used to obtain or maintain monopoly power and cause harm to consumers.[53]

The Department embraces a series of "safe harbors" applicable to individual practices, even though each of these practices has substantial potential to lead to anticompetitive foreclosure if employed by a firm with monopoly power or near-monopoly power. In other words, each practice might be used by a firm with monopoly power or near-monopoly power to foreclose a rival from making sales the rival needs to compete effectively. As a result, the dominant firm might be sheltered from competition that otherwise would constrain its exercise of monopoly power.

Even for practices that fall outside the "safe harbors," the Department would impose rigorous burdens of proof on both public and private plaintiffs. These burdens of proof will be difficult, if not impossible, for plaintiffs to meet.

In short, the Department's Report erects a multi-layered protective screen for firms with monopoly or near-monopoly power. As an inevitable consequence, dominant firms would be able to engage in these practices with impunity, regardless of potential foreclosure effects and impact on consumers. Indeed, it appears that the Department intends for this screen to apply even when a firm uses two or more of these practices collectively, instead of just one practice individually.

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50 REPORT, Chapter 8 at 141.

51 *Id.* at 137.

52 *Id.* at 140.

53 As one notable example, except for a passing reference, the Report ignores forms of "cheap exclusion;" that is, virtually costless forms of exclusionary conduct, which may be employed by a firm with monopoly or near-monopoly power. *See* Susan A. Creighton, D. Bruce Hoffman, Thomas G. Krattenmaker & Ernest A. Nagata, *Cheap Exclusion*, 72 ANTITRUST L.J. 975 (2005) (citing, as examples, the Commission's *Unocal* case and the Commission's Orange Book exclusion payment cases).

This Commission stands ready to fill any Sherman Act enforcement void that might be created if the Department actually implements the policy decisions expressed in its Report. We will continue to be vigilant in investigating and, where necessary, prosecuting Section 2 violations.

The Department's Report undoubtedly will spark lively discussion and spur additional Section 2 scholarship, and we look forward to being a part of that process. In addition, we will continually seek to strengthen our relationships with our foreign counterparts, as we look around the world for additional perspectives on dominant firm conduct and other competition issues.

## *Statement of Federal Trade Commission Chairman William E. Kovacic*[1]

## *Modern U.S. Competition Law and the Treatment of Dominant Firms: Comments on the Department of Justice and Federal Trade Commission Proceedings Relating to Section 2 of the Sherman Act*

### *I. Introduction*

To advance the analysis of dominant firm conduct, the Antitrust Division of the Department of Justice (DOJ) and the Federal Trade Commission (FTC) in 2006 undertook an ambitious program of public consultations.[2] When these proceedings began, I hoped that if the agencies were to publish something based on the deliberations, they would prepare one document that reflected their common views. That did not come to pass. Today the DOJ has issued its policy prescriptions based on the proceedings and related research.[3]

Robust public debate – even between the two federal antitrust agencies – can serve the valuable end of pressing the U.S. antitrust system toward the acceptance of better practices. If one fears one's ideas cannot survive an open intellectual contest, it is time to get new ideas. I do not expect today's events to diminish the efforts of the DOJ and the FTC to cooperate in addressing key issues and in performing the valuable function of giving guidance about their views of doctrine and about their enforcement intentions.

I am most grateful to the DOJ and FTC staff attorneys, economists, and administrative professionals who organized the proceedings and worked heroically to prepare a draft report that both federal antitrust agencies might endorse. The DOJ Report acknowledges these contributions and graciously thanks the FTC team for their efforts. To

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[1] This statement draws extensively on themes developed at greater length in William E. Kovacic, *The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Behavior: The Chicago/Harvard Double Helix*, 2007 Colum. Bus. L. Rev. 1.

[2] *See* Federal Trade Commission, News Release, *Federal Trade Commission/Department of Justice Hearings on Single-firm Conduct to Begin June 20* (June 6, 2006), available online at http://www.ftc.gov/opa/2006/06/section2.htm (describing start of FTC/DOJ proceedings).

[3] U.S. Dep't of Justice, Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act (2008).

recognize the extraordinary, thoughtful participation of the FTC staff in this process, I thank Bill Cohen, Karen Grimm, Bill Adkinson, Chris Bryan, Karen Goldman, Andrew Heimert, Doug Hilleboe, Tom Klotz, Pat Schultheiss, and Jim Taronji. In a number of chapters, the DOJ Report absorbed much of the work of this outstanding group, although the specific assessments and interpretations in the DOJ document are the Department's alone. I hope the FTC finds ways to place the excellent work product of the Cohen team in the public domain for the benefit of public officials, practitioners, and researchers at home and abroad.

I had hoped that a DOJ/FTC report on the unilateral conduct deliberations would devote considerable effort to put modern developments in context – to examine how the U.S. antitrust system developed as it did, and to assess what that history means for the future of U.S. and global competition policy. Historical context can supply an extremely helpful foundation for a review of current doctrine and a statement of suggested enforcement approaches. Studying the history of enforcement of prohibitions against monopolization and attempted monopolization can identify formative influences in the evolution of the U.S. system and help assess how those influences bear upon the future development of law and policy toward dominant firms.

## *II. The Value of an Historical Perspective*

One great FTC strength in the modern era has been to understand that insights from history can be valuable in setting legal rules and enforcement policy on a sound footing. In several ways, the historical view improves the interpretation of existing judicial doctrine and the formulation of prescriptions about enforcement policy.

### *A. Path of Doctrine and Policy Governing Dominant Firms: 1930s to Present*

An examination of U.S. antitrust experience with dominant firms illuminates how greatly law and policy have changed over time. In particular, developments in U.S.

antitrust doctrine and enforcement policy since the 1970s have narrowed significantly the range of dominant firm conduct that is subject to condemnation. Before the change of direction in the past three decades, U.S. doctrine and enforcement policy toward dominant firms generally had been more intervention-minded than the competition policy systems of other jurisdictions before or since.[4] Judicial decisions adopted an expansive view of abuse. For a time in the 1940s, the Supreme Court seemed poised to dispense with the requirement of abusive conduct and endorse a no-fault theory of monopolization.[5] Although Section 2 cases in this period required some element of bad conduct, courts defined the concept of wrongful behavior so broadly that a wide range of conduct sufficed to create liability. Public enforcement policy toward dominant firms in this period also was far-reaching and at times featured ambitious efforts to restructure the affected industries through divestitures or the compulsory licensing of intellectual property.[6]

Due to doctrinal changes since the mid-1970s, dominant firms today have relatively broad freedom to choose pricing, product development, and marketing strategies as they please. Several aspects of modern Section 2 jurisprudence stand out. The first is the judiciary's almost exclusive focus on whether challenged behavior yields harmful economic effects or is likely to do so.[7] The definition of liability standards and the analysis of specific claims of unlawful exclusion overwhelmingly address efficiency effects. The relevant decisions do not consider how the defendant's conduct might have affected the

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[4] *See* William E. Kovacic, *The Modern Evolution of U.S. Competition Policy Enforcement Norms*, 71 Antitrust L.J. 377, 448-52 (2003) (hereinafter Enforcement Norms) (discussing federal government enforcement programs in late 1960s and in 1970s in United States).

[5] *See* Andrew I. Gavil, William E. Kovacic & Jonathan B. Baker, Antitrust Law in Perspective: Cases, Concepts and Problems in Competition Policy 615-17 (2d. ed. 2008) (describing how cases suggested abandonment of the improper conduct requirement).

[6] *See, e.g.*, William E. Kovacic, *Failed Expectations: The Troubled Past and Uncertain Future of the Sherman Act as a Tool for Deconcentration*, 74 Iowa L. Rev. 1105, 1106-08, 1119-20 (1989) (discussing government cases against concentrated industries in late 1960s through early 1980s).

[7] Earlier this decade, commentators noted that U.S. competition policy was shifting from reliance on the categorization of conduct toward effects-based analytical techniques that emphasize the application of overarching concepts. *See* Andrew I. Gavil et al., Antitrust Law in Perspective: Cases, Concepts and Problems in Competition Policy 38 (2002).

attainment of a more egalitarian economic environment or the pursuit of related objectives that animated competition policy at various times from the 1940s to the early 1970s.[8]

The second trait of this jurisprudence is wariness of rules that might discourage dominant firms from pursuing price-cutting, product development, or other strategies that generally serve to improve consumer welfare. This wariness reflects respect for the economic contributions of large firms and concern that overly restrictive rules will induce passivity.[9] Implicit in this view is confidence in the resilience of the U.S. economic system and the capacity of the dominant firm's rivals, suppliers, and customers to adopt effective counterstrategies to blunt exclusionary strategies. Judicial concerns about over-deterrence also appear to stem from perceptions that the existing system of private rights of action is unduly expansive. Fears about unduly expansive private enforcement are driving doctrine in an increasingly non-intervention minded direction that encumbers public agencies as well. In their efforts to correct what they believe to be overreaching by private litigants, courts are embracing liability standards that inevitably curb public enforcement bodies.

A third factor is concern for the limitations of antitrust courts and enforcement agencies to ensure that analytical approaches which are conceptually sound are applied sensibly in practice. Decisions such as *Trinko*, for example, focus directly on the relative capabilities of antitrust courts and sectoral regulators and view sectoral oversight more favorably than antitrust decisions did in the 1970s and early 1980s.[10]

Modern Supreme Court jurisprudence gives no reason to conclude that future doctrine will be less hospitable to dominant firms in the foreseeable future. A proper

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[8] *See* Terry Calvani & Craig Sibarium, *Antitrust Today: Maturity or Decline*, 35 Antitrust Bull. 123 (1990) (reviewing growing importance of efficiency and related economic goals in Supreme Court antitrust decisions since mid-1970s).

[9] *See Verizon Communs., Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 414 (2003) ("The cost of false positives counsels against an undue expansion of § 2 liability."); *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. Thus, mistaken inferences in cases such as this one are especially costly, because they chill the very conduct the antitrust laws are designed to protect.").

[10] *Trinko*, 540 U.S. at 411-17.

appreciation for these trends ought to inspire caution before one embraces the proposition that U.S. antitrust doctrine and policy today expose dominant firms to significant, systematic risks attributable to over-inclusive liability rules.

***B. Formative Intellectual Influences***

To see the trend sketched above is to ask why it happened. A fuller historical perspective would explain why U.S. antitrust system has grown more tolerant of dominant firm behavior since the mid-1970s. A key reason for the course of U.S. doctrinal and policy evolution lies in the ideas that have narrowed the zone of intervention. The intellectual DNA of U.S. antitrust doctrine governing single-firm conduct today is mainly a double helix[11] that intertwines two chains of ideas, one drawn from the Chicago School of Robert Bork, Richard Posner, and Frank Easterbrook, and the other drawn from the modern Harvard School of Phillip Areeda, Donald Turner, and Steven Breyer.[12] The combination of Chicago School and Harvard School perspectives features shared prescriptions about the appropriate substantive theories for antitrust enforcement (Chicago's main contribution to the double helix) and cautions about the administrability of legal rules and the capacity of the institutions entrusted with implementing them (Harvard's main contribution to the double helix). The double helix of ideas does not preclude enforcement, but it has supported the acceptance of presumptions that elevate the hurdles that antitrust plaintiffs must clear to prevail in the courts.

Three presumptions embedded in the Chicago-Harvard double helix stand out in the treatment of dominant firms. First, both schools generally embrace an economic efficiency orientation that emphasizes reliance on economic theory in forming antitrust rules.[13]

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[11] The image borrows from Francis Crick's and James Watson's discovery of the double helix structure of DNA. *See* James D. Watson, The Double Helix (Penguin Books 1999).
[12] By speaking of the modern Harvard School, I mean to distinguish the work of Areeda, Turner, and Breyer from the 1970s onward from the more intervention-minded scholarship that characterized the Harvard School from the 1940s through the 1960s.
[13] *See* I Phillip Areeda & Donald F. Turner, Antitrust Law, paras. 103-13 (1978); Robert H. Bork, The Antitrust Paradox 69-89 (1978).

Chicago School and Harvard School scholars do not define efficiency identically, but the two schools discourage consideration of non-efficiency objectives such as the dispersion of political power and the preservation of opportunities for smaller enterprises to compete.[14]

The second presumption endorses the elements of economic theory that favor giving individual firms broad freedom to select product development, pricing, and distribution strategies. Among other policy implications, this presumption generally disfavors intervention to control dominant firms.[15] Here Chicago School and Harvard School commentators tend to share the view that the social costs of enforcing antitrust rules against dominant firms too aggressively exceed the costs of enforcing them too weakly.[16]

The third presumption demands that courts and enforcement agencies pay close attention to considerations of institutional design and capacity in formulating and applying antitrust rules. The insistence that competition policy take account of the limitations of the institutional arrangements of the U.S. antitrust system is perhaps the Harvard School's main contribution to the double helix. Areeda and Turner urged courts and agencies to account for institutional factors and taught the precept that antitrust rules should not outrun the capabilities of implementing institutions.[17] These scholars argued that antitrust rules and decision-making tasks must be administrable for the central participants in the antitrust system (courts, enforcement agencies, the private bar, and business managers).[18] They also recommended that special substantive and procedural screens be used to ensure that private

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[14] For example, Areeda and Turner said "As a goal of antitrust policy, 'fairness' is a vagrant claim applied to any value that one happens to favor." 4 Phillip Areeda & Donald F. Turner, Antitrust Law 21 (1980).
[15] Bork, Antitrust Paradox, 163-97; Phillip Areeda & Donald F. Turner, *Predatory Pricing and Practices Under Section 2 of the Sherman Act*, 88 Harv. L. Rev. 697, 704-12 (1975).
[16] *See* Walter Adams & James W. Brock, *Areeda/Turner on Antitrust: A Hobson's Choice*, 41 Antitrust Bull. 735, 741-42 (1996) (noting similarity of views of Easterbrook, Areeda, and Turner of relative dangers of over-inclusive and under-inclusive enforcement of restrictions on dominant firm behavior).
[17] *See* I Areeda & Turner, Antitrust Law, at 31-33 (discussing institutional limitations of courts and enforcement agencies).
[18] *See* 3 Phillip Areeda & Donald F. Turner, Antitrust Law 150-53 (1978) (discussing flaws in previous judicial efforts to define illegal predatory pricing).

antitrust suits were consistent with larger social aims. An acute wariness of U.S. private rights of action (including mandatory trebling of damages, asymmetric fee-shifting, and jury trials) is a major theme of Areeda's and Turner's writing. Their concern for overly expansive private enforcement guided their proposals concerning substantive antitrust standards and procedural screens relating to standing and injury.[19]

### *III. The Chicago-Harvard Double Helix and Future U.S. Policy*

The modern Harvard School has had as much to do as the Chicago School with creating many of the widely-observed presumptions and precautions that disfavor intervention by U.S. courts and enforcement agencies. Having a clear view of the framework of formative ideas helps us we understand how these ideas can be extended or limited, stretched or collapsed. The Chicago-Harvard double helix sheds insights on two specific issues with substantial practical significance for competition policy.

The first issue is why the adjustments in U.S. doctrine and policy from 1960 to the present were so extensive and have been so enduring. Recognition of the Chicago-Harvard double helix provides an important explanation. The reorientation of U.S. competition law and policy since 1960 derived its strength from two complementary streams of thought and would have been considerably weaker if only one school had set the intellectual agenda. The reorientation would not have endured without the support of the two schools.

The second issue is to identify the content of the modern presumptions that disfavor intervention. The Chicago-Harvard double helix embodies a strong concern for over-inclusive, rather than under-inclusive, applications of competition law. This perspective assumes that the likelihood that entry and adaptability by competitors, customers, and suppliers more often than not will blunt dominant firm efforts to exercise market power.

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[19] *See, e.g.*, Areeda & Turner, *Predatory Pricing*, at 699 (in framing rules for predatory pricing, it is necessary to use "extreme care … lest the threat of litigation, particularly by private parties, materially deters legitimate, competitive pricing").

The perspective also makes important judgments based on institutional considerations and pays close attention to how institutional design affects substantive outcomes. This emerges most clearly in the Chicago/Harvard concern for the administrability of standards, the limitations of enforcement agencies and courts and the corresponding need to account for their limitations and strengths in formulating legal rules and enforcement policies, and the treatment of private rights of action and the mandatory trebling of damages.

The last consideration mentioned above may be the most important for public agencies. If, as I believe, judicial perceptions of overreaching by private suits are narrowing the zone of substantive liability, public agencies eventually may be unable to do their job. This consideration points to the need for a deeper empirical examination of how the operation of private rights actually affects business decision making and how public agencies can prosecute cases without carrying burdens that courts have imposed on private litigants to cure perceived deficiencies in the system of private rights.

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## JUSTICE DEPARTMENT WITHDRAWS REPORT ON ANTITRUST MONOPOLY LAW

***Antitrust Division to Apply More Rigorous Standard With Focus on the Impact of Exclusionary Conduct on Consumers***

WASHINGTON — Christine A. Varney, Assistant Attorney General in charge of the Department's Antitrust Division, today announced that the Department is withdrawing, effective immediately, a report relating to monopolization offenses under the antitrust laws that was issued in September 2008. As of today, the Section 2 report will no longer be Department of Justice policy. Consumers, businesses, courts and antitrust practitioners should not rely on it as Department of Justice antitrust enforcement policy.

The report, "Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act," raised too many hurdles to government antitrust enforcement and favored extreme caution and the development of safe harbors for certain conduct within reach of Section 2, Varney said. Varney announced the withdrawal of the report today at a speech at the Center for American Progress.

"Withdrawing the Section 2 report is a shift in philosophy and the clearest way to let everyone know that the Antitrust Division will be aggressively pursuing cases where monopolists try to use their dominance in the marketplace to stifle competition and harm consumers," said Varney. "The Division will return to tried and true case law and Supreme Court precedent in enforcing the antitrust laws."

The report was issued after a series of joint hearings, involving more than 100 participants, that the Department and the Federal Trade Commission (FTC) held from June 2006 to May 2007 to explore the antitrust treatment of single-firm conduct. The FTC did not join with the Department in its report.

Varney said that while there is no question that Section 2 cases present unique challenges, the report advocated hesitancy in the face of potential abuses by monopoly firms. She said that implicit in this overly cautious approach is the notion that most unilateral conduct is driven by efficiency and that monopoly markets are generally self-correcting. "The recent developments in the marketplace should make it clear that we can no longer rely upon the marketplace alone to ensure that competition and consumers will be protected," Varney added.

"I want to commend the efforts of those who participated in the Section 2 hearings," said Varney. "While I do not agree with the conclusions of the Section 2 report, I do believe that the hearings and the report provided a valuable discussion of the enforcement issues involving single-firm conduct."

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09-459

## AFTERMATH OF THE SECTION 2 REPORT WITHDRAWAL

The Antitrust Division withdrew the DOJ Section 2 Report on May 11, 2009, as one of the first acts of the new assistant attorney general in the Obama Administration. As expected, the withdrawal was essentially symbolic. Since the withdrawal of the report more than five years ago, neither the Antitrust Division nor the FTC has taken any significant Section 2 enforcement action. In the courts, the Section 2 Report has only been cited twice, and neither time for its policy prescriptions.[1]

1. Computer Automation Sys., Inc. v. Intelutions, 998 F. Supp. 2d 3, 11 (D.P.R. 2014) (citing an example); *In re* Pool Prods. Distrib. Market Antitrust Litig., 940 F. Supp. 2d 367, 382-83 (E.D. La. 2013) (citing the report as authority for the proposition that a firm with 50% or less market share is unlikely to have market power).

# COMPETITION AND MONOPOLY:

# SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT

ISSUED BY THE

U.S. DEPARTMENT OF JUSTICE

SEPTEMBER 2008

[Executive Summary and Chapters 1-3]

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# EXECUTIVE SUMMARY

## INTRODUCTION

The U.S. antitrust laws reflect a national commitment to the use of free markets to allocate resources efficiently and to spur the innovation that is the principal source of economic growth. Section 2 of the Sherman Act plays a unique role in U.S. antitrust law by prohibiting single-firm conduct that undermines the competitive process and thereby enables a firm to acquire, credibly threaten to acquire, or maintain monopoly power.

Competition and consumers are best served if section 2 standards are sound, clear, objective, effective, and administrable. After more than a century of evolution, section 2 standards have not entirely achieved these goals, and there has been a vigorous debate about the proper standards for evaluating unilateral conduct under section 2. In June 2006, the Department of Justice (Department) and the Federal Trade Commission (FTC) began a series of wide-ranging hearings relating to unilateral conduct under section 2. The hearings encompassed twenty-nine separate panels and were conducted over the course of an entire year. Academics, businesspeople, and antitrust practitioners presented a broad array of views.

This report synthesizes views expressed at the hearings, in extensive scholarly commentary, and in the jurisprudence of the Supreme Court and lower courts. It reflects the Department's enforcement policy and is intended to make progress toward the goal of sound, clear, objective, effective, and administrable standards for analyzing single-firm conduct under section 2.

## CHAPTER 1: Overview

Chapter 1 provides an overview of section 2 and its application. This overview explains that the purpose of section 2 is to prevent conduct that harms the competitive process, while not discouraging aggressive competition, whether that aggressive competition is from monopolists or other competitors. Chapter 1 also articulates and elaborates on basic principles that have emerged from court decisions and commentary:

1. Single-firm conduct comes within the scope of section 2 only if the firm possesses, or is likely to achieve, monopoly power.
2. Section 2 does not prohibit the mere possession or exercise of monopoly power.
3. Acquiring or maintaining monopoly power through conduct harming the competitive process should be condemned.
4. Section 2 protects the competitive process but not individual competitors.
5. Distinguishing beneficial competitive conduct from harmful exclusionary or predatory conduct often is difficult.
6. Section 2 standards should prevent conduct that harms the competitive process, but should avoid overly broad prohibitions that suppress legitimate competition.
7. Section 2 standards should be understandable and clear to businesspeople and judges and must account for the possibility of error and administrative costs in their application.

## CHAPTER 2: Monopoly Power

Chapter 2 addresses the meaning and identification of monopoly power.

***Meaning of a Dominant Market Share.*** A dominant market share typically is a prerequisite for the possession of monopoly power, but it is only a starting point for determining whether a competitor possesses monopoly power. Competitive conditions must be such that the competitor can persistently charge prices well above competitive levels without substantial erosion of its dominant position through the expansion of incumbent rivals or the entry of new competitors. Where courts have found monopoly power—as opposed to market power—the defendant's market share has been at least fifty percent and typically substantially higher.

When a firm has maintained a market share in excess of two-thirds for a significant period and the Department concludes that market conditions likely would prevent the erosion of its market position in the near future, the Department will presume that the firm possesses monopoly power absent convincing evidence to the contrary.

***Market Definition.*** Defining the market involves an assessment of likely substitution by customers in response to an exercise of monopoly power. This assessment can be problematic in a monopoly-maintenance case because the threshold issue is whether the defendant already possesses, and hence already is exercising, monopoly power. It is important in those cases not to evaluate substitution possibilities at the prevailing monopoly price, but it is difficult to evaluate substitution possibilities at hypothetical prices significantly below prevailing levels. The Department views direct evidence of anticompetitive effects as useful but normally not sufficient by itself to demonstrate monopoly power in the absence of a defined antitrust market.

## CHAPTER 3: General Conduct Standards

Chapter 3 initially discusses the importance of an appropriate framework that structures the analysis, including an efficient allocation of burdens of production and proof in litigation. The plaintiff should have the initial burden of establishing that challenged conduct harms the competitive process and therefore has a potentially anticompetitive effect. If plaintiff carries that burden, defendant should have the opportunity to proffer and substantiate a procompetitive justification for the challenged conduct. If defendant does so, plaintiff then should have the burden of establishing that the challenged conduct is anticompetitive under the applicable standard. This allocation can enable courts to resolve cases more quickly and efficiently.

Turning to the general tests, the Department does not believe that any one test works well in all cases and encourages the development of conduct-specific tests and safe harbors, which are discussed in subsequent chapters. The five general tests discussed in the chapter are:

***Effects-Balancing.*** Although focusing analysis on the effect on consumer welfare is appropriate, the Department does not believe that using an effects-balancing test as a general standard under section 2 is likely to maximize consumer welfare. The Department believes that it is better for long-run economic growth and consumer welfare not to incur the costs and errors from attempting to quantify and precisely balance procompetitive and anticompetitive effects as required under this test.

***Profit-Sacrifice.*** The Department believes that a profit-sacrifice test that asks whether conduct is more profitable in the short run than other less-exclusionary conduct the firm could have undertaken raises serious concerns of enforcement error and administrability and should not be the test for section 2 liability. The Department believes that a firm should not be liable for failure to maximize its profits.

***No-Economic-Sense.*** The Department finds the no-economic-sense test useful, among other things, as a counseling device to focus businesspeople on the reasons for undertaking potentially exclusionary conduct. At the same time, the Department does not believe that a trivial benefit should protect conduct that is significantly harmful to consumers and the competitive process. Therefore, the Department does not believe that this test should serve as the general standard under section 2.

***Equally Efficient Competitor.*** The Department finds it useful to ask in pricing cases whether conduct would exclude an equally efficient competitor. In non-pricing cases, that inquiry does not readily lead to administrable rules, and, even in pricing cases, there is difficulty in comparing the efficiency of two firms doing different things. Accordingly, the Department does not believe that this test should be the general standard for liability under section 2.

***Disproportionality.*** In the absence of an applicable conduct-specific test, the Department believes that conduct should be unlawful under section 2 if its anticompetitive effects are shown to be substantially disproportionate to any associated procompetitive effects. While also subject to valid criticism, the test focuses on the consumer-welfare goals of antitrust and represents the best combination of effectiveness and administrability (including the need to avoid chilling beneficial competition) of the general tests identified to date.

## CHAPTER 4: Predatory Pricing

Chapter 4—the first chapter addressing a specific category of potentially exclusionary conduct—focuses on predatory pricing. In 1993 the Supreme Court held that a plaintiff alleging predatory pricing must show that the defendant cut prices below an appropriate measure of its costs and had a dangerous probability of recouping its investment in below-cost prices. While acknowledging that above-cost pricing can sometimes be exclusionary, the Court held that attempting to identify such instances would harm beneficial price competition. The Department believes that the Court's holding is consistent with promoting competition and consumer welfare under section 2.

***Measure of Cost.*** The courts have not settled on an appropriate measure of cost for evaluating predatory-pricing claims. Consistent with the thinking expressed in case law, the Department concludes that the appropriate measure of cost should identify loss-creating sales that could force an equally efficient rival out of the market and that such a measure should be administrable by businesses and the courts.

In most cases, the best cost measure likely will be average avoidable cost. This measure of cost includes fixed costs to the extent that they were incurred only because of the predatory strategy, for example, as a result of expanding capacity to enable the predatory sales. When an increment to a defendant's output associated with the predatory strategy cannot be identified, the best cost measure typically is average variable cost. The Department does not favor the use of average variable cost in general because it does not focus on the predatory scheme itself and does not indicate as reliably whether the firm might be losing money to achieve anticompetitive ends.

***Recoupment.*** The Department believes that the recoupment requirement is an important reality check in assessing predatory-pricing allegations. Without a dangerous probability that the investment in below-cost prices will be recouped through later supracompetitive pricing, below-cost prices most likely reflect nothing more than intense price competition that is in the interests of consumers. In some cases, focusing first on recoupment may avoid difficult issues in comparing prices with costs. The Department believes that recoupment outside the relevant market may be relevant in some cases.

***Predatory Bidding.*** In 2007 the Supreme Court applied its two-part test for predatory pricing to predatory bidding. The Court reasoned that, in important respects, predatory bidding is the mirror image of predatory pricing and therefore that the same sort of analysis is required to avoid chilling procompetitive conduct. The Department supports the Court's ruling and analysis.

## CHAPTER 5: Tying

Chapter 5 discusses various forms of tying—selling a product only on the condition that the buyer also purchase a second product. Examples of tying include contractual restrictions on future purchases of consumable complements to a durable good, the simultaneous sale of two or more products only in a bundle, and linking two products technologically.

In some circumstances, tying can allow a competitor with monopoly power over one product to acquire monopoly power in a tied product or to maintain its monopoly in the tying product. Those circumstances, however, are limited.

In many others, tying can promote efficiency and benefit consumers through a reduction in production or distribution costs. It also can be used to price discriminate, which generally does not create or maintain monopoly power. Consequently, the Department believes that the historical hostility of the law to tying is unjustified. In particular, the qualified rule of per se illegality applicable to tying is inconsistent with the Supreme Court's modern antitrust decisions and should be abandoned.

Tying in the form of technologically linking products is an area where enforcement intervention poses a particular risk of harming consumers more than it helps them in the long run. Technological tying often efficiently gives consumers features they want and judicial control of product design risks chilling innovation. This form of tying, therefore, should be condemned only in exceptional cases, such as when integrating two separate products serves no purpose other than to disadvantage competitors and harms the competitive process.

## CHAPTER 6: Bundled and Loyalty Discounts

Chapter 6 considers two particular pricing practices: bundled discounts and loyalty discounts.

***Bundled Discounts.*** When a defendant's rivals can effectively compete on a bundle-to-bundle basis, bundled discounting is much like single-product price cutting, and the practice is best analyzed as predatory pricing.

When a defendant's rivals cannot compete bundle-to-bundle, discounts or rebates work more like tying, and a different analysis is appropriate. In those circumstances, the Department believes a cost-based safe harbor for bundled discounting, in which an imputed price for the item (or items) in the bundle potentially subject to competition is computed by allocating to that item (or items) the entire discount or rebate received by a customer, is appropriate. The rationale of this safe harbor is that an equally efficient competitor that does not sell all the items in the bundle would not be excluded if this imputed price exceeds an appropriate measure of a defendant's cost.

Bundled discounting failing this safe harbor is not necessarily anticompetitive and should not be presumed to be so. Rather, a plaintiff should be required to demonstrate that the practice has harmed the competitive process or likely would do so if allowed to continue. If the defendant demonstrates that the practice has a procompetitive explanation, it should be condemned only if plaintiff demonstrates a substantially disproportionate anticompetitive harm.

***Loyalty Discounts.*** Chapter 6 also considers single-product loyalty discounts. Single-product loyalty discounts often are procompetitive, but they can be anticompetitive under certain limited circumstances. The Department is inclined to treat this practice as predatory pricing and therefore consider the discounting lawful unless the seller's revenues are less than an appropriate measure of its costs. This approach is administrable, guards against chilling legitimate discounting, and is especially appropriate if the seller's rivals can reasonably compete for the entirety of a customer's purchases.

When a significant portion of a customer's purchases are not subject to meaningful competition, the Department recognizes the possibility that single-product loyalty discounts might produce an anticompetitive effect even though the discounted price over all of a customer's purchases exceeds the seller's cost. Accordingly, the Department believes that further study of the real-world impact of the practice is necessary before concluding that standard predatory-pricing analysis is appropriate in all cases.

## CHAPTER 7: Unilateral, Unconditional Refusals to Deal with Rivals

Chapter 7 discusses unilateral, unconditional refusals by firms with monopoly power to deal with their rivals. Such refusals can include refusing to sell inputs, license intellectual property rights, or share scarce resources. In certain decisions, the Supreme Court held that such refusals violated section 2, but the Court's most recent decision on this subject took a very cautious approach. Compelling access to inputs, property rights, or resources undoubtedly can enhance short-term price competition, but doing so can do more harm than good to the competitive process over the longer term.

The Department agrees with the Court that forcing a competitor with monopoly power to deal with rivals can undermine the incentive of either or both to innovate. The Department also agrees with the Court that judges and enforcement agencies are ill-equipped to set and supervise the terms on which inputs, property rights, or resources are provided. Thus, the Department concludes that antitrust liability for mere unilateral, unconditional refusals to deal with rivals should not play a meaningful role in section 2 enforcement.

## CHAPTER 8: Exclusive Dealing

Chapter 8 addresses the practice of exclusive dealing. Exclusive dealing can enhance efficiency by aligning the incentives of trading partners, by preventing free riding, and in other ways. Exclusive dealing also can undermine the competitive process by, for example, barring smaller competitors from efficient distribution channels and denying them the ability to operate at efficient scale.

The Department believes that exclusive-dealing arrangements foreclosing less than thirty percent of existing customers or effective distribution should not be illegal. The Department does not believe that the legality of an exclusive-dealing arrangement should be determined solely by the explicit duration of the contract or agreement. When a firm with lawful monopoly power utilizes exclusive dealing, the Department will examine whether the exclusive dealing contributed significantly to maintaining monopoly power and whether alternative distribution channels allow competitors to pose a real threat to the monopoly before potentially imposing liability.

## CHAPTER 9: Remedies

Chapter 9 focuses on remedies in section 2 cases. Implementing effective remedies is key to section 2 enforcement.

***Equitable Remedies.*** Section 2 equitable remedies should terminate a defendant's unlawful conduct, prevent its recurrence, and re-establish the opportunity for competition. And they should do so without imposing undue costs on the court or the parties, without unnecessarily chilling legitimate competition, and without undermining incentives to invest and innovate. This often is a daunting challenge.

The Department believes that prohibiting a defendant from engaging in specific acts, defined by clear and objective criteria, is the proper remedy if it would be effective. In some circumstances, however, re-establishing the opportunity for competition requires the imposition of additional affirmative obligations on defendant. Structural remedies, including various forms of divestiture, may be appropriate if there is a clear, significant causal connection between defendant's monopoly power and the unlawful acts. Radical restructuring of the defendant, however, is appropriate only if there is no other way to achieve the remedial goals and the determination is made that such restructuring would likely benefit consumers.

***Monetary Remedies.*** The Department believes that further consideration of appropriate monetary damages and penalties for section 2 violations may be useful.

## CHAPTER 10: International Perspective

Chapter 10 offers an international perspective. Over one hundred nations have antitrust laws, nearly all including provisions on single-firm exclusionary conduct, but there are significant differences among various countries' laws, legal institutions, and enforcement policies. With increasingly globalized markets, the diversity of competition regimes has raised concerns. Firms doing business globally, when confronted with, for example, a product-design decision, may be pushed to conform to the rules of the most restrictive jurisdiction. Certain types of remedies, such as mandatory disclosures of intellectual property, also have global impacts.

The Department and the FTC have addressed the challenges posed by multi-jurisdictional enforcement against single-firm exclusionary conduct in several ways. They have entered into bilateral cooperation agreements with seven countries and the European Communities. They actively participate in several international organizations, such as the International Competition Network and the Organisation for Economic Co-Operation and Development. And they provide technical assistance to nations in the early stages of adopting and implementing antitrust laws. The Department will continue to explore ways of strengthening cooperation with counterparts in other jurisdictions and increasing convergence on sound enforcement policies.

## CONCLUSION

The Department believes that the hearings advanced the debate with respect to the appropriate legal standards for single-firm conduct under section 2 of the Sherman Act. The Department hopes that this report will contribute to the public debate in this complex but important area, and that it makes progress toward the goal of sound, clear, objective, effective, and administrable standards for analyzing single-firm conduct. The Department, of course, will continue to review the legal and economic scholarship in this area, to learn from its own investigations and cases, to consult with other enforcement officials, and to engage in the public dialogue over how best to advance that goal in the future.

## CHAPTER 1

# SINGLE-FIRM CONDUCT AND SECTION 2 OF THE SHERMAN ACT: AN OVERVIEW

This chapter provides an overview of section 2 and its application to single-firm conduct. Part I describes the elements of the primary section 2 offenses—monopolization and attempted monopolization. Part II discusses the purpose of section 2 and the important role it plays in U.S. antitrust enforcement. Part III identifies key enforcement principles that flow from the U.S. experience with section 2.

### I. The Structure and Scope of Section 2

Section 2 of the Sherman Act makes it unlawful for any person to "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 . . . ."[1]

Section 2 establishes three offenses, commonly termed "monopolization," "attempted monopolization," and "conspiracy to monopolize."[2] Although this report and most of the legal and economic debate focus specifically on the two forms of monopolization—monopoly acquisition and monopoly maintenance—much of the discussion applies to the attempt offense as well.[3]

#### A. Monopolization

At its core, section 2 makes it illegal to acquire or maintain monopoly power through improper means. The long-standing requirement for monopolization is both "(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."[4]

**Monopolization requires (1) monopoly power 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.**

Regarding the first element, it is "settled law" that the offense of monopolization requires "the possession of monopoly power in the relevant market."[5] As discussed in chapter 2, monopoly power means substantial market power that is durable rather than fleeting—market power being the ability to raise prices profitability above those that would be charged in a competitive market.[6]

But, as the second element makes clear, "the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct."[7] Such conduct often is described as "exclusionary" or "predatory" conduct. This element includes both conduct used to acquire a monopoly unlawfully and conduct used to maintain a

[1] 15 U.S.C. § 2 (2000).

[2] *See, e.g.*, 1 SECTION OF ANTITRUST LAW, AM. BAR ASS'N, ANTITRUST LAW DEVELOPMENTS 225, 317 (6th ed. 2007).

[3] The conspiracy to monopolize offense addresses concerted action directed at the acquisition of monopoly power, *see generally id.* at 317–22, and is largely outside the scope of this report because the hearings focused on the legal treatment of unilateral conduct.

[4] United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

[5] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004).

[6] *See infra* Chapter 2, Part II.

[7] *Trinko*, 540 U.S. at 407 (emphasis omitted).

monopoly unlawfully. A wide range of unilateral conduct has been challenged under section 2, and it often can be difficult to determine whether the conduct of a firm with monopoly power is anticompetitive.

### B. Attempted Monopolization

Section 2 also proscribes "attempt[s] to monopolize."[8] Establishing attempted monopolization requires proof "(1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power."[9] It is "not necessary to show that success rewarded [the] attempt to monopolize;"[10] rather, "when that intent and the consequent dangerous probability exist, this statute, like many others and like the common law in some cases, directs itself against the dangerous probability as well as against the completed result."[11]

**Attempted monopolization requires (1) anticompetitive conduct, (2) a specific intent to monopolize, and (3) a dangerous probability of achieving monopoly power.**

The same principles are applied in evaluating both attempt and monopolization claims.[12] Conduct that is legal for a monopolist is also legal for an aspiring monopolist.[13] But conduct that is illegal for a monopolist may be legal for a firm that lacks monopoly power because certain conduct may not have anticompetitive effects unless undertaken by a firm already possessing monopoly power.[14]

Specific intent to monopolize does not mean "an intent to compete vigorously;"[15] rather, it entails "a specific intent to destroy competition or build monopoly."[16] Some courts have criticized the intent element as nebulous and a distraction from proper analysis of the potential competitive effects of the challenged conduct.[17] One treatise concludes that "'objective intent' manifested by the use of prohibited means should be sufficient to satisfy the intent component of attempt to monopolize"[18] and that "consciousness of wrong-doing is not itself important, except insofar as it (1) bears on the appraisal of ambiguous conduct or (2) limits the reach of the offense by those courts that improperly undervalue the power component of the attempt offense."[19]

The "dangerous probability" inquiry requires consideration of "the relevant market and the defendant's ability to lessen or destroy

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[8] 15 U.S.C. § 2 (2000).

[9] Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 456 (1993).

[10] Lorain Journal Co. v. United States, 342 U.S. 143, 153 (1951).

[11] *Spectrum Sports*, 506 U.S. at 455 (quoting Swift & Co. v. United States, 196 U.S. 375, 396 (1905)).

[12] *See* SECTION OF ANTITRUST LAW, *supra* note 2, at 307 ("The same principles used in the monopolization context to distinguish aggressive competition from anticompetitive exclusion thus apply in attempt cases.").

[13] Olympia Equip. Leasing Co. v. W. Union Tel. Co., 797 F.2d 370, 373 (7th Cir. 1986) (Posner, J.) (citing 3 PHILLIP E. AREEDA & DONALD F. TURNER, ANTITRUST LAW ¶ 828a (1978)).

[14] United States v. Dentsply Int'l, Inc., 399 F.3d 181, 187 (3d Cir. 2005) ("Behavior that otherwise might comply with antitrust law may be impermissibly exclusionary when practiced by a monopolist."); 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 806e (2d ed. 2002).

[15] *Spectrum Sports*, 506 U.S. at 459; *see also* AREEDA & HOVENKAMP, *supra* note 14, ¶ 805b1, at 340 ("There is at least one kind of intent that the proscribed 'specific intent' clearly cannot include: the mere intention to prevail over one's rivals. To declare that intention unlawful would defeat the antitrust goal of encouraging competition . . . which is heavily motivated by such an intent." (footnote omitted)).

[16] Times-Picayune Publ'g Co. v. United States, 345 U.S. 594, 626 (1953).

[17] *See, e.g.*, A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1402 (7th Cir. 1989) (Easterbrook, J.) ("Intent does not help to separate competition from attempted monopolization and invites juries to penalize hard competition. . . . Stripping intent away brings the real economic questions to the fore at the same time as it streamlines antitrust litigation.").

[18] AREEDA & HOVENKAMP, *supra* note 14, ¶ 805b2, at 342.

[19] *Id.* ¶ 805a, at 339–40.

competition in that market."[20] In making these assessments, lower courts have relied on the same factors used to ascertain whether a defendant charged with monopolization has monopoly power,[21] while recognizing that a lesser quantum of market power can suffice.[22]

## II. The Purpose of Section 2 and Its Important Role in Sound Antitrust Enforcement

The statutory language of section 2 is terse. Its framers left the statute's centerpiece—what it means to "monopolize"—undefined, and the statutory language offers no further guidance in identifying prohibited conduct.[23] Instead, Congress gave the Act "a generality and adaptability comparable to that found to be desirable in constitutional provisions"[24] and "expected the courts to give shape to the statute's broad mandate by drawing on the common-law tradition"[25] in furtherance of the underlying statutory goals.

Section 2 serves the same fundamental purpose as the other core provisions of U.S. antitrust law: promoting a market-based economy that increases economic growth and maximizes the wealth and prosperity of our society. As the Supreme Court has explained:

> The Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade. It rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress . . . .[26]

Section 2 achieves this end by prohibiting conduct that results in the acquisition or maintenance of monopoly power, thereby preserving a competitive environment that gives firms incentives to spur economic growth. Competition spurs companies to reduce costs, improve the quality of their products, invent new products, educate consumers, and engage in a wide range of other activity that benefits consumer welfare. It is the process by which more efficient firms win out and society's limited resources are allocated as efficiently as possible.[27]

Section 2 also advances its core purpose by ensuring that it does not prohibit aggressive competition. Competition is an inherently dynamic process. It works because firms strive to attract sales by innovating and otherwise seeking to please consumers, even if that means rivals will be less successful or never materialize at all. Failure—in the form of lost sales, reduced profits, and even going out of business—is a natural and indeed essential part of this competitive process. "Competition is a

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[20] *Spectrum Sports*, 506 U.S. at 456.

[21] *See, e.g.*, United States v. Microsoft Corp., 253 F.3d 34, 81 (D.C. Cir. 2001) (en banc) (per curiam) ("Defining a market for an attempted monopolization claim involves the same steps as defining a market for a monopoly maintenance claim . . . ."); SECTION OF ANTITRUST LAW, *supra* note 2, at 312–17 (cataloging factors considered by courts, including, most importantly, market share and barriers to entry).

[22] *See, e.g.*, Rebel Oil Co. v. Atl. Richfield Co., 51 F.3d 1421, 1438 (9th Cir. 1995) ("[T]he minimum showing of market share required in an attempt case is a lower quantum than the minimum showing required in an actual monopolization case."); SECTION OF ANTITRUST LAW, *supra* note 2, at 312.

[23] 15 U.S.C. § 2 (2000); *see also* 3 AREEDA & HOVENKAMP, *supra* note 14, ¶ 632, at 49 ("[T]he question whether judicial intervention under §2 requires more than monopoly is not answered by the words of the statute."); ROBERT H. BORK, THE ANTITRUST PARADOX 57 (1978) ("The bare language of the Sherman Act conveys little . . . ."); Frank H. Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 ANTITRUST L.J. 135, 136 (1984) ("The language of the Sherman Act governs no real cases."); Thomas E. Kauper, *Section Two of the Sherman Act: The Search for Standards*, 93 GEO. L.J. 1623, 1623 (2005) ("Over its 114-year history, Section Two of the Sherman Act has been a source of puzzlement to lawyers, judges and scholars, a puzzlement derived in large part from the statute's extraordinary brevity." (footnote omitted)).

[24] Appalachian Coals, Inc. v. United States, 288 U.S. 344, 360 (1933).

[25] Nat'l Soc'y of Prof'l Eng'rs v. United States, 435 U.S. 679, 688 (1978).

[26] N. Pac Ry. Co. v. United States, 356 U.S. 1, 4 (1958).

[27] *See* 2B PHILLIP E. AREEDA ET AL., ANTITRUST LAW ¶ 402 (3d ed. 2007). *See generally* WILLIAM W. LEWIS, THE POWER OF PRODUCTIVITY: WEALTH, POVERTY, AND THE THREAT TO GLOBAL STABILITY 13–14 (2004).

ruthless process. A firm that reduces cost and expands sales injures rivals—sometimes fatally."[28] While it may be tempting to try to protect competitors, such a policy would be antithetical to the free-market competitive process on which we depend for prosperity and growth.

Likewise, although monopoly has long been recognized as having the harmful effects of higher prices, curtailed output, lowered quality, and reduced innovation,[29] it can also be the outcome of the very competitive striving we prize. "[A]n efficient firm may capture unsatisfied customers from an inefficient rival," and this "is precisely the sort of competition that promotes the consumer interests that the Sherman Act aims to foster."[30] Indeed, as courts and enforcers have in recent years come to better appreciate, the prospect of monopoly profits may well be what "attracts 'business acumen' in the first place; it induces risk taking that produces innovation and economic growth."[31] Competition is ill-served by insisting that firms pull their competitive punches so as to avoid the degree of marketplace success that gives them monopoly power or by demanding that winning firms, once they achieve such power, "lie down and play dead."[32]

Section 2 thus aims neither to eradicate monopoly itself, nor to prevent firms from exercising the monopoly power their legitimate success has generated, but rather to protect the process of competition that spurs firms to succeed. The law encourages all firms—monopolists and challengers alike—to continue striving. It does this by preventing firms from achieving monopoly, or taking steps to entrench their existing monopoly power, through means incompatible with the competitive process.

## III. Principles that Have Guided the Evolution of Section 2 Standards and Enforcement

The history of section 2 reflects an ongoing quest to align the statute's application with the underlying goals of the antitrust laws. Consistent with the law's common-law character, courts have interpreted the Sherman Act's broad mandate differently over time and have revisited particular section 2 rules in response to advances in economic learning, changes in the U.S. economy, and experience with the application of section 2 to real-world conduct. Today, a consensus—as reflected in both judicial decisions[33] and the views of a broad cross-section of commentators—exists on at least seven core principles regarding section 2, each of which is discussed in the sections that follow:

- Unilateral conduct is outside the purview of section 2 unless the actor possesses

[28] Ball Mem'l Hosp., Inc. v. Mut. Hosp. Ins., Inc., 784 F.2d 1325, 1338 (7th Cir. 1986) (Easterbrook, J.).

[29] *See, e.g.*, Standard Oil Co. of N.J. v. United States, 221 U.S. 1, 52 (1911) (citing the danger that a monopoly will "fix the price," impose a "limitation on production," or cause a "deterioration in quality of the monopolized article"); Sherman Act Section 2 Joint Hearing: Empirical Perspectives Session Hr'g Tr. 13, Sept. 26, 2006 [hereinafter Sept. 26 Hr'g Tr.] (Scherer) (observing that reluctance to "cannibalize the rents that they are earning on the products that they already have marketed" may make monopolists "sluggish innovators"); Sherman Act Section 2 Joint Hearing: Welcome and Overview of Hearings Hr'g Tr. 25, June 20, 2006 [hereinafter June 20 Hr'g Tr.] (Barnett) (identifying as "a major harm of monopoly" the possibility that a monopolist may not feel pressure to innovate).

[30] Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 767 (1984).

[31] Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004); *see also* June 20 Hr'g Tr., *supra* note 29, at 25–27 (Barnett).

[32] Goldwasser v. Ameritech Corp., 222 F.3d 390, 397 (7th Cir. 2000).

[33] Underscoring the degree of consensus on many antitrust matters today, the Justices of the Supreme Court have shown remarkable agreement in recent antitrust matters. The aggregate voting totals for the twelve antitrust cases decided over the past decade show ninety-one votes in favor of the judgment and only thirteen in dissent. Even more striking, and directly relevant to this report, all three cases addressing claims under section 2 were decided without dissent. *See* Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 127 S. Ct. 1069 (2007); *Trinko*, 540 U.S. 398; NYNEX Corp. v. Discon, Inc., 525 U.S. 128 (1998).

monopoly power or is likely to achieve it.

- The mere possession or exercise of monopoly power is not an offense; the law addresses only the anticompetitive acquisition or maintenance of such power (and certain related attempts).
- Acquiring or maintaining monopoly power through assaults on the competitive process harms consumers and is to be condemned.
- Mere harm to competitors—without harm to the competitive process—does not violate section 2.
- Competitive and exclusionary conduct can look alike—indeed, the same conduct can have both beneficial and exclusionary effects—making it hard to distinguish conduct that should be deemed unlawful from conduct that should not.
- Because competitive and exclusionary conduct often look alike, courts and enforcers need to be concerned with both underdeterrence and overdeterrence.
- Standards for applying section 2 should take into account the costs, including error and administrative costs, associated with courts and enforcers applying those standards in individual cases and businesses applying them in their own day-to-day decision making.

**A. The Monopoly-Power Requirement**

Section 2's unilateral-conduct provisions apply only to firms that already possess monopoly power or have a dangerous probability of achieving monopoly power. This core requirement's importance as a basic building block of section 2 application to unilateral conduct should not be overlooked. Among other things, this requirement ensures that conduct within the statute's scope poses some realistic threat to the competitive process, and it also provides certainty to firms that lack monopoly power (or any realistic likelihood of attaining it) that they need not constrain their vigorous and creative unilateral-business strategies out of fear of section 2 liability.[34]

As the Supreme Court explained in its 1984 *Copperweld* decision, because "robust competition" and "conduct with long-run anti-competitive effects" may be difficult to distinguish in the single-firm context, Congress had authorized "scrutiny of single firms" only where they "pose[d] a danger of monopolization."[35] The application of the monopoly-power requirement is discussed in detail in chapter 2 of the report.

**B. The Anticompetitive-Conduct Requirement**

Section 2 prohibits acquiring or maintaining (and in some cases attempting to acquire) monopoly power only through improper means.[36] As long as a firm utilizes only lawful means, it is free to strive for competitive success and reap the benefits of whatever market position (including monopoly) that success brings, including charging whatever price the market will bear. Prohibiting the mere possession of monopoly power is inconsistent with harnessing the competitive process to achieve economic growth.

Nearly a century ago, in *Standard Oil*, one of the Supreme Court's first monopolization cases, the Court observed that the Act does not include "any direct prohibition against monopoly in the concrete."[37] The Court thus rejected the United States's assertion that section 2 bars the attainment of monopoly or monopoly power regardless of the means and instead held that without unlawful conduct, mere "size, aggregated capital, power and volume of business are not monopolizing in a legal sense."[38]

*United States v. Aluminum Co. of America* re-emphasized *Standard Oil*'s distinction between the mere possession of monopoly and unlawful

[34] *See* John Vickers, *Market Power in Competition Cases*, 2 EUR. COMPETITION J. 3, 12 (2006).

[35] 467 U.S. at 768.

[36] *See* Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 456 (1993); United States v. Grinnell, 384 U.S. 563, 570–71 (1966).

[37] 221 U.S. 1, 62 (1911).

[38] *Id.* at 10; *see also id.* at 62.

monopolization as a key analytical concept.[39] Writing for the Second Circuit, Judge Hand reasoned that, simply because Alcoa had a monopoly in the market for ingot, it did "not follow" that "it [had] 'monopolized'" the market: "[I]t may not have achieved monopoly; monopoly may have been thrust upon it."[40] The court determined that mere "size does not determine guilt" under section 2 and that monopoly can result from causes that are not unlawful, such as "by force of accident" or where a market is so limited it can profitably accommodate only one firm.[41] Further, the court observed that monopoly can result from conduct that clearly is within the spirit of the antitrust laws. Where "[a] single producer may be the survivor out of a group of active competitors, merely by virtue of his superior skill, foresight and industry," punishment of that producer would run counter to the spirit of the antitrust laws: "The successful competitor, having been urged to compete, must not be turned upon when he wins."[42]

Twenty years after *Alcoa*, and more than fifty years after *Standard Oil*, the Supreme Court articulated in *Grinnell*[43] what remains the classic formulation of the section 2 prohibition. Drawing from *Alcoa*, the Court condemned "the willful acquisition or maintenance of [monopoly] power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident."[44]

### C. Assaults on the Competitive Process Should Be Condemned

Competition has long stood as the touchstone of the Sherman Act. "The law," the Supreme Court has emphasized, "directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself."[45] The Sherman Act rests on "a legislative judgment that ultimately competition will produce not only lower prices, but also better goods and services."[46] Section 2 stands as a vital safeguard of that competitive process. As Assistant Attorney General Thomas O. Barnett emphasized at the commencement of the hearings, "individual firms with . . . monopoly power can act anticompetitively and harm consumer welfare."[47] Firms with ill-gotten monopoly power can inflict on consumers higher prices, reduced output, and poorer quality goods or services.[48] Additionally, in certain circumstances, the existence of a monopoly can stymie innovation.[49] Section 2 enforcement saves

[39] 148 F.2d 416 (2d Cir. 1945) (Hand, J.).

[40] *Id.* at 429.

[41] *Id.* at 429–30.

[42] *Id.* at 430.

[43] 384 U.S. 563 (1966).

[44] *Id.* at 571.

[45] Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993).

[46] Nat'l Soc'y of Prof'l Eng'rs v. United States, 435 U.S. 679, 695 (1978). As an important corollary, it is now generally accepted that section 2 may not be enforced to achieve other ends, such as the protection of certain kinds of enterprises or the furtherance of environmental, social, or other interests. *See generally* RICHARD A. POSNER, ANTITRUST LAW vii–x (2d ed. 2001). That is not to say that these other interests are not important—they are—but they should be addressed through other tools, not the antitrust laws.

[47] June 20 Hr'g Tr., *supra* note 29, at 35 (Barnett); *see also id.* at 9 (Majoras) (stressing that "private actors can and do distort competition" and that "halting conduct that goes beyond aggressive competition to distorting it is vital to promoting vigorous competition and maximizing consumer welfare").

[48] *See, e.g.*, DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 94–99 (4th ed. 2005); POSNER, *supra* note 46, at 9–32; Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 ANTITRUST L.J. 3, 33 (2004).

[49] *See, e.g.*, Sept. 26 Hr'g Tr., *supra* note 29, at 13 (Scherer) (stating that "firms in dominant positions are almost surely sluggish innovators"); Sherman Act Section 2 Joint Hearing: Refusals to Deal Panel Hr'g Tr. 55, July 18, 2006 [hereinafter July 18 Hr'g Tr.] (Salop) ("Monopolists have weaker innovation incentives than competitors."); AREEDA ET AL., *supra* note 27, ¶ 407; Peter C. Carstensen, *False Positives in Identifying Liability for Exclusionary Conduct: Conceptual Error, Business Reality, and* Aspen, 2008 WIS. L. REV. 295, 306 (arguing that "a monopolist has no incentive to support technological innovation that could undermine its dominant position in the market" and "having sunk investments in existing technology, it may well delay or refuse to pursue work on new technology until it has accounted for its past investments"); *cf.* POSNER, *supra*

consumers from these harms by deterring or eliminating exclusionary conduct that produces or preserves monopoly.

A number of panelists stated that section 2 is essential to preserving competition.[50] They noted that the threat of anticompetitive conduct is real, "far from an isolated event" in the words of one.[51] Section 2 enforcement has played a vital role in U.S. antitrust enforcement for a century.[52] From the seminal case against Standard Oil in 1911,[53] through litigation resulting in the break-up of AT&T,[54] to the present-day enforcement in high-technology industries with the *Microsoft* case,[55] government enforcement of section 2 has benefitted U.S. consumers. Private cases brought under section 2 by injured parties are also important to U.S. businesses and consumers. Equally important, the potential for significant injunctive relief and damages awards provides strong incentives for firms to refrain from engaging in the types of conduct prohibited by the statute.

### D. Protection of Competition, Not Competitors

The focus on protecting the competitive process has special significance in distinguishing between lawful and unlawful unilateral conduct. Competition produces injuries; an enterprising firm may negatively affect rivals' profits or drive them out of business. But competition also benefits consumers by spurring price reductions, better quality, and innovation. Accordingly, mere harm to competitors is not a basis for antitrust liability. "The purpose of the [Sherman] Act," the Supreme Court instructs, "is not to protect businesses from the working of the market; it is to protect the public from the failure of the market."[56] Thus, preserving the rough-and-tumble of the marketplace ultimately "promotes the consumer interests that the Sherman Act aims to foster."[57]

The Supreme Court has underscored this basic principle repeatedly over the past several decades. In 1984, it observed in *Copperweld* that the type of "robust competition" encouraged by the Sherman Act could very well lead to injury to individual competitors.[58] Accordingly, the Court stated that, without more (i.e., injury to competition), mere injury to a competitor is not in itself unlawful under the Act.[59] In so stating, the Court cited its 1977 decision in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.* for the proposition that the antitrust laws "were enacted for 'the protection of *competition*, not *competitors*.'"[60]

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note 46, at 20 (explaining that "it is an empirical question whether monopoly retards or advances innovation").

[50] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Business Testimony Hr'g Tr. 12, Feb. 13, 2007 [hereinafter Feb. 13 Hr'g Tr.] (Balto) ("Antitrust enforcement in the generic drug industry is essential."); Sherman Act Section 2 Joint Hearing: Business Testimony Hr'g Tr. 133, Jan. 30, 2007 [hereinafter Jan. 30 Hr'g Tr.] (Haglund) ("The application of Section 2 to [regional forest product, fishing, and agricultural] markets is important . . . ."); *id.* at 159–60 (Dull) ("The antitrust laws have an important role in policing the conduct of firms who would seek to take control of those interconnections so as to eliminate competition and thus harm consumers.").

[51] Feb. 13 Hr'g Tr., *supra* note 50, at 58 (Skitol); *see also* Jan. 30 Hr'g Tr., *supra* note 50, at 158 (Dull) ("Obtaining control of key interfaces through anticompetitive means, or using control of key interfaces to extend a dominant position in one market into other markets, is a real danger in our industry.").

[52] Other provisions of the antitrust laws can play a role in preventing the formation or preservation of monopoly, as when section 7 of the Clayton Act is enforced against mergers to monopoly, or section 1 of the Sherman Act is enforced against certain market-allocation agreements. But section 2 uniquely allows antitrust enforcers to reach conduct engaged in unilaterally by a firm that has achieved, or dangerously threatens to achieve, monopoly power.

[53] 221 U.S. 1 (1911).

[54] United States v. AT&T, 552 F. Supp. 131 (D.D.C. 1982), *aff'd mem. sub nom.* Maryland v. United States, 460 U.S. 1001 (1983).

[55] United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001) (en banc) (per curiam).

[56] Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458 (1993).

[57] Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 767 (1984).

[58] *Id.* at 758.

[59] *See id.* at 767–68.

[60] *Id.* at 767 n.14 (quoting Brunswick Corp. v. Pueblo

A year after *Copperweld*, in a decision that it subsequently referred to as being "at or near the outer boundary of § 2 liability,"[61] the Court, in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, found that a firm operating three of four mountain ski areas in Aspen, Colorado, violated section 2 by refusing to continue cooperating with a smaller rival in offering a combined four-area ski pass.[62] The Court considered the challenged conduct's "impact on consumers and whether it [had] impaired competition in an unnecessarily restrictive way."[63]

In a 1993 decision, the Court re-emphasized the importance of focusing on competition, rather than competitors. In *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, the Court commented on the elements of a predatory-pricing claim, noting that, even where facts "indicate that below-cost pricing could likely produce its intended effect on the target, there is still the further question whether it would likely injure competition in the relevant market."[64] In particular, the *Brooke Group* recoupment requirement was a logical outgrowth of the Court's concern with protecting competition, not competitors. Absent the possibility of recoupment through supracompetitive pricing, there can be no injury to competition: "That below-cost pricing may impose painful losses on its target is of no moment to the antitrust laws if competition is not injured."[65]

Again, in its 1998 decision in *NYNEX*, the Court reaffirmed that Sherman Act liability requires harm to the competitive process, not simply a competitor.[66] Discon alleged that NYNEX and related entities had violated the Sherman Act by engaging in an unlawful fraudulent scheme that injured Discon and benefitted one of Discon's competitors. While conceding that NYNEX's scheme "hurt consumers by raising telephone service rates," the Court found that any consumer injury "naturally flowed not so much from a less competitive market" for certain services as from "the exercise of market power that is *lawfully* in the hands of a monopolist . . . combined with a deception worked upon the regulatory agency that prevented the agency" from controlling that exercise of monopoly power.[67] The Court explained that a Sherman Act "plaintiff . . . must allege and prove harm, not just to a single competitor, but to the competitive process, *i.e.*, to competition itself."[68]

### E. Distinguishing Competitive and Exclusionary Conduct Is Often Difficult

Courts and commentators have long recognized the difficulty of determining what means of acquiring and maintaining monopoly power should be prohibited as improper. Although many different kinds of conduct have been found to violate section 2, "[d]efining the contours of this element . . . has been one of the most vexing questions in antitrust law."[69] As

Bowl-O-Mat, Inc., 429 U.S. 477, 488 (1977) (quoting Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962))) (emphasis in original).

[61] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 409 (2004).

[62] 472 U.S. 585, 606, 610 (1985).

[63] *Id.* at 605; *see also id.* at 605 n.32 ("'[E]xclusionary' comprehends at the most behavior that not only (1) tends to impair the opportunities of rivals, but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way." (quoting AREEDA & TURNER, *supra* note 13, ¶ 626b, at 78)). The Court found that the evidence supported the jury's finding that "consumers were adversely affected by the elimination" of the four-area ski pass. 472 U.S. at 606.

[64] 509 U.S. 209, 225 (1993).

[65] *Id.* at 224.

[66] 525 U.S. 128, 139 (1998). While the Court focused its analysis on the section 1 claim, it stated that the section 2 claim in the case could not survive unless the challenged conduct harmed the competitive process. *Id.* at 139–40.

[67] *Id.* at 136 (emphasis in original).

[68] *Id.* at 135.

[69] SECTION OF ANTITRUST LAW, *supra* note 2, at 241; *see also* United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001) (en banc) (per curiam) ("Whether any particular act of a monopolist is exclusionary, rather than merely a form of vigorous competition, can be difficult to discern: the means of illicit exclusion, like the means of legitimate competition, are myriad. The challenge for an antitrust court lies in stating a general rule for distinguishing between exclusionary acts, which reduce social welfare, and competitive acts, which increase it."); ANTITRUST MODERNIZATION

Judge Easterbrook observes, "Aggressive, competitive conduct by any firm, even one with market power, is beneficial to consumers. Courts should prize and encourage it. Aggressive, exclusionary conduct is deleterious to consumers, and courts should condemn it. The big problem lies in this: competitive and exclusionary conduct look alike."[70]

The problem is not simply one that demands drawing fine lines separating different categories of conduct; often the *same conduct* can both generate efficiencies and exclude competitors.[71] Judicial experience and advances in economic thinking have demonstrated the potential procompetitive benefits of a wide variety of practices that were once viewed with suspicion when engaged in by firms with substantial market power. Exclusive dealing, for example, may be used to encourage beneficial investment by the parties while also making it more difficult for competitors to distribute their products.[72]

When a competitor achieves or maintains monopoly power through conduct that serves no purpose other than to exclude competition, such conduct is clearly improper. There also are examples of conduct that is clearly legitimate, as when a firm introduces a new product that is simply better than its competitors' offerings. The hard cases arise when conduct enhances economic efficiency or reflects the kind of dynamic and disruptive change that is the hallmark of competition, but at the same time excludes competitors through means other than simply attracting consumers. In these situations, distinguishing between vigorous competition by a firm with substantial market power and illegitimate forms of conduct is one of the most challenging puzzles for courts, enforcers, and antitrust practitioners.

### F. Concern with Underdeterrence and Overdeterrence

Experience with section 2 enforcement teaches the importance of correctly distinguishing between aggressive competition and actions that exclude rivals and harm the competitive process. Some basic boundaries are provided by the law's requirements that the conduct harm "competition itself,"[73] that it be

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COMM'N, REPORT AND RECOMMENDATIONS 81 (2007), *available at* http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf ("How to evaluate single-firm conduct under Section 2 poses among the most difficult questions in antitrust law."); Sherman Act Section 2 Joint Hearing: Loyalty Discounts Session Hr'g Tr. 110, Nov. 29, 2006 (Muris) (stating that "the scope and meaning of exclusionary behavior remains . . . very poorly defined"); July 18 Hr'g Tr., *supra* note 49, at 21 (Pitofsky) (identifying "the definition of exclusion under Section 2 . . . as about the toughest issue[] that an antitrust lawyer is required to face today"); June 20 Hr'g Tr., *supra* note 29, at 12 (Majoras) ("[I]t is difficult to distinguish between aggressive procompetitive unilateral conduct and anticompetitive unilateral conduct."); Susan A. Creighton et al., *Cheap Exclusion*, 72 ANTITRUST L.J. 975, 978 (2005) ("Much of the 'long, and often sorry, history of monopolization in the courts' has been devoted to attempting to provide an answer to the question at the center of the Supreme Court's formulation—that is, when is monopolizing conduct 'anticompetitive.'" (footnote omitted)); Timothy J. Muris, *The FTC and the Law of Monopolization*, 67 ANTITRUST L.J. 693, 695 (2000) ("Much of the monopolization case law struggles with the question of when conduct is, or is not, exclusionary."); Mark S. Popofsky, *Defining Exclusionary Conduct: Section 2, the Rule of Reason, and the Unifying Principle Underlying Antitrust Rules*, 73 ANTITRUST L.J. 435, 438 (2006) ("Over a century since the Sherman Act's passage, and some forty years since the Supreme Court held that Section 2 condemns the 'willful' acquisition or maintenance of monopoly power, great uncertainty persists as to the test for liability under Section 2 of the Sherman Act." (footnote omitted)).

[70] Frank H. Easterbrook, *When Is It Worthwhile to Use Courts to Search for Exclusionary Conduct?*, 2003 COLUM. BUS. L. REV. 345, 345.

[71] June 20 Hr'g Tr., *supra* note 29, at 17 (Majoras); *see also* Sept. 26 Hr'g Tr., *supra* note 29, at 20 (Froeb) ("[M]echanisms with opposing effects usually appear in a single kind of behavior."); June 20 Hr'g Tr., *supra* note 29, at 29 (Barnett) ("The difficulty lies in cases . . . that have the potential for both beneficial cost reductions, innovation, development, integration, and at the same time potentially anticompetitive exclusion."); A. Douglas Melamed, *Exclusionary Conduct Under the Antitrust Laws: Balancing, Sacrifice, and Refusals to Deal*, 20 BERKELEY TECH. L.J. 1247, 1249 (2005) ("In the vast majority of cases, exclusion is the result of conduct that has both efficiency properties and the tendency to exclude rivals.").

[72] *See generally* Benjamin Klein, *Exclusive Dealing as Competition for Distribution "On the Merits,"* 12 GEO. MASON L. REV. 119 (2003); *infra* Chapter 8, Part III.

[73] Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447,

"willful,"[74] and that it not be "competition on the merits,"[75] but these maxims offer insufficient guidance to be of much use in many of the hard cases.[76] Failure to make proper distinctions will either unnecessarily perpetuate a monopoly harming consumers or disrupt the dynamic process of competition that is so vital to economic growth and prosperity.

**It is important to distinguish correctly between aggressive competition and actions that exclude rivals and harm the competitive process.**

Standards of section 2 liability that underdeter not only shelter a single firm's exclusionary conduct, but also "empower other dominant firms to adopt the same strategy."[77] They thereby "seriously undermine Section 2's vitality as a shield that guards the competitive process."[78] And "because it can be so difficult for courts to restore competition once it has been lost, the true cost of exclusion to consumer welfare—and its benefit to dominant firms—are likely to be understated."[79]

Standards of section 2 liability that overdeter risk harmful disruption to the dynamic competitive process itself. Being able to reap the gains from a monopoly position attained through a hard-fought competitive battle, or to maintain that position through continued competitive vigor, may be crucial to motivating the firm to innovate in the first place. Rules that overdeter, therefore, undermine the incentive structure that competitive markets rely upon to produce innovation.[80] Such rules also may sacrifice the efficiency benefits associated with the competitive behavior.

Importantly, rules that are overinclusive or unclear will sacrifice those benefits not only in markets in which enforcers or courts impose liability erroneously, but in other markets as well. Firms with substantial market power typically attempt to structure their affairs so as to avoid either section 2 liability or even having to litigate a section 2 case because the costs associated with antitrust litigation can be extraordinarily large. These firms must base their business decisions on their understanding of the legal standards governing section 2, determining in advance whether a proposed course of action leaves their business open to antitrust liability or investigation and litigation. If the lines are in the wrong place, or if there is uncertainty about where those lines are, firms will pull their competitive punches unnecessarily, thereby depriving consumers of the benefits of their efforts.[81] The Supreme

459 (1993).

[74] United States v. Grinnell Corp., 384 U.S. 563, 570 (1966).

[75] Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 223 (1993).

[76] As commentators note, for example, the *Grinnell* standard provides little concrete guidance, either to the lower courts or to businesses attempting to conform their conduct to the requirements of section 2, because virtually all conduct—both "good" and "bad"—is undertaken "willfully." *See, e.g.*, SECTION OF ANTITRUST LAW, *supra* note 2, at 242 ("Courts have not been able to agree, however, on any general standard beyond the highly abstract *Grinnell* language, which has been criticized as not helpful in deciding concrete cases."); Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 261 (2003) (noting that the *Grinnell* standard is difficult to apply because "[i]t seems obvious that often firms willfully acquire or maintain monopoly power precisely through business acumen or developing a superior product" and it is difficult to conceive "of cases where a firm really has a monopoly thrust upon it without the aid of any willful conduct").

[77] Carstensen, *supra* note 49, at 321.

[78] Gavil, *supra* note 48, at 5.

[79] *Id.* at 39.

[80] *See* Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407–08 (2004).

[81] *See, e.g.*, Jan. 30 Hr'g Tr., *supra* note 50, at 36 (Heiner) ("[T]here have been cases . . . where decisions were made not to include particular features that would have been valuable to consumers based at least in part on antitrust advice."); *id.* at 95 (Hartogs) (identifying a risk that a lack of clear rules on loyalty discounts and bundled pricing may cause firms not "to always choose what may be the most price friendly, consumer friendly result"); *id.* at 96 (Skitol) ("There are lots of situations I find where a client has in mind doing X, Y, Z with its consumables, which would be of significant consumer value, would enhance the product, and it looks great. But because of *Kodak* and all of the law that's built up

Court has consistently emphasized the potential dangers of overdeterrence. The Court's concern about overly inclusive or unclear legal standards may well be driven in significant part by the particularly strong chilling effect created by the specter of treble damages and class-action cases.[82] Many hearing panelists reiterated this concern.[83]

### G. The Importance of Administrability when Crafting Liability Standards Under Section 2

Courts and commentators increasingly have recognized that section 2 standards cannot "embody every economic complexity and qualification"[84] and have sought to craft legal tests that account for these limitations. Then-Judge Breyer explained the need for simplifying rules more than two decades ago:

> [W]hile technical economic discussion helps to inform the antitrust laws, those laws cannot precisely replicate the economists' (sometimes conflicting) views. For, unlike economics, law 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. Rules 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.[85]

Frequently, courts and commentators dealing with antitrust have employed decision theory,[86] which articulates a process for

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around it, this is problematic . . . .").

[82] *See* Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 728 (1988) (expressing concern regarding a rule that likely would cause manufacturers "to forgo legitimate and competitively useful conduct rather than risk treble damages and perhaps even criminal penalties"); *Roundtable Discussion: Antitrust and the Roberts Court*, ANTITRUST, Fall 2007, at 8, 11 (roundtable participant stating that "the Court continues to endorse arguments made by the government and by defendants that treble-damages over-incentivize antitrust cases"). *See generally Trinko*, 540 U.S. at 414 ("The cost of false positives counsels against an undue expansion of § 2 liability."); Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 456 (1993); *id.* at 458 (stating that "this Court and other courts have been careful to avoid constructions of § 2 which might chill competition, rather than foster it"); Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 594 (1986) (stating that mistaken inferences in predatory-pricing cases "are especially costly because they chill the very conduct the antitrust laws are designed to protect"); Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 767–68 (1984) (noting that scrutiny of single firms under the Sherman Act is appropriate only when they pose a danger of monopolization, an approach that "reduces the risk that the antitrust laws will dampen the competitive zeal of a single aggressive [competitor]"); William E. Kovacic, *The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Conduct: The Chicago/Harvard Double Helix*, 2007 COLUM. BUS. L. REV. 1, 21 (noting the "wariness of rules that might discourage dominant firms" from "strategies that generally serve to improve consumer welfare" resulting from a "fear that overly restrictive rules will induce a harmful passivity").

[83] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Section 2 Policy Issues Hr'g Tr. 45, May 1, 2007 [hereinafter May 1 Hr'g Tr.] (Willig); *id.* at 46 (Jacobson); Feb. 13 Hr'g Tr., *supra* note 50, at 168 (Wark) ("Given the punitive nature of the antitrust laws and the inevitability of private class action litigation, including the prospect of treble damages, defending ourselves in that situation, irrespective of the courage of our convictions, is high-stakes poker indeed."). Moreover, competitors have incentives to use the antitrust laws to impede their rivals. *See* Sherman Act Section 2 Joint Hearing: Misleading and Deceptive Conduct Session Hr'g Tr. 25–28, Dec. 6, 2006 (McAfee) (contending that, among other reasons, private parties bring antitrust claims to "extort[] funds from a successful rival," "chang[e] the terms of a contract," "punish noncooperative behavior," "respond[] to an existing lawsuit," "prevent[] a hostile takeover," and prevent entry); 2 AREEDA ET AL., *supra* note 27, ¶ 348a, at 387 (2d ed. 2000) (cautioning that "a competitor opposes efficient, aggressive, and legitimate competition by its rivals [and therefore] has an incentive to use an antitrust suit to delay their operations or to induce them to moderate their competition").

[84] Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 234 (1st Cir. 1983) (Breyer, J.); *see also* Kovacic, *supra* note 82, at 36 (noting that both the Chicago and Harvard schools have insisted "that courts and enforcement agencies pay close attention to considerations of institutional design and institutional capacity in formulating and applying antitrust rules").

[85] *Barry Wright*, 724 F.2d at 234.

[86] *See, e.g.*, POSNER, *supra* note 46, at ix (observing that "[a]lmost everyone professionally involved in antitrust today" agrees that "the design of antitrust rules should take into account the costs and benefits of

making decisions when information is costly and imperfect.[87] Decision theory teaches that optimal legal standards should minimize the inevitable error and enforcement costs, considering both the probability and the magnitude of harm from each.[88]

Decision theory identifies two types of error costs. First, there are "false positives" (or Type I errors), meaning the wrongful condemnation of conduct that benefits competition and consumers. The cost of false positives includes not just the costs associated with the parties before the court (or agency), but also the loss of procompetitive conduct by other actors that, due to an overly inclusive or vague decision, are deterred from undertaking such conduct by a fear of litigation.[89]

Second, there are "false negatives" (or Type II errors), meaning the mistaken exoneration of conduct that harms competition and consumers. As with false positives, the cost of false negatives includes not just the failure to condemn a particular defendant's anti-competitive conduct but also the loss to competition and consumers inflicted by other firms' anticompetitive conduct that is not deterred.[90]

It also is important to consider enforcement costs—the expenses of investigating and litigating section 2 claims (including potential claims)—when framing legal tests. Because agency resources are finite, it is important to exercise enforcement discretion to best promote consumer welfare. Enforcement costs include the judicial or agency resources devoted to antitrust litigation, the expenses of parties in litigation (including time spent by management and employees on the litigation as opposed to producing products or services), and the legal fees and other expenses incurred by firms in complying with the law.[91]

In structuring a legal regime, it is important to consider the practical consequences of the regime and the relative magnitude and frequency of the different types of errors. If, for example, the harm from erroneously exonerating anticompetitive conduct outweighs the harm from erroneously penalizing procompetitive conduct, then, all other things

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individual assessment of challenged practices"); Gavil, *supra* note 48, at 66 ("It is rare today in cases where fundamental questions are raised about the 'right standard' that the parties and courts do not assess the[] issues" raised by decision theory.).

[87] *See* C. Frederick Beckner III & Steven C. Salop, *Decision Theory and Antitrust Rules*, 67 ANTITRUST L.J. 41, 41–42 (1999) (defining decision theory); Isaac Ehrlich & Richard A. Posner, *An Economic Analysis of Legal Rulemaking*, 3 J. LEGAL STUD. 257, 272 (1974) (applying a decision-theoretic approach to legal rulemaking generally).

[88] *See* Ken Heyer, *A World of Uncertainty: Economics and the Globalization of Antitrust*, 72 ANTITRUST L.J. 375, 381 (2005).

[89] *See* Feb. 13 Hr'g Tr., *supra* note 50, at 170 (Wark) (in-house counsel reporting that his client had altered its conduct "based not on what we thought was illegal, but on what we feared others might argue is illegal" and that "in these circumstances competition has likely been compromised"); June 20 Hr'g Tr., *supra* note 29, at 55 (Carlton) ("[T]he biggest effect of any antitrust policy is likely to be, not on litigants in litigated cases, but rather, on firms that are not involved in litigation at all but are forced to change their business behavior in contemplation of legal rules."); Dennis W. Carlton, *Does Antitrust Need to Be Modernized?*, J. ECON. PERSP., Summer 2007, at 155, 159–60 ("[T]he cost of errors must include not only the cost of mistakes on the firms involved in a particular case, but also the effect of setting a legal precedent that will cause other firms to adjust their behavior inefficiently."); *cf.* May 1 Hr'g Tr., *supra* note 83, at 86 (Jacobson) (stating that the "problem" of overdeterrence "is larger in the eyes of the enforcement community than it is in the real world.").

[90] *See, e.g.*, Gavil, *supra* note 48, at 5 (expressing concern that lax section 2 standards may "lead to 'false negatives' and under-deterrence, with uncertain, but very likely substantial adverse consequences for . . . nascent competition"); William Kolasky, *Reinvigorating Antitrust Enforcement in the United States: A Proposal*, ANTITRUST, Spring 2008, at 85, 86 (stating that "the risk of false positives is now much less serious than it was, thanks in large part to the Supreme Court's rulings over the last fifteen years," and that "if anything, we are now in greater danger of false negatives").

[91] *See* Feb. 13 Hr'g Tr., *supra* note 50, at 47 (Stern) ("It's important to help avoid inadvertent violations and disputes and investigations that end up wasting company time and resources as well as the time and resources of the agencies."); *id.* at 163 (Wark) (in-house counsel commenting that "it diverts a tremendous amount of management attention and company resources" to defend an antitrust lawsuit); Ehrlich & Posner, *supra* note 87, at 270.

equal, the legal regime should seek to avoid false negatives. Some believe as a general rule that, in the section 2 context, the cost of false positives is higher than the cost of false negatives.[92] In the common law regime of antitrust law, stare decisis inhibits courts from routinely correcting errors or updating the law to reflect the latest advances in economic thinking.[93] Some believe that the persistence of errors can be particularly harmful to competition in the case of false positives because "[i]f the court errs by condemning a beneficial practice, the benefits may be lost for good. Any other firm that uses the condemned practice faces sanctions in the name of stare decisis, no matter the benefits."[94] In contrast, over time "monopoly is self-destructive. Monopoly prices eventually attract entry. . . . [Thus] judicial errors that tolerate baleful practices are self-correcting, while erroneous condemnations are not."[95] This self-correcting tendency, however, may take substantial time. As a result, courts and enforcers should be sensitive to the potential that, once created, some monopolies may prove quite durable, especially if allowed to erect entry barriers and engage in other exclusionary conduct aimed at artificially prolonging their existence.[96]

One manifestation of decision theory in antitrust jurisprudence is the use of rules of per se illegality developed by courts. As the Supreme Court has explained, these rules reduce the administrative costs of determining whether particular categories of conduct harm competition and consumer welfare.[97] Per se prohibitions are justified when experience with conduct establishes that it is always or almost always sufficiently pernicious that it should be condemned without inquiry into its actual effects in each case.[98] Rules of per se illegality are not designed to achieve perfection; to the contrary, courts explicitly acknowledge the potential that they could from time to time penalize conduct that does not in fact harm consumer welfare, but the rule is nonetheless warranted so long as false positives are sufficiently rare and procompetitive benefits from conduct deterred by the rules are sufficiently small.

Equally important, if one or the other type of error is relatively rare (and that error is unlikely to result in great harm), the most effective approach to enforcement may be an easy-to-administer bright-line test that reduces uncertainty and minimizes administrative costs. In the antitrust arena, such rules can take the form of safe harbors. Court have long

[92] *See* Kovacic, *supra* note 82, at 36 ("Chicago School and Harvard School commentators tend to share the view that the social costs of enforcing antitrust rules involving dominant firm conduct too aggressively exceed the costs of enforcing them too weakly."); Sherman Act Section 2 Joint Hearing: Conduct as Related to Competition Hr'g Tr. 23, May 8, 2007 (Rule) (stating that "we as a society, given the way we are organized, should be very concerned about the adverse economic effects, the false positives").

[93] Although the Supreme Court has overturned several long-standing per se rules, *see, e.g.*, Leegin Creative Leather Prods., Inc. v. PSKS, Inc., 127 S. Ct. 2705 (2007) (overturning the per se rule against minimum resale price maintenance), it did so only after decades of criticism.

[94] Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1, 2 (1984); *see also* Thomas C. Arthur, *The Costly Quest for Perfect Competition:* Kodak *and Nonstructural Market Power*, 69 N.Y.U. L. REV. 1, 18 (1994) ("The principle of stare decisis makes obsolete doctrines hard to overrule, even after their economic underpinnings have been discredited. This has been especially true in antitrust."). *But see* May 1 Hr'g Tr., *supra* note 83, at 89 (Jacobson) (maintaining that false positives are more ephemeral than commonly suggested); *id.* (Krattenmaker) (same).

[95] Easterbrook, *supra* note 94, at 2–3.

[96] *See, e.g.*, May 1 Hr'g Tr., *supra* note 83, at 34–35 (Jacobson) (arguing that monopoly may prove enduring absent effective antitrust intervention); Gavil, *supra* note 48, at 39–41 (same).

[97] *See, e.g.*, Cont'l T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 50 n.16 (1977) (explaining that per se rules "minimize the burdens on litigants and the judicial system").

[98] *See* NYNEX Corp. v. Discon, Inc., 525 U.S. 128, 133 (1998) ("[C]ertain kinds of agreements will so often prove so harmful to competition and so rarely prove justified that the antitrust laws do not require proof that an agreement of that kind is, in fact, anticompetitive in the particular circumstances."); State Oil Co. v. Khan, 522 U.S. 3, 10 (1997) (Certain "types of restraints . . . have such predictable and pernicious anticompetitive effects, and such limited potential for procompetitive benefit, that they are deemed unlawful *per se*.").

recognized the benefits of bright-line tests of legality (also known as safe harbors) when conduct is highly likely to bring consumer-welfare benefits and the threat of anticompetitive harm is remote.[99] The best known example is the section 2 rule applicable to predatory pricing. Building on *Matsushita*,[100] the Court in *Brooke Group* laid out a two-pronged, objective test for evaluating predatory-pricing claims.[101] The Court held that to prevail on a predatory-pricing claim, plaintiff must show that defendant priced below an appropriate measure of its costs and that defendant "had a reasonable prospect, or . . . a dangerous probability, of recouping its investment in below-cost prices."[102] In *Weyerhaeuser*, the Court recently extended these principles to predatory-bidding claims.[103]

In *Matsushita, Brooke Group*, and *Weyerhaeuser*, the Court stressed the importance, in crafting a rule of decision, of taking into account the risks of false positives, the risks of false negatives, and administrability. The Court's 2004 decision in *Trinko* likewise applies decision-theory principles in crafting section 2 liability rules.[104] In reaching its decision, the Court articulated the same policy concerns with false positives that it had raised in previous section 2 cases. The Court observed that it had been "very cautious" in limiting "the right to refuse to deal with other firms" because enforced sharing "may lessen the incentive for the monopolist, the rival, or both to invest in . . . economically beneficial facilities" and obligates courts to identify "the proper price, quantity, and other terms of dealing—a role for which they are ill suited."[105] As the Court further explained:

> Against the slight benefits of antitrust intervention here, we must weigh a realistic assessment of its costs . . . . Mistaken inferences and the resulting false condemnations "are especially costly because they chill the very conduct the antitrust laws are designed to protect." The cost of false positives counsels against an undue expansion of § 2 liability.[106]

## IV. Conclusion

Section 2 enforcement is crucial to the U.S. economy. It is a vexing area, however, given that competitive conduct and exclusionary conduct often look alike. Indeed, the same exact conduct can have procompetitive and exclusionary effects. An efficient legal regime will consider the effects of false positives, false negatives, and the costs of administration in determining the standards to be applied to single-firm conduct under section 2.

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[99] As then-Judge Breyer explained, such rules conceivably may shelter some anticompetitive conduct, but they avoid "authoriz[ing] a search for a particular type of undesirable . . . behavior [that may] end up . . . discouraging legitimate . . . competition." Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 234 (1st Cir. 1983).

[100] 475 U.S. 574 (1986).

[101] 509 U.S. 209, 222, 224 (1993). *See generally infra* Chapter 4, Part I.

[102] *Id.* at 224.

[103] Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 127 S. Ct. 1069 (2007).

[104] 540 U.S. 398 (2004); *see also* Popofsky, *supra* note 69, at 452 (describing how the Supreme Court used decision theory to decide *Trinko*).

[105] 540 U.S. at 408.

[106] *Id.* at 414 (quoting Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 594 (1986)).

# CHAPTER 2

# MONOPOLY POWER

## I. Introduction

Monopoly power can harm society by making output lower, prices higher, and innovation less than would be the case in a competitive market.[1] The possession of monopoly power is an element of the monopolization offense,[2] and the dangerous probability of obtaining monopoly power is an element of the attempted monopolization offense.[3] As discussed in chapter 1, the mere possession of monopoly power does not violate section 2.[4]

This monopoly-power requirement serves as an important screen for evaluating single-firm liability. It significantly reduces the possibility of discouraging "the competitive enthusiasm that the antitrust laws seek to promote,"[5] assures the vast majority of competitors that their unilateral actions do not violate section 2, and reduces enforcement costs by keeping many meritless cases out of court and allowing others to be resolved without a trial. Accordingly, it is important to determine when monopoly power exists within the meaning of section 2.

An understanding of monopoly power helps in crafting appropriate antitrust policy towards single-firm conduct. Drawing on lessons from the hearings, along with existing jurisprudence and economic learning, this chapter discusses the Department's view on appropriate assessment of monopoly power in enforcing section 2.

## II. Market Power and Monopoly Power

Market power is a seller's ability to exercise some control over the price it charges. In our economy, few firms are pure price takers facing perfectly elastic demand.[6] For example, the unique location of a dry cleaner may confer slight market power because some customers are willing to pay a little more rather than walk an extra block or two to the next-closest dry cleaner. Economists say the dry cleaner possesses market power, if only to a trivial degree. Virtually all products that are differentiated from one another, if only because of consumer tastes, seller reputation, or producer location, convey upon their sellers at least some degree of market power. Thus, a small degree of market power is very common and understood not to warrant antitrust intervention.[7]

Market power and monopoly power are related but not the same. The Supreme Court has defined market power as "the ability to

[1] *See generally* 2B PHILLIP E. AREEDA ET AL., ANTITRUST LAW ¶ 403b, at 8 & n.2 (3d ed. 2007); RICHARD A. POSNER, ANTITRUST LAW 9–32 (2d ed. 2001).

[2] United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

[3] Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993).

[4] *See* Chapter 1, Part I(A); *see also Grinnell*, 384 U.S. at 570–71 (requiring improper conduct—as opposed to superior skill, foresight, or industry—as an element of a section 2 violation).

[5] Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 775 (1984).

[6] *See* Sherman Act Section 2 Joint Hearing: Monopoly Power Session Hr'g Tr. 13–14, Mar. 7, 2007 [hereinafter Mar. 7 Hr'g Tr.] (Nelson) ("[I]f you have a differentiated product and thus have a downward-sloping demand curve for your product, you might have some degree of ability to raise prices above costs and you might in that sense have market power . . . .").

[7] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Conduct as Related to Competition Hr'g Tr. 55, May 8, 2007 [hereinafter May 8 Hr'g Tr.] (Sidak) ("I don't think that the downward-sloping demand curve itself is a cause for antitrust intervention."); Dennis W. Carlton, *Market Definition: Use and Abuse*, COMPETITION POL'Y INT'L, Spring 2007, at 3, 7.

raise prices above those that would be charged in a competitive market,"[8] and monopoly power as "the power to control prices or exclude competition."[9] The Supreme Court has held that "[m]onopoly power under § 2 requires, of course, something greater than market power under § 1."[10] Precisely where market power becomes so great as to constitute what the law deems to be monopoly power is largely a matter of degree rather than one of kind. Clearly, however, monopoly power requires, at a minimum, a substantial degree of market power.[11] Moreover, before subjecting a firm to possible challenge under antitrust law for monopolization or attempted monopolization, the power in question is generally required to be much more than merely fleeting; that is, it must also be durable.[12]

Although monopoly power will generally result in the setting of prices above competitive levels, the desire to obtain profits that derive from a monopoly position provides a critical incentive for firms to invest and create the valuable products and processes that drive economic growth.[13] For this reason, antitrust law does not regard as illegal the mere possession of monopoly power where it is the product of superior skill, foresight, or industry.[14] Where monopoly power is acquired or maintained through anticompetitive conduct, however, antitrust law properly objects.

Section 2's requirement that single-firm conduct create or maintain, or present a dangerous probability of creating, monopoly power serves as an important screen for evaluating single-firm liability. Permitting conduct that likely creates at most an ability to exercise a minor degree of market power significantly reduces the possibility of discouraging "the competitive enthusiasm that the antitrust laws seek to promote"[15] and assures the majority of competitors that their unilateral actions will not violate section 2. It also reduces enforcement costs, including costs associated with devising and policing remedies. The costs that firms, courts, and competition authorities would incur in identifying and litigating liability, as well as devising and policing remedies for any and all conduct with the potential to have a minor negative impact on competition for short periods, would almost certainly far outweigh the benefits, particularly if the calculus includes, as it should, the loss of procompetitive activity that would inevitably

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[8] NCAA v. Bd. of Regents of the Univ. of Okla., 468 U.S. 85, 109 n.38 (1984); *see also* Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 27 n.46 (1984) ("As an economic matter, market power exists whenever prices can be raised above levels that would be charged in a competitive market."); *cf.* DENNIS W. CARLTON & JEFFREY M. PERLOFF, MODERN INDUSTRIAL ORGANIZATION 642 (4th ed. 2005) (noting that a firm has market power "if it is profitably able to charge a price above that which would prevail under competition"); William M. Landes & Richard A. Posner, *Market Power in Antitrust Cases*, 94 HARV. L. REV. 937, 939 (1981) ("A simple economic meaning of the term 'market power' is the ability to set price above marginal cost."). The demand curve faced by the perfectly competitive firm is a horizontal line—the market price: the firm can sell as much as it wants at the market price, but it can sell nothing at a price even slightly higher. Consequently, the perfectly competitive firm maximizes its profits by producing up to the point at which its marginal cost equals the market price.

[9] United States v. E. I. du Pont de Nemours & Co. (*Cellophane*), 351 U.S. 377, 391 (1956).

[10] Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451, 481 (1992).

[11] *See, e.g.*, Bacchus Indus., Inc. v. Arvin Indus., Inc., 939 F.2d 887, 894 (10th Cir. 1991) (defining monopoly power as "substantial" market power); Deauville Corp. v. Federated Dep't Stores, Inc., 756 F.2d 1183, 1192 n.6 (5th Cir. 1985) (defining monopoly power as an "extreme degree of market power"); 3A PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 801, at 318 (2d ed. 2002) (stating that "the Sherman Act § 2 notion of monopoly power . . . is conventionally understood to mean 'substantial' market power"); Landes & Posner, *supra* note 8, at 937 (defining monopoly power as "a high degree of market power").

[12] *See* AREEDA & HOVENKAMP, *supra* note 11, ¶ 801d, at 323; *see also* Colo. Interstate Gas Co. v. Natural Gas Pipeline Co. of Am., 885 F.2d 683, 695–96 (10th Cir. 1989) (finding a firm lacked monopoly power because its "ability to charge monopoly prices will necessarily be temporary").

[13] *See* Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407–08 (2004).

[14] *See, e.g.*, United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

[15] Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 775 (1984).

be discouraged in such a system.

## III. Identifying Monopoly Power

Monopoly power is conventionally demonstrated by showing that both (1) the firm has (or in the case of attempted monopolization, has a dangerous probability of attaining) a high share of a relevant market and (2) there are entry barriers—perhaps ones created by the firm's conduct itself—that permit the firm to exercise substantial market power for an appreciable period.[16] Unless these conditions are met, defendant is unlikely to have either the incentive or ability to exclude competition.[17]

### A. Market Shares

#### 1. Courts Typically Have Required a Dominant Market Share to Infer Monopoly Power

In determining whether a competitor possesses monopoly power in a relevant market, courts typically begin by looking at the firm's market share.[18] Although the courts "have not yet identified a precise level at which monopoly power will be inferred,"[19] they have demanded a dominant market share. Discussions of the requisite market share for monopoly power commonly begin with Judge Hand's statement in *United States v. Aluminum Co. of America* that a market share of ninety percent "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."[20] The Supreme Court quickly endorsed Judge Hand's approach in *American Tobacco Co. v. United States*.[21]

Following *Alcoa* and *American Tobacco*, courts typically have required a dominant market share before inferring the existence of monopoly power. The Fifth Circuit observed that "monopolization is rarely found when the defendant's share of the relevant market is below 70%."[22] Similarly, the Tenth Circuit noted that to establish "monopoly power, lower courts generally require a minimum market share of between 70% and 80%."[23] Likewise, the Third Circuit stated that "a share significantly larger than 55% has been required to establish prima facie market power"[24] and held that a market share between seventy-five percent and eighty percent of sales is "more than adequate to establish a prima facie case of power."[25]

It is also important to consider the share levels that have been held insufficient to allow courts to conclude that a defendant possesses monopoly power. The Eleventh Circuit held

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[16] *See* W. Parcel Express v. UPS, 190 F.3d 974, 975 (9th Cir. 1999); Am. Council of Certified Podiatric Physicians & Surgeons v. Am. Bd. of Podiatric Surgery, Inc., 185 F.3d 606, 622–23 (6th Cir. 1999).

[17] *See, e.g.*, May 8 Hr'g Tr., *supra* note 7, at 46 (Creighton) (noting that "the percentage of the market that you control actually can be helpful as direct evidence regarding how profitable it is likely to be to you, and both your incentives and your ability to enter into some kind of exclusionary conduct"); Mar. 7 Hr'g Tr., *supra* note 6, at 69–71 (Katz); HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY 82–83 (3d ed. 2005); Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 336 (2003) (asserting that market share "bears on the ability of the defendant to persuade buyers to agree to exclusionary schemes, the likelihood that those schemes will impair rival efficiency, the profitability to the defendant of impairing rival efficiency, and the relevance of any economies of share the defendant may enjoy from the scheme").

[18] *See, e.g.*, U.S. Anchor Mfg., Inc. v. Rule Indus., Inc., 7 F.3d 986, 999 (11th Cir. 1993) ("The principal measure of actual monopoly power is market share . . . ."); Movie 1 & 2 v. United Artists Commc'ns, Inc., 909 F.2d 1245, 1254 (9th Cir. 1990) (stating that "although market share does not alone determine monopoly power, market share is perhaps the most important factor to consider in determining the presence or absence of monopoly power"); Weiss v. York Hosp., 745 F.2d 786, 827 (3d Cir. 1984) ("A primary criterion used to assess the existence of monopoly power is the defendant's market share.").

[19] SECTION OF ANTITRUST LAW, AM. BAR ASS'N, MARKET POWER HANDBOOK 19–20 (2005) (footnote omitted).

[20] 148 F.2d 416, 424 (2d Cir. 1945).

[21] *See* 328 U.S. 781, 813–14 (1946).

[22] Exxon Corp. v. Berwick Bay Real Estates Partners, 748 F.2d 937, 940 (5th Cir. 1984) (per curiam).

[23] Colo. Interstate Gas Co. v. Natural Gas Pipeline Co. of Am., 885 F.2d 683, 694 n.18 (10th Cir. 1989) (citation omitted).

[24] United States v. Dentsply Int'l, Inc., 399 F.3d 181, 187 (3d Cir. 2005).

[25] *Id.* at 188.

that a "market share at or less than 50% is inadequate as a matter of law to constitute monopoly power."[26] The Seventh Circuit observed that "[f]ifty percent is below any accepted benchmark for inferring monopoly power from market share."[27] A treatise agrees, contending that "it would be rare indeed to find that a firm with half of a market could individually control price over any significant period."[28]

Some courts have stated that it is possible for a defendant to possess monopoly power with a market share of less than fifty percent.[29] These courts provide for the possibility of establishing monopoly power through non-market-share evidence, such as direct evidence of an ability profitably to raise price or exclude competitors. The Department is not aware, however, of any court that has found that a defendant possessed monopoly power when its market share was less than fifty percent.[30] Thus, as a practical matter, a market share of greater than fifty percent has been necessary for courts to find the existence of monopoly power.[31]

**2. Significance of a Dominant Market Share**

A dominant market share is a useful starting point in determining monopoly power. Modern decisions consistently hold, however, that proof of monopoly power requires more than a dominant market share. For example, the Sixth Circuit instructed that "market share is only a starting point for determining whether monopoly power exists, and the inference of monopoly power does not automatically follow from the possession of a commanding market share."[32] Likewise, the Second Circuit held that a "court will draw an inference of monopoly power only after full consideration of the relationship between market share and other relevant characteristics."[33]

A simple example illustrates the "pitfalls in mechanically using market share data" to

[26] Bailey v. Allgas, Inc., 284 F.3d 1237, 1250 (11th Cir. 2002).

[27] Blue Cross & Blue Shield United of Wis. v. Marshfield Clinic, 65 F.3d 1406, 1411 (7th Cir. 1995) (Posner, C.J.); *accord* Rebel Oil Co. v. Atl. Richfield Co., 51 F.3d 1421, 1438 (9th Cir. 1995) (noting that "numerous cases hold that a market share of less than 50 percent is presumptively insufficient to establish market power" in a claim of actual monopolization); U.S. Anchor Mfg., Inc. v. Rule Indus., Inc., 7 F.3d 986, 1000 (11th Cir. 1993).

[28] AREEDA ET AL., *supra* note 1, ¶ 532c, at 250.

[29] *See* Hayden Publ'g Co., Inc. v. Cox Broad. Corp., 730 F.2d 64, 69 n.7 (2d Cir. 1984) ("[A] party may have monopoly power in a particular market, even though its market share is less than 50%."); Broadway Delivery Corp. v. UPS, 651 F.2d 122, 129 (2d Cir. 1981) ("[W]hen the evidence presents a fair jury issue of monopoly power, the jury should not be told that it must find monopoly power lacking below a specified share."); Yoder Bros., Inc. v. Cal.-Fla. Plant Corp., 537 F.2d, 1347, 1367 n.19 (5th Cir. 1976) (rejecting "a rigid rule requiring 50% of the market for a monopolization offense without regard to any other factors").

[30] *Cf. U.S. Anchor Mfg.*, 7 F.3d at 1000 ("[W]e have discovered no cases in which a court found the existence of actual monopoly established by a bare majority share of the market.").

[31] This observation does not apply to claims of attempted monopolization. Courts, commentators, and panelists all recognize that situations can exist where "there [is] a dangerous probability that the defendant's conduct would propel it from a non-monopolistic share of the market to a share that would be large enough to constitute a monopoly for purposes of the monopolization offense." Colo. Interstate Gas Co. v. Natural Gas Pipeline Co. of Am., 885 F.2d 683, 694 (10th Cir. 1989); *see also, e.g.*, *Rebel Oil*, 51 F.3d at 1438 ("[T]he minimum showing of market share required in an attempt case is a lower quantum than the minimum showing required in an actual monopolization case."); Domed Stadium Hotel, Inc. v. Holiday Inns, Inc., 732 F.2d 480, 490 (5th Cir. 1984) (holding that "a share of less than the fifty percent generally required for actual monopolization may support a claim for attempted monopolization"); May 8 Hr'g Tr., *supra* note 7, at 46–47 (Creighton); Mar. 7 Hr'g Tr., *supra* note 6, at 154 (Krattenmaker); AREEDA & HOVENKAMP, *supra* note 11, ¶ 807d, at 372 (noting that "[t]he all important consideration is that the alleged conduct must be reasonably capable of creating a monopoly in the defined market. . . . [A] moderate but rising share may pose more 'dangerous probability' than would a higher but falling share.").

[32] Am. Council of Certified Podiatric Physicians & Surgeons v. Am. Bd. of Podiatric Surgery, Inc., 185 F.3d 606, 623 (6th Cir. 1999).

[33] Tops Mkts., Inc. v. Quality Mkts., Inc., 142 F.3d 90, 98 (2d Cir. 1998).

measure monopoly power.[34] Suppose a large firm competes with a fringe of small rivals, all producing a homogeneous product. In this situation, the large firm's market share is only one determinant of its power over price. Even a very high share does not guarantee substantial power over price for a significant period: if the fringe firms can readily and substantially increase production at their existing plants in response to a small increase in the large firm's price (that is, if the fringe supply is highly elastic), a decision by the large firm to restrict output may have no effect on market prices.[35]

Even if fringe firms cannot readily and substantially increase production, a firm with a very high market share is still not guaranteed substantial power over price if the quantity demanded decreases significantly in response to a small price increase—in other words, if market demand is highly elastic.[36] That is, when demand is elastic, a firm may be unable to raise price without losing so many sales that it will prove to be an unprofitable strategy.[37]

Instances of high fringe-firm supply elasticity or high industry-demand elasticity are not the only situations where a high market share may be a misleading indicator of monopoly power. In markets characterized by rapid technological change, for example, a high market share of current sales or production may be consistent with the presence of robust competition over time rather than a sign of monopoly power.[38] In those situations, any power a firm may have may be both temporary and essential to the competitive process. Indeed, in the extreme case, "market structure may be a series of temporary monopolies" in a dynamically competitive market.[39]

Notwithstanding that a high share of the relevant market does not always mean that monopoly power exists, a high market share is one of the most important factors in the Department's examination of whether a firm has, or has a dangerous probability of obtaining, monopoly power. A high share indicates that it is appropriate to examine other relevant factors. In this regard, if a firm has maintained a market share in excess of two-thirds for a significant period and market conditions (for example, barriers to entry) are such that the firm's market share is unlikely to be eroded in the near future, the Department believes that such evidence ordinarily should establish a rebuttable presumption that the firm possesses monopoly power. This approach is consistent with the case law.[40]

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[34] Landes & Posner, *supra* note 8, at 947; *see also id.* at 944–97.

[35] *Id.* at 945–46 n.20.

[36] *Cf.* Jonathan B. Baker & Timothy F. Bresnahan, *Empirical Methods of Identifying and Measuring Market Power*, 61 ANTITRUST L.J. 3, 10 (1992) ("[W]hen industry demand is highly elastic, firms with market power behave similarly to those without market power.").

[37] *See* CARLTON & PERLOFF, *supra* note 8, at 92–93; Landes & Posner, *supra* note 8, at 941–42.

[38] *See, e.g.*, May 8 Hr'g Tr., *supra* note 7, at 53–54 (Rule) (stating that as the economy becomes "more dynamic and complex," it "becomes a little more difficult to use the market power and monopoly power market share screen that traditionally we have used"); Sherman Act Section 2 Joint Hearing: Monopoly Power Session Hr'g Tr. 11–12, Mar. 8, 2007 [hereinafter Mar. 8 Hr'g Tr.] (Schmalensee) ("In a number of markets marked by rapid technological change, network effects can lead some firms to high shares. If you have a snapshot in which network effects have led to a dominant position, that snapshot is consistent with a world of vigorous Schumpeterian competition, in which the next hot product may displace the leader."); Mar. 7 Hr'g Tr., *supra* note 6, at 78–79 (Katz) (noting that "the R&D capabilities . . . may be much more important than current market shares in terms of understanding innovation").

[39] Michael L. Katz, Market Definition, Concentration & Section 2, at 5 (Mar. 7, 2007) (hearing submission).

[40] *See generally* 1 SECTION OF ANTITRUST LAW, AM. BAR ASS'N, ANTITRUST LAW DEVELOPMENTS 231 (6th ed. 2007) ("A market share in excess of 70 percent generally establishes a prima facie case of monopoly power, at least with evidence of substantial barriers to entry and evidence that existing competitors could not expand output." (footnotes omitted)); AREEDA & HOVENKAMP, *supra* note 11, ¶ 801a, at 319 ("Although one cannot be too categorical, we believe it reasonable to presume the existence of substantial single-firm market power from a showing that the defendant's share of a well-defined market protected by sufficient entry barriers has exceeded 70 or 75 percent for the five years preceding the complaint."); *supra* notes 20–25 and accompanying text.

### 3. Market-Share Safe Harbor

To give businesses greater certainty in circumstances where significant competitive concerns are unlikely, many panelists supported a market-share safe harbor in section 2 cases, voicing skepticism about how frequently monopoly power would be present when a firm possesses a market share less than Alcoa's "sixty or sixty-four percent" market share.[41] Market shares "can be used to eliminate frivolous antitrust cases, [and] that use can contribute enormous value to society."[42]

However, other panelists voiced objections to a market-share safe harbor. Market definition can lack precision,[43] and it is possible that an incorrect market definition could allow anticompetitive conduct to avoid liability.[44] Additionally, some assert that, just as firms with large shares may not have monopoly power, firms with relatively small shares can sometimes still harm competition by their unilateral conduct. They thus are concerned that a safe harbor may protect anticompetitive conduct.[45]

The Department believes that a market-share safe harbor for monopoly—as opposed to market—power warrants serious consideration by the courts. In many decades of section 2 enforcement, we are aware of no court that has found monopoly power when defendant's share was less than fifty percent, suggesting instances of monopoly power below such a share, even if theoretically possible, are exceedingly rare in practice. It is therefore plausible that the costs of seeking out such instances exceed the benefits.

## B. Durability of Market Power

The Second Circuit has defined monopoly power as "the ability '(1) to price substantially above the competitive level *and* (2) to persist in doing so for a significant period without erosion by new entry or expansion.'"[46] Likewise, other circuit courts have found that firms with dominant market shares lacked monopoly power when their market power was insufficiently durable.[47]

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[41] *See* May 8 Hr'g Tr., *supra* note 7, at 41 (Eisenach) (stating that he is "not opposed in any way to a 75 percent safe harbor or a 70 percent safe harbor"); *id.* at 42 (Rill) (noting that "70 percent sounds reasonable . . . maybe a little higher"); Mar. 7 Hr'g Tr., *supra* note 6, at 216 (Sims) (stating that he might be "very comfortable" with a "70 percent or an 80 percent number"); *id.* at 218 (Bishop) (stating that he "would set the threshold at 70–80 percent"). *But see id.* at 217 (Stelzer) (opposing a market-share safe harbor); *cf. id.* at 218 (Krattenmaker) (supporting market-share safe harbors but deeming a single safe harbor inappropriate for all conduct).

[42] Carlton, *supra* note 7, at 27.

[43] *Cf.* May 8, Hr'g Tr., *supra* note 7, at 44 (Melamed) ("From my experience in counseling, market share-type screens are of limited value because market share depends on market definition, and it is a binary concept and we are often sitting there saying well, gidgets might be in the market with widgets, but they might not be and who knows."); Sherman Act Section 2 Joint Hearing: Section 2 Policy Issues Hr'g Tr. 54, May 1, 2007 [hereinafter May 1 Hr'g Tr.] (Jacobson) (noting that "there are a lot of differentiated products where you do not know where the market definition fight is going to come out").

[44] *Cf.* Mar. 7 Hr'g Tr., *supra* note 6, at 57–58 (Gilbert); *id.* at 65, 74–76 (Katz).

[45] *See, e.g.*, May 8 Hr'g Tr., *supra* note 7, at 49 (Pitofsky) ("Let me just say that first of all, I'm not comfortable with safe harbors. I like rebuttable presumptions because there are too many quirky situations. Somebody has 40 percent of the market but everybody else has one percent each."); *id.* at 52 (Sidak) ("Would we infer that there is not a problem because the market share is only 40 percent and that is way below Judge Hand's ALCOA threshold or would we look at a price increase or loss of competitor market share and say that is a more direct set of facts that elucidates what the price elasticity of demand is?").

[46] AD/SAT v. Associated Press, 181 F.3d 216, 227 (2d Cir. 1999) (quoting 2A AREEDA ET AL., *supra* note 1, ¶ 501, at 90 (2d. ed. 2002) (emphasis in original)); *see also* United States v. Dentsply Int'l, Inc., 399 F.3d 181, 188–89 (3d Cir. 2005) ("In evaluating monopoly power, it is not market share that counts, but the ability to *maintain* market share." (quoting United States v. Syufy Enters., 903 F.2d 659, 665–66 (9th Cir. 1990) (emphasis in original))).

[47] *See, e.g.*, W. Parcel Express v. UPS, 190 F.3d 974, 975 (9th Cir. 1999) (finding that a firm with an allegedly "dominant share" could not possess monopoly power because there were no significant "barriers to entry"); *Colo. Interstate Gas*, 885 F.2d at 695–96 ("If the evidence demonstrates that a firm's ability to charge monopoly prices will necessarily be temporary, the firm will not possess the degree of market power required for the

Panelists agreed that monopoly power is the ability to engage profitably in substantial, sustained supracompetitive pricing. As one panelist noted, the "picture [of monopoly power] that we carry around in our head" is "the sustained charging of a price above marginal cost, maintaining . . . a price substantially above marginal cost."[48] Another stressed, "[F]or antitrust to worry about market power . . . it has to be durable."[49]

"[A] firm cannot possess monopoly power in a market unless that market is also protected by significant barriers to entry."[50] In particular, a high market share provides no reliable indication of the potential for rivals to supply market demand. Even when no current rival exists, an attempt to increase price above the competitive level may lead to an influx of competitors sufficient to make that price increase unprofitable.[51] In that case, the firm lacks monopoly power even though it may currently have a dominant market share.[52]

## IV. Market Definition and Monopoly Power

The Supreme Court has noted the crucial role that defining the relevant market plays in section 2 monopolization and attempt cases.[53] The market-definition requirement brings discipline and structure to the monopoly-power inquiry, thereby reducing the risks and costs of error.

The relevant product market in a section 2 case, as elsewhere in antitrust, "is composed of products that have reasonable interchangeability for the purposes for which they are produced—price, use and qualities considered."[54] Thus, the market is defined with regard to demand substitution, which focuses

monopolization offense."); Williamsburg Wax Museum, Inc. v. Historic Figures, Inc., 810 F.2d 243, 252 (D.C. Cir. 1987) (finding that a firm did not have monopoly power when a competitor was able to supply customer's demand within a year); Borough of Lansdale v. Phila. Elec. Co., 692 F.2d 307, 312–14 (3d Cir. 1982) (affirming finding that power company did not have monopoly power when customer could have built its own power line within sixteen months).

[48] Mar. 7 Hr'g Tr., *supra* note 6, at 32 (White); *see also id.* at 61 (Gilbert); *id.* at 82–83 (Gavil); *id.* at 87 (White) (monopoly power is the ability profitably to charge "a price significantly above marginal cost, sustained for a sustained amount of time . . . how much and for how long, I do not know"); *id.* at 96–97 (Katz).

[49] Mar. 8 Hr'g Tr., *supra* note 38, at 80 (Lande); *see also* AREEDA & HOVENKAMP, *supra* note 11, ¶ 801, at 319 (suggesting that "it is generally reasonable to presume that a firm has monopoly power when the firm's dominant market share has lasted, or will last, for at least five years").

[50] United States v. Microsoft Corp., 253 F.3d 34, 82 (D.C. Cir. 2001) (en banc) (per curiam); *see also* Harrison Aire, Inc. v. Aerostar Int'l, Inc., 423 F.3d 374, 381 (3d Cir. 2005) ("In a typical section 2 case, monopoly power is 'inferred from a firm's possession of a dominant share of a relevant market that is protected by entry barriers.'" (quoting *Microsoft*, 253 F.3d at 51)); *cf.* Mar. 7 Hr'g Tr., *supra* note 6, at 139–40 (de la Mano) (stating that "substantial market power" entails "barriers to entry and expansion" that are "significant").

[51] *See, e.g.*, 2A AREEDA ET AL., *supra* note 1, ¶ 501, at 91 (2d ed. 2002) ("In spite of its literal imprecision, the standard formulation is essentially correct in asking whether the defendant can price monopolistically without prompt erosion from rivals' entry or expansion.").

[52] *See, e.g.*, United States v. Waste Mgmt., Inc., 743 F.2d 976, 983–84 (2d Cir. 1984) (noting that, in a market where entry is easy, a firm that raised price "would then face lower prices charged by all existing competitors as well as entry by new ones, a condition fatal to its economic prospects if not rectified"). *See generally* Franklin M. Fisher, *Diagnosing Monopoly*, Q. REV. ECON. & BUS., Summer 1979, at 7, 23 (noting that "consideration of the role of entry plays a major part in any assessment of monopoly power").

[53] *See* Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993) (explaining that "the dangerous probability of monopolization in an attempt case . . . requires inquiry into the relevant product and geographic market and the defendant's economic power in that market"); United States v. Grinnell Corp., 384 U.S. 563, 571 (1966); Walker Process Equip., Inc. v. Food Mach. & Chem. Corp., 382 U.S. 172, 177 (1965) ("Without a definition of that market there is no way to measure [a defendant's] ability to lessen or destroy competition.").

[54] United States v. E. I. du Pont de Nemours & Co. (*Cellophane*), 351 U.S. 377, 404 (1956); *see also Microsoft*, 253 F.3d at 51–52 ("'Because the ability of consumers to turn to other suppliers restrains a firm from raising prices above the competitive level,' the relevant market must include all products 'reasonably interchangeable by consumers for the same purposes.'" (citation omitted) (quoting Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 218 (D.C. Cir. 1986) and *Cellophane*, 351 U.S. at 395)).

on buyers' views of which products are acceptable substitutes or alternatives.[55]

However, particular care is required when delineating relevant markets in monopolization cases. In merger cases, the antitrust enforcement agencies define markets by applying the hypothetical monopolist paradigm. The Horizontal Merger Guidelines state:

> A market is defined as a product or group of products and a geographic area in which it is produced or sold such that a hypothetical, profit-maximizing firm, not subject to price regulation, that was the only present and future producer or seller of those products in that area likely would impose at least a 'small but significant and nontransitory' increase in price, assuming the terms of sale of all other products are held constant.[56]

The Guidelines go on to explain that in implementing this definition, the agencies "use prevailing prices."[57] In the section 2 context, however, if the inquiry is being conducted after monopoly power has already been exercised, using prevailing prices can lead to defining markets too broadly and thus inferring that monopoly power does not exist when, in fact, it does.[58]

The problem with using prevailing prices to define the market in a monopoly-maintenance case is known as the "Cellophane Fallacy" because it arose in a case involving cellophane, where an issue before the Supreme Court was whether the relevant market was cellophane or all flexible-packaging materials.[59] During the relevant period, du Pont produced over seventy percent of the cellophane in the United States.[60] Cellophane, however, "constituted less than 20% of all 'flexible packaging material' sales."[61] The Court concluded that cellophane's interchangeability with other materials made it part of a broader, flexible-packaging market.

Many have criticized the Court's reasoning because it assessed the alternatives for cellophane after du Pont already had raised its price to the monopoly level, failing to recognize that a firm with monopoly power finds it profitable to raise price—above the competitive level—until demand becomes elastic. Hence, it should not be at all surprising to find that at the monopoly price the firm faces close substitutes and would not be able profitably to raise price further.[62] "Because every monopolist faces an elastic demand . . . at its profit-maximizing output and price, there is bound to be some substitution of other products for its own when it is maximizing profits, even if it has great market power."[63]

One panelist suggested using the hypothetical-monopolist paradigm in certain monopoly-acquisition cases, defining the relevant market as of a time before the challenged conduct began and carrying forward the resulting market definition to the present to assess whether the firm possesses

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[55] *See* Jonathan B. Baker, *Market Definition: An Analytical Overview*, 74 ANTITRUST L.J. 129, 132 (2007).

[56] U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES § 1.0 (1992) (rev. ed. 1997), *available at* http://www.usdoj.gov/atr/public/guidelines/hmg.pdf.

[57] *Id.* § 1.11. However, the Guidelines recognize that when "premerger circumstances are strongly suggestive of coordinated interaction . . . the Agency will use a price more reflective of the competitive price." *Id.* (footnote omitted).

[58] *See, e.g.*, Mark A. Glick et al., *Importing the Merger Guidelines Market Test in Section 2 Cases: Potential Benefits and Limitations*, 42 ANTITRUST BULL. 121, 145–49 (1997); Philip Nelson, Monopoly Power, Market Definition, and the *Cellophane* Fallacy 7 (n.d.) (hearing submission).

[59] *Cellophane*, 351 U.S. at 377.

[60] *Id.* at 379.

[61] *Id.*

[62] *See, e.g.*, Landes & Posner, *supra* note 8, at 960–61. *See generally* George W. Stocking & Willard F. Mueller, *The* Cellophane *Case and the New Competition*, 45 AM. ECON. REV. 29, 53–54 (1955).

[63] Landes & Posner, *supra* note 8, at 961 (footnote omitted); *see also, e.g.*, Lawrence J. White, Market Power and Market Definition in Monopolization Cases: A Paradigm Is Missing 7 (Jan. 24, 2007) (hearing submission) ("[A]ll firms—regardless of whether they are competitive or are truly monopolists—will be found to be unable to raise price profitably from currently observed levels, since they will already have established a profit-maximizing price for themselves; and thus this 'test' will fail to separate the true monopolist that does exercise market power from the firm that does not have market power.").

monopoly power.[64] This suggestion is sound in theory. Unfortunately, however, substantial practical problems may make it difficult to determine consumers' preferences and other relevant factors as of some prior date, thereby impeding the ability to conduct an accurate "but-for" exercise.[65] Moreover, the market definition as of the pre-conduct time may no longer be relevant because of intervening new product introductions or other significant changes in the marketplace.

An additional problem concerns allegations of monopoly maintenance where the conduct in question allegedly has maintained preexisting monopoly power rather than created that power. One possibility is to apply the hypothetical-monopolist paradigm of the Horizontal Merger Guidelines just as in merger cases, except at the competitive price rather than the prevailing price. However, accurately determining the competitive price is apt to be quite difficult in such cases.

Despite its limitations in the section 2 context, there exists no clear and widely accepted alternative to the hypothetical-monopolist methodology for defining relevant markets.[66] Some commentators suggest that, for all its limitations, the hypothetical-monopolist paradigm still has value in monopolization cases.[67] It appropriately focuses the market-definition process on market-power considerations and thereby helps to avoid ad hoc conclusions regarding the boundaries of the market and the effects of the conduct.

Moreover, and importantly, concerns over the Cellophane Fallacy need not confound market definition in all section 2 cases. Panelists observed that, although there may be no reliable paradigm for defining the relevant market in every case, courts often are able to draw sound conclusions about the relevant market based on the facts and circumstances of the industry.[68] Furthermore, "[T]he issue in many cases arising under Section 2 of the Sherman Act is whether ongoing or threatened conduct, if left unchecked, would create monopoly power—not whether the defendant already possesses monopoly power."[69] In particular, *Cellophane* considerations present less of a problem in attempted monopolization cases where monopoly prices are either not yet being charged or where competitive prices were being charged in the not-too-distant pre-conduct past. The Department believes that market definition remains an important aspect of section 2 enforcement and that continued consideration and study is warranted regarding how to appropriately determine relevant markets in this context.

## V. Other Approaches to Identifying Monopoly Power

As noted above, courts typically determine whether a firm possesses monopoly power by first ascertaining the relevant market and then examining market shares, entry conditions, and other factors with respect to that market. One important issue is whether plaintiffs should instead be permitted to demonstrate monopoly power solely through direct evidence—for example, proof of high profits[70]—thus

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[64] May 1 Hr'g Tr., *supra* note 43, at 162 (Willig) (stating that "mentally, we can go back to before" the exclusion, and "there is a relevant market that's pertinent for this analysis").

[65] *See* Carlton, *supra* note 7, at 20 ("It may sometimes be difficult to figure out the [but-for] benchmark price, though not always.").

[66] *See* Mar. 7 Hr'g Tr., *supra* note 6, at 127–28 (Bishop); Nelson, *supra* note 58, at 13 (stating that "there is no 'cookbook' methodology for defining markets" in monopolization cases); White, *supra* note 63, at 15 (stating that the "absence of a generally accepted market definition paradigm is a genuine problem").

[67] Gregory J. Werden, *Market Delineation Under the Merger Guidelines: Monopoly Cases and Alternative Approaches*, 16 REV. INDUS. ORG. 211, 214–15 (2000) ("[T]he Guidelines' hypothetical monopolist paradigm [can] play a very useful, albeit conceptual, role . . . provid[ing] the critical insight necessary to decide the case without any need to get into the details of their application."); White, *supra* note 63, at 14.

[68] *See* Mar. 7 Hr'g Tr., *supra* note 6, at 67–68 (Katz) (stating that market definition is often obvious); *cf. id.* at 51 (Gavil) (noting that defendants did not contest the existence of monopoly power in *LePage's, Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003) (en banc) and *Conwood Co. v. U.S. Tobacco Co.*, 290 F.3d 768 (6th Cir. 2002)).

[69] Werden, *supra* note 67, at 212.

[70] *See, e.g.*, Broadcom Corp. v. Qualcomm Inc., 501

rendering market definition unnecessary. While no court has relied solely on direct evidence to establish monopoly power, one court found direct evidence sufficient to survive summary judgment despite plaintiff's failure "to define the relevant market with precision."[71]

### A. Direct Evidence of High Profits, Price-Cost Margins, and Demand Elasticity

Relying exclusively on direct evidence of profits to establish monopoly power presents a number of difficult issues.[72] High accounting profits do not necessarily reflect the exercise of monopoly power. In particular, cost measures are normally available only from reports prepared in conformity with accounting conventions, but economics and accounting have significantly different notions of cost.[73] Accounting figures seldom reflect the firm's true economic cost of producing its goods and services, and accounting rates of return will often differ from true economic rates of return.[74]

For example, determining if a firm is earning an economic profit requires accounting properly for depreciation and the economic replacement cost of the assets the firm is using to generate its income. Yet the information reported by accountants frequently is not designed to measure and accurately reflect those costs.[75] In addition, determining if a firm is earning a profit reflecting the exercise of monopoly power should take into account the opportunity cost of employing those assets in their current use. Accounting records rarely attempt to make such assessments.

Moreover, available estimates of a firm's capital costs, an important input into calculating a firm's profitability, are generally based on accounting rules that do not account for the riskiness of the investment. If the investment, at the time it was made, was quite risky, a very high accounting rate of return may reflect a modest economic return. More generally, when all relevant economic costs are properly accounted for, what may at first seem to be a supracompetitive return may be no more than a competitive one (or vice versa).[76]

Using price-cost margins, rather than profits, as evidence of monopoly power is also unsatisfactory. Economists have long pointed to a firm's price-cost margin—its price minus its short-run marginal cost, all divided by its price (known as the Lerner index[77])—as a

F.3d 297, 307 (3d Cir. 2007) ("The existence of monopoly power may be proven through direct evidence of supracompetitive prices and restricted output."); PepsiCo, Inc. v. Coca-Cola Co., 315 F.3d 101, 107 (2d Cir. 2002) (per curiam) (holding that "there is authority to support [the proposition] that a relevant market definition is not a necessary component of a monopolization claim"); *Conwood*, 290 F.3d at 783 n.2 (noting that monopoly power "'may be proven directly by evidence of the control of prices or the exclusion of competition'" (quoting Tops Mkts., Inc. v. Quality Mkts., Inc., 142 F.3d 90, 97–98 (2d Cir. 1998))).

[71] Re/Max Int'l, Inc. v. Realty One, Inc., 173 F.3d 995, 1016 (6th Cir. 1999) ("[A]lthough the plaintiffs failed to define the relevant market with precision and therefore failed to establish the defendants' monopoly power through circumstantial evidence, there does exist a genuine issue of material fact as to whether the plaintiffs' evidence shows direct evidence of a monopoly, that is, actual control over prices or actual exclusion of competitors.").

[72] *See generally* Baker & Bresnahan, *supra* note 36, at 5 (noting that problems with accounting profits or mark-ups methodology "loom[s] so large that antitrust today does not rely heavily on profitability measures in making inferences about market power"); Richard Schmalensee, *Another Look at Market Power*, 95 HARV. L. REV. 1789, 1805 (1982) (discussing "serious problems with using profitability to gauge market power").

[73] This is not to suggest that financial data lack value for the economic analysis of competition. *See* Nelson, *supra* note 58, at 17.

[74] *See generally* George J. Benston, *Accounting Numbers and Economic Values*, 27 ANTITRUST BULL. 161, 162–66 (1982); Franklin M. Fisher & John J. McGowan, *On the Misuse of Accounting Rates of Return to Infer Monopoly Profits*, 73 AM. ECON. REV. 82, 82–84 (1983) (noting that standard accounting treatments of investment and depreciation are inappropriate for determining a firm's economic rate of return).

[75] *See* Fisher & McGowan, *supra* note 74.

[76] *See generally* Bailey v. Allgas, Inc., 284 F.3d 1237, 1252–55 (11th Cir. 2002); AREEDA ET AL., *supra* note 1, ¶ 516f; Margaret Sanderson & Ralph A. Winter, *"Profits" Versus "Rents" in Antitrust Analysis: An Application to the Canadian Waste Services Merger*, 70 ANTITRUST L.J. 485, 510–11 (2002).

[77] *See* A. P. Lerner, *The Concept of Monopoly and the*

measure of the extent to which the firm is exercising short-run market power.[78] For some purposes, such as attempting to determine the firm's short-run elasticity of demand at a given price, the measure can have value.

Short-run price-cost margins are not, however, of much use in determining whether a firm has monopoly power. Monopoly power requires that the firm be able profitably to charge prices high enough to earn a supernormal return on its investment. It is not clear how much price must exceed short-run marginal cost before there is monopoly power.[79] Depending on the size of the firm's fixed costs, even a significant margin between price and short-run marginal cost may be insufficient to earn even a normal return. Indeed, a firm should not be found to possess monopoly power simply because it prices in excess of short-run marginal cost and hence has a high price-cost margin.[80]

In principle, a better measure of margin would be the ratio of price to the firm's long-run marginal cost.[81] Unfortunately, such information, and in particular data allowing accurate adjustments for risk, is unlikely to be available.[82]

Nor does evidence concerning the elasticity of demand for the firm's products establish the existence of monopoly power. Demand elasticity can, to be sure, provide information about the firm's market power.[83] For example, a firm with no market power faces infinitely elastic demand.[84] Sellers of differentiated products, on the other hand, may face a significantly less elastic demand at their profit-maximizing prices. In those cases, they will generally have high price-cost margins and market power. Only rarely, however, will those firms possess monopoly power. As one panelist noted, "[E]lasticities do not help us very much. You cannot tell the difference between a true monopolist and . . . a seller of a differentiated product."[85] As an indicator of monopoly power, demand elasticities suffer from the same fundamental problem that margins do: neither tell us whether the firm is earning durable, supernormal profits.[86]

In short, direct evidence of a firm's profits, margins, or demand elasticities is not likely to provide an accurate or reliable alternative to the traditional approach of first defining the relevant market and then examining market shares and entry conditions when trying to determine whether the firm possesses monopoly power.

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*Measurement of Monopoly Power*, 1 REV. ECON. STUD. 157, 169 (1934).

[78] *See, e.g.*, CARLTON & PERLOFF, *supra* note 8, at 93.

[79] *See* Dennis W. Carlton, *Does Antitrust Need to be Modernized?*, J. ECON. PERSP., Summer 2007, at 155, 164 ("Since monopolistically competitive firms have some market power in the sense that price exceeds marginal cost, presumably the deviation between price and marginal cost . . . should be significant if it is to expose the firm to antitrust scrutiny. But no consensus exists in the courts or among economists as to how large this deviation should be.").

[80] *See* Mar. 7 Hr'g Tr., *supra* note 6, at 13–14 (Nelson); *id.* at 97 (Katz); *see also* CARLTON & PERLOFF, *supra* note 8, at 93 (distinguishing monopoly from market power on the basis that more than just a competitive profit is earned when a firm with monopoly power optimally sets its price above its short-run marginal cost).

[81] *See* Werden, *supra* note 67, at 214.

[82] *See generally* AREEDA ET AL., *supra* note 1, ¶ 504b, at 123–24; 3 AREEDA & HOVENKAMP, *supra* note 11, ¶ 739e; Werden, *supra* note 67, at 214 (noting that "[i]nferences based on econometrics and first-order conditions allow one to determine whether, and even how much, price exceeds short-run marginal cost, but not how much price exceeds long-run marginal cost"); Diane P. Wood, *"Unfair" Trade Injury: A Competition-Based Approach*, 41 STAN. L. REV. 1153, 1180–81 n.96 (1989) (noting that long-run marginal cost figures "are extremely difficult to calculate in practice").

[83] *See* CARLTON & PERLOFF, *supra* note 8, at 97–99.

[84] *Id.* at 66.

[85] Mar. 7 Hr'g Tr., *supra* note 6, at 38 (White); *see also* May 8 Hr'g Tr., *supra* note 7, at 56 (Muris) (stating that "it is difficult to have simple uses of Lerner indexes and downward sloping demand as measures of anything meaningful").

[86] Attempts to compare actual with competitive prices suffer from similar infirmities. Determining the competitive price is difficult, as is determining when price so exceeds the competitive level for so long that it amounts to monopoly power rather than just market power. *See* Carlton, *supra* note 7, at 6–7.

### B. Direct Evidence of Anticompetitive Effects

Focusing on anticompetitive effects, such as the reduction of output, may be more useful than focusing on profits, price-cost margins, or demand elasticity. In section 1 cases involving concerted conduct by competitors, courts have held that direct evidence of anticompetitive effects can demonstrate market power.[87] However, courts have not held expressly that direct evidence of anticompetitive effects can prove monopoly power in section 2 cases. But in several cases, courts have suggested that such an approach would make sense, and a number of panelists agreed.[88] If a dominant firm's conduct has been demonstrated to cause competitive harm, one could rely simply on that evidence and dispense with the market-definition requirement entirely.

However, there are concerns with taking such an approach. One important concern is that effects evidence, while very valuable, is generally imperfect, and sometimes subject to differing interpretations. For this reason, also requiring a traditional market-definition exercise—incorporating, perhaps, available evidence of alleged effects—likely adds value by strengthening inferences and thereby avoiding potentially costly errors.

The Department agrees with panelists who maintained that an assessment of actual or potential anticompetitive effects can be useful in a section 2 case.[89] In some circumstances, an inability to find any anticompetitive effects may serve as a useful screen, enabling courts or enforcement officials to conclude quickly that a section 2 violation is implausible. In other cases, there may be effects evidence strongly suggestive of harm and the existence of a relevant market that has indeed been monopolized.[90]

## VI. Conclusion

Monopoly power entails both greater and more durable power over price than mere market power and serves as an important screen for section 2 cases. As a practical matter, a market share of greater than fifty percent has been necessary for courts to find the existence of monopoly power. If a firm has maintained a market share in excess of two-thirds for a significant period and the firm's market share is unlikely to be eroded in the near future, the Department believes that such facts ordinarily should establish a rebuttable presumption that the firm possesses monopoly power. The Department is not likely to forgo defining the

[87] *See* FTC v. Ind. Fed'n of Dentists, 476 U.S. 447, 460–61 (1986) (noting that "'proof of actual detrimental effects, such as reduction of output,' can obviate the need for an inquiry into market power, which is but a 'surrogate for detrimental effects'" (quoting 7 PHILLIP E. AREEDA, ANTITRUST LAW ¶ 1511, at 429 (1986))).

[88] *See* Broadcom Corp. v. Qualcomm Inc., 501 F.3d 297, 307 (3d Cir. 2007); Conwood Co. v. U.S. Tobacco Co., 290 F.3d 768, 783 n.2 (6th Cir. 2002); *see also* Mar. 7 Hr'g Tr., *supra* note 6, at 39–40 (White) (proposing that analysis of alleged exclusion consider comparison of existing market with exclusion to hypothetical consequences of absence of exclusion); *id.* at 61–63 (Gilbert).

[89] *See, e.g.*, Mar. 7 Hr'g Tr., *supra* note 6, at 25–26 (Simons) ("[O]ne could argue that the first condition [should be] that the unilateral conduct be such that it is reasonably likely to significantly raise price and/or reduce quality . . . ."); *id.* at 40 (White); *id.* at 44–49 (Gavil); *id.* at 63 (Gilbert); *id.* at 114–119 (multiple panelists); Sherman Act Section 2 Joint Hearing: Academic Testimony Hr'g Tr. 90, Jan. 31, 2007 (Bresnahan) ("[Y]ou can gain a lot of clarity about a Section 2 case by bringing the competitive effects and causation arguments to the forefront."); *id.* at 174–76 (Rubinfeld).

[90] *See* Mar. 7 Hr'g Tr., *supra* note 6, at 40 (White) ("You have already found the effect. Implicitly, you have said there must be a market there . . . ."); *id.* at 63 (Gilbert) ("Too often, I think many of us would agree that the market definition exercise puts the cart in front of the horse. We should be thinking about where are the competitive effects . . . and then let the market definition respond to that rather than defining where the competitive effects are."); *id.* at 114 (Nelson) (stating that "the market definition exercise helps you understand what is going on . . . but that is not to say you have to do it in every case, and there are numerous cases where you may be able to expedite things by going straight to the competitive effects bottom line"). *But see id.* at 117 (Gilbert) ("But I also can sympathize that if we did away with market definition completely, it could be highly problematic in leading to a lot of cases."); *id.* at 195 (White) ("Yes, you ought to look at competitive effects more than we have, but I think there is still going to be a role for market definition.").

relevant market or calculating market shares in section 2 monopolization and attempt cases, but will use direct evidence of anticompetitive effects when warranted and will not rely exclusively on market shares in concluding that a firm possesses monopoly power.

U.S. Dep't of Justice, Competition and Monopoly: Single-Firm Conduct under Section 2 of the Sherman Act (issued by the Bush administration on Sept. 11, 2008) (withdrawn by the Obama administration on May 11, 2009).

## CHAPTER 3

# GENERAL STANDARDS FOR EXCLUSIONARY CONDUCT

### I. Introduction

As discussed in chapter 1, the Supreme Court's description of conduct that violates section 2 in *United States v. Grinnell Corp.*—"the willful acquisition or maintenance of [monopoly] power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident"[1]—provides little useful guidance.[2] The trial court's instruction to the jury approved in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, that a refusal to deal with a competitor is lawful if justified by "valid business reasons,"[3] has proven similarly unavailing as a source of specific guidance because of uncertainty over what constitutes a valid business reason. Indeed, commentators draw quite different conclusions from that instruction.[4]

While the Supreme Court has established conduct-specific tests for predatory pricing and bidding, it has neither articulated similarly explicit standards for many other types of potentially exclusionary conduct nor adopted a test applicable to all conduct.[5] The lower courts also have not settled on either a general test or conduct-specific tests.[6]

Accordingly, there has been increasing focus in recent years on developing more refined tests to determine whether conduct is anticompetitive under section 2. This effort has been informed, in large part, by the following principles set forth in chapter 1:

- Unilateral conduct is outside the purview of section 2 unless the actor possesses monopoly power or is likely to achieve it.
- The mere possession or exercise of monopoly power is not an offense; the law addresses only the anticompetitive acquisition or maintenance of such power (and certain related attempts).
- Acquiring or maintaining monopoly power through assaults on the competitive process harms consumers and is to be condemned.
- Mere harm to competitors—without harm to the competitive process—does not violate section 2.
- Competitive and exclusionary conduct can look alike—indeed, the same conduct can have both beneficial and exclusionary

[1] United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966).

[2] *See, e.g.*, 1 SECTION OF ANTITRUST LAW, AM. BAR ASS'N, ANTITRUST LAW DEVELOPMENTS 210, 242 (6th ed. 2007) (noting that "the highly abstract *Grinnell* language . . . has been criticized as not helpful in deciding concrete cases"); 3 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW, ¶ 651b, at 74 (2d ed. 2002) (describing the *Grinnell* formulation as "not helpful" and "sometimes misleading").

[3] 475 U.S. 585, 597 (1985) (quoting trial court).

[4] *See generally* Mark S. Popofsky, *Defining Exclusionary Conduct: Section 2, the Rule of Reason, and the Unifying Principle Underlying Antitrust Rules*, 73 ANTITRUST L.J. 435, 439 (2006) ("[A]dvocates of rival Section 2 tests treat *Aspen* as a mirror, reflecting support for their favored doctrine.").

[5] *See, e.g.*, Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 409 (2004) (not adopting a specific test and characterizing *Aspen Skiing* as at the outer boundaries of section 2 enforcement without further explanation); Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447 (1993); *see also* United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945).

[6] *Compare, e.g.*, Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 903 (9th Cir. 2008) (applying a cost-based test to bundled discounting), *with* LePage's Inc. v. 3M, 324 F.3d 141, 155 (3d Cir. 2003) (en banc) (condemning bundled discounting practices without applying a cost-based test).

effects—making it hard to distinguish conduct that should be deemed unlawful from conduct that should not.

- Because competitive and exclusionary conduct often look alike, courts and enforcers need to be concerned with both underdeterrence and overdeterrence.
- Standards for applying section 2 should take into account the costs, including error and administrative costs, associated with courts and enforcers applying those standards in individual cases and businesses applying them in their own day-to-day decision making.

While there is general consensus that clearer and more predictable standards are desirable, legal scholarship and the record from the hearings suggest far less consensus on what those standards should be.[7] Some advocate a single test for analyzing all, or substantially all, conduct challenged under section 2, but there is no agreement on what that single test should be.[8] Others maintain that no unitary test can be applied to the broad range of conduct that may be subject to challenge under section 2.[9] Some urge development of specific tests or safe harbors for specific categories of conduct.[10]

[7] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Tying Hr'g Tr. 59, Nov. 1, 2006 (Popofsky) ("[T]here is a holy war raging over the appropriate liability standard under Section 2 generally."); Popofsky, *supra* note 4, at 435 ("The antitrust community is engaged in a renewed debate over the legal test for exclusionary conduct under Section 2 of the Sherman Act.").

[8] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Conduct as Related to Competition Hr'g Tr. 31, May 8, 2007 [hereinafter May 8 Hr'g Tr.] (Pitofsky) (advocating a framework whereby "procompetitive justifications" are balanced against "anticompetitive effects"); Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 330 (2003) (advocating rules of per se legality and illegality based on monopolist's efficiency); A. Douglas Melamed, *Exclusive Dealing Agreements and Other Exclusionary Conduct—Are There Unifying Principles?*, 73 ANTITRUST L.J. 375, 389 (2006) (advocating a "test" under which "conduct is anticompetitive if, but only if, it makes no business sense or is unprofitable for the defendant but for the exclusion of rivals and resulting supra–competitive recoupment"); Mark R. Patterson, *The Sacrifice of Profits in Non-Price Predation*, ANTITRUST, Fall 2003, at 37, 43 (stating that "the sacrifice-of-profits test provides a desirable approach both for litigation and business planning"); Steven C. Salop, *Exclusionary Conduct, Effect on Consumers, and the Flawed Profit-Sacrifice Standard*, 73 ANTITRUST L.J. 311, 341 (2006) (proposing a standard where "the court would evaluate the likelihood and magnitude of expected consumer benefits or harms based on the information reasonably available at the time that the conduct was undertaken").

[9] *See, e.g.*, ANTITRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATIONS 91 (2007), *available at* http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf ("Many commentators are skeptical that any one legal standard should be used to evaluate the wide variety of different types of conduct that may be challenged under Section 2."); May 8 Hr'g Tr., *supra* note 8, at 21 (Rule) ("The problem with the unitary standards is . . . [that] they presume a . . . capability of regulators and enforcers and courts to distinguish efficient from inefficient conduct that just doesn't exist."); Sherman Act Section 2 Joint Hearing: Section 2 Policy Issues Session Hr'g Tr. 12, May 1, 2007 [hereinafter May 1 Hr'g Tr.] (McDavid) (recommending that the search for a single standard be abandoned and noting that antitrust is "very fact-specific"); *id.* at 56 (Jacobson) ("I think the consensus today is that there cannot be a single test for all aspects of [section 2] conduct . . . ."); Sherman Act Section 2 Joint Hearing: Monopoly Power Session Hr'g Tr. 172, Mar. 7, 2007 (Sims) (stating that there is no consensus for section 2 approaches except to pay attention to the facts); Sherman Act Section 2 Joint Hearing: International Issues Session Hr'g Tr. 15, Sept. 12, 2006 [hereinafter Sept. 12 Hr'g Tr.] (Lowe) ("[O]ne test may not be the final answer to the analysis we need to carry out. There may be several tests which have been proposed which are relevant to a particular case."); *id.* at 101–02 (Addy) (asserting that "we should [not] expect the kind of detail or precision that some proponents might advocate" and that "there is no Holy Grail").

[10] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Business Testimony Session Hr'g Tr. 95–96, Feb. 13, 2007 [hereinafter Feb. 13 Hr'g Tr.] (Stern) (stating that meaningful safe harbors that clarify what is clearly legal and not questionable should be developed); Sherman Act Section 2 Joint Hearing: Academic Testimony Session Hr'g Tr. 161–62, Jan. 31, 2007 [hereinafter Jan. 31 Hr'g Tr.] (Gilbert) (advocating different standards for different types of behavior); *id.* at 117 (Bloom) ("[W]e may need more than one test . . . to cover different types of exclusionary conduct."); *id.* at 130 (Rill) (advocating that conduct safe harbors be developed). *But cf.* Melamed, *supra* note 8, at 384 (contending that different rules for different types of conduct "would be problematic in practice" because "[d]ifferent rules . . . would inevitably invite disputes about how the conduct at issue should be categorized").

This chapter first discusses the allocation of burdens of production and proof in section 2 cases, an important issue no matter the substantive test adopted. The chapter then turns to five tests that have been proposed as a general standard for assessing whether conduct is anticompetitive under section 2—namely, (1) the effects-balancing test, (2) the profit-sacrifice test, (3) the no-economic-sense test, (4) the equally efficient competitor test, and (5) the disproportionality test.[11] The chapter briefly describes the tests and assesses the relative advantages and disadvantages of each against modern Supreme Court section 2 jurisprudence and the principles set forth in chapter 1.

## II. Allocation of Burdens of Production and Proof

Regardless of the substantive standard applied, the proper allocation of burdens of production and proof is key to facilitating the efficient resolution of cases that are notoriously complex, time consuming, and expensive.[12] As the Supreme Court has observed, "[P]roceeding to antitrust discovery can be expensive" as it sometimes entails "'a potentially massive factual controversy.'"[13] Allocating burdens can enable courts more quickly to dispose of non-meritorious cases and sometimes to identify violations.[14]

Excessively lengthy antitrust litigation helps neither businesses nor consumers. As one commentator observed, it can be impossible to obtain effective relief in a matter that drags on for years and years before resolution: "As litigation stretches on—perhaps with no interim relief—the competitive moment that brought forth the rival may be lost, and along with it the prospect of new or improved products and services."[15] Lengthy litigation of non-meritorious claims can have similarly harmful competitive effects by restraining innovative or efficient conduct.

Noting the costs and complexities of section 2 litigation, several panelists voiced concern about the process of deciding such cases. One panelist stressed the need for a "sound analytical framework" for deciding section 2 claims.[16] Another noted that merely "punt[ing] issues downstream to juries . . . leads to forced settlement because people are risk averse and don't want to go to trial."[17] Another expressed the view that pressure to settle can lead to "a lot of hidden false positives . . . particularly in the private cases."[18]

One commentator explains:

> To be effective, antitrust rules must be "operative," i.e., they must work reasonably well in the context of litigation where they are ultimately going to be applied. That means they must be structured to take into account such basic litigation features as due process, burdens of pleading, production, and proof, and rules of evidence. Rules that make perfect sense as a matter of economics may not make sense from the point of view of procedure.[19]

[11] The chapter focuses on five prominent tests, although others have been proposed. *See, e.g.*, Elhauge, *supra* note 8, at 330; Kenneth L. Glazer & Brian R. Henry, *Coercive vs. Incentivizing Conduct: A Way Out of the Section 2 Impasse?*, ANTITRUST, Fall 2003, at 45, 47–48.

[12] *See* Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1, 17 (1984); Andrew I. Gavil, *Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance*, 72 ANTITRUST L.J. 3, 64 (2004).

[13] Bell Atl. Corp. v. Twombly, 127 S. Ct. 1955, 1967 (2007) (quoting Associated Gen. Contractors of Cal., Inc. v. Carpenters, 459 U.S. 519, 528 n.17 (1983)); *see also, e.g.*, Feb. 13 Tr., *supra* note 10, at 209 (Sewell) (noting that firms "expend[] an enormous amount of resources, legal resources, trying to figure out" what is illegal under section 2).

[14] *See* HERBERT HOVENKAMP, THE ANTITRUST ENTERPRISE: PRINCIPLE AND EXECUTION 108 (2005) (observing that a "staged inquiry is particularly conducive to summary judgment or other early termination of the dispute").

[15] Gavil, *supra* note 12, at 80.

[16] May 1 Tr., *supra* note 9, at 17 (Kolasky).

[17] Sherman Act Section 2 Joint Hearing: Loyalty Discounts Session Hr'g Tr. 186, Nov. 29, 2006 [hereinafter Nov. 29 Hr'g Tr.] (Crane).

[18] Jan. 31 Tr., *supra* note 10, at 73–74 (Shelanski).

[19] Gavil, *supra* note 12, at 66; *cf.* HOVENKAMP, *supra* note 14, at 105 ("If the rule of reason is to be administered rationally through the costly antitrust enterprise, it should never be an unfocused inquiry into all aspects of a defendant's business.").

A proper allocation of the burdens can help "limit the cases that proceed to discovery and trial" and "structure the proceedings in the rest, leading courts to focus on the most important issues."[20]

The D.C. Circuit outlined a useful procedural framework for distinguishing exclusionary from competitive acts. First, "[T]o be condemned as exclusionary, a monopolist's act must have an 'anticompetitive effect.' That is, it must harm the competitive *process* and thereby harm consumers. . . . [And] the plaintiff, on whom the burden of proof of course rests, must demonstrate that the monopolist's conduct indeed has the requisite anticompetitive effect."[21] Second, "[I]f a plaintiff successfully establishes a prima facie case under § 2 by demonstrating anticompetitive effect, then the monopolist may proffer a [nonpretextual] 'procompetitive justification' for its conduct."[22] Third, "[I]f the monopolist's procompetitive justification stands unrebutted, then the plaintiff must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit."[23]

Requiring plaintiffs to make a showing of harm to the competitive process at the outset facilitates the disposition of non-meritorious claims. One commentator describes this type of requirement as an "important initial filter[]"[24] that can "weed[] out either at the pleading stage or the summary judgment stage"[25] meritless claims. Likewise, requiring a defendant, upon a prima facie showing of harm to the competitive process, to come forward with a nonpretextual justification for its conduct enables courts and juries to condemn patently anticompetitive conduct without any weighing of offsetting effects.[26]

These steps can spare courts and juries difficult questions. In many cases, the plaintiff will not be able to make a plausible showing of harm to the competitive process, or the defendant will not be able to muster a plausible efficiency-enhancing rationale for its conduct, meaning that the court or jury can readily determine whether or not the conduct is anticompetitive. In effect, this approach "strip[s] away those explanations that are implausible or unproven until we have a 'core' left that characterizes the practice as pro- or anticompetitive."[27]

The Department urges courts to apply such a procedural framework and to consider litigation costs and the substantive goals of antitrust when allocating the burdens of proof and production.

## III. Proposed General Standards

If the allegation of competitive harm is not meritless but the conduct is not patently anticompetitive, the standard for evaluating the conduct plays a crucial role in ensuring that section 2 promotes competition and consumer welfare. This section discusses five general tests that have been proposed for determining whether or not challenged conduct is anticompetitive.

### A. Effects-Balancing Test

Given the objective of identifying conduct that causes harm to the competitive process, it is natural that some commentators and courts favor applying an effects-balancing test that focuses on a challenged practice's "overall impact on consumers" or net effects on consumer welfare.[28] The test asks whether

[20] Easterbrook, *supra* note 12, at 18.

[21] United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001) (en banc) (per curiam) (citations omitted) (emphasis in original).

[22] *Id.* at 59.

[23] *Id.*

[24] Gavil, *supra* note 12, at 62.

[25] *Id.* at 75; *see also* Easterbrook, *supra* note 12, at 17 (endorsing "filters" that "help to screen out cases in which the risk of loss to consumers and the economy is sufficiently small that there is no need of extended inquiry and significant risk that inquiry would lead to wrongful condemnation or to the deterrence of competitive activity as firms try to steer clear of the danger zone").

[26] *Cf.* Gavil, *supra* note 12, at 80.

[27] HOVENKAMP, *supra* note 14, at 108.

[28] Salop, *supra* note 8, at 330. It is not always clear whether the consumer-welfare test focuses only on consumer surplus or includes both consumer and producer surplus. *See* Sherman Act Section 2 Joint

particular conduct "reduces competition without creating a sufficient improvement in performance to fully offset these potential adverse effect[s] on prices and thereby prevent consumer harm."[29] At its core, the test entails quantifying and weighing procompetitive and anticompetitive effects of the challenged conduct.

The effects-balancing test makes illegal all conduct by which a monopolist acquires or maintains monopoly power where the conduct causes net harm to consumers. The effects-balancing test has the advantage of focusing the exclusionary-conduct analysis on the impact on consumers, a key concern of Sherman Act jurisprudence.[30]

Critics of this test contend that it is not easily administrable and is inconsistent with the Supreme Court's recent section 2 jurisprudence.[31] Administrability is crucial, as then-Judge Breyer explained in *Barry Wright Corp. v. ITT Grinnell Corp.*: "Rules 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."[32]

Recent Supreme Court decisions have reflected then-Judge Breyer's appreciation of the need to adopt standards that reasonably identify truly anticompetitive conduct, minimizing administrative costs and risk of Type I and Type II errors that would ultimately undermine effective antitrust enforcement. The Supreme Court has realized that a search for every possible anticompetitive effect can do more harm than good. The Court's predatory-pricing test in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, for example, provides a safe harbor for pricing above a relevant measure of cost, even though the Court explicitly recognized a possibility of such pricing causing consumer harm through the exclusion of rivals.[33] Similarly, in *Trinko*, the Court observed that violations of certain sharing duties imposed by statute may be "'beyond the practical ability of a judicial tribunal to control,'" even where enforcement of such duties might increase competition in the short run.[34]

The effects-balancing test confronts a court with the administrative challenge of conducting an open-ended measuring of effects that includes comparing the existing world with a hypothetical world that is subject to debate. These administrability problems include limitations on both the ability of economists accurately to measure the net consumer-welfare effects of particular conduct[35] and the ability of judges and juries to evaluate this evidence.[36]

Hearing: Predatory Pricing Hr'g Tr. 178–190, June 22, 2006 [hereinafter June 22 Hr'g Tr.]; *id.* at 180 (Salop) ("I think by consumer welfare I mean true consumer welfare."); *id.* at 184 (Salop) (noting that "what the Supreme Court meant by consumer welfare is total welfare").

[29] Salop, *supra* note 8, at 330.

[30] *See id.* at 330–32.

[31] *See, e.g.*, Popofsky, *supra* note 4, at 464 (stating that the effects-balancing test "cannot be reconciled with certain . . . Section 2 rules").

[32] 724 F.2d 227, 234 (1983).

[33] 509 U.S. 209, 223 (1993).

[34] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 414 (2004) (quoting *Brooke Group*, 509 U.S. at 223); *see also* Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 127 S. Ct. 1069, 1078 (2007) (holding that, while higher bidding for inputs may potentially have exclusionary effects even where it does not result in below-cost output pricing, such effects are "'beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate' procompetitive conduct" (quoting *Brooke Group*, 509 U.S. at 223)).

[35] *See, e.g.*, Gregory J. Werden, *Identifying Exclusionary Conduct Under Section 2: The "No Economic Sense" Test*, 73 ANTITRUST L.J. 413, 431–32 (2006).

[36] *See, e.g.*, Elhauge, *supra* note 8, at 317 (The "open-ended balancing inquiry" required by an effects-balancing test, when performed by "antitrust judges and juries[,] would often be inaccurate, hard to predict years in advance when the business decision must be made, and too costly to litigate."); Melamed, *supra* note 8, at 386–87 (noting that the effects-balancing test would "pose a daunting challenge to any decision maker"); Popofsky, *supra* note 4, at 465 (observing that "the inquiry adjudicators need to make" under the effects-balancing test "is too difficult"); Werden, *supra* note 35, at 431–32 ("Reliance on the jury system assures that the consumer-welfare test would result in a high incidence of false positive findings of exclusionary conduct.").

Indeed, several panelists and commentators have pointed out that, in practice, courts do not engage in the precise balancing called for by the effects-balancing test. One panelist explained that, "when you look at the decisions, the courts never reach [a] final balancing stage."[37] Another panelist agreed, stating that no "court has ever written an opinion saying, now that it is all over, we find that there are these harms and these efficiencies and we are now going to weigh them and we are going to choose between the two."[38] Similarly, in commenting on the D.C. Circuit's *Microsoft* decision,[39] another asserts that the court, "while using the language of comparing effects, in fact *avoided* that inquiry."[40]

The effects-balancing test also may lead courts to focus too much on static, short-run consumer effects. Because dynamic effects are often more difficult to assess than static effects, the effects-balancing test may well be misapplied to condemn conduct with dynamic effects that benefit consumers significantly. As one commentator notes, "Even if economists could perfectly sort out the relatively short-run economic consequences of all marketplace conduct, they still could not accurately account for the important long-term effects of any remedial action on incentives for innovation and risk-taking—the twin engines of our prosperity."[41] To the extent it is applied in a manner that focuses more on short-run consumer effects of specific conduct, the effects-balancing test may ultimately harm, rather than benefit, consumers in the long run.

Further, critics note that the complexity of administering the effects-balancing test would make it difficult for firms to determine at the outset whether specific conduct would violate section 2, thereby potentially chilling pro-competitive conduct and reducing consumer welfare.[42] Moreover, a legal rule under which every action of a monopolist must be scrutinized for net consumer-welfare effects threatens to chill a monopolist's incentives to engage in procompetitive conduct out of fear of antitrust investigation, litigation, or even mistaken liability—again, potentially harming consumer welfare.

Given the open-ended nature of the effects-balancing test and the inherent uncertainty for businesses in predicting its outcome, the Department does not believe it should be the general test for analyzing conduct under section 2. Although consumer welfare should remain the goal of enforcement efforts, that objective likely is better served by a standard that takes better account of administrative costs and the benefits of dynamic competition for economic growth.

**The Department does not believe that the effects-balancing test should be the general test for analyzing conduct under section 2.**

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*But see* Salop, *supra* note 8, at 314 ("Although [the consumer- welfare] standard has been criticized, it can be implemented without causing excessive false positives that might lead to over-deterrence or a welfare-reducing diminution in innovation incentives.").

[37] May 1 Hr'g Tr., *supra* note 9, at 60 (Kolasky).

[38] *Id.* at 103 (Krattenmaker); *see also* May 8 Hr'g Tr., *supra* note 8, at 30 (Melamed) ("[T]o talk about . . . balancing as a solution to the problem where you have both benefit and harm . . . is nonsense. And I don't think any court does it."); *id.* at 32 (Rule) (stating that balancing "becomes infinitely more difficult . . . in a Section 2 context for a variety of reasons"); May 1 Hr'g Tr., *supra* note 9, at 81 (Calkins) ("[Y]ou never get to the last step, and so it is not really a balancing."). *But see* May 8 Hr'g Tr., *supra* note 8, at 31 (Pitofsky) ("The balancing test is the baseline of all antitrust. . . . Why do you single out Section 2 of the Sherman Act as an area where balancing is nonsense?").

[39] United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001) (en banc) (per curiam).

[40] Popofsky, *supra* note 4, at 445 (emphasis in original).

[41] *Id.* at 431–32.

[42] *See, e.g.*, Sherman Act Section 2 Joint Hearing: Refusals to Deal Session Hr'g Tr. 46, July 18, 2006 [hereinafter July 18 Hr'g Tr.] (Pate) ("[W]hile a general balancing test is flexible . . . it is inherently lacking in any objective content that businesses can apply in a predictable manner to make their decisions."); Melamed, *supra* note 8, at 387 (stating that a "static market-wide balancing test" would "place a costly and often impossible burden on the defendant when deciding in real time how to conduct its business").

### B. Profit-Sacrifice and No-Economic-Sense Tests

Some commentators favor reducing the uncertainties, and thus perceived chilling effects, surrounding the application of an effects-balancing test by applying tests that do away with the need for that balancing altogether. The profit-sacrifice and no-economic-sense tests are two prominent examples. These tests are often discussed together and commentary is not always clear as to their precise definitions. Indeed, some appear to equate them, while others believe they are different. The Department does not consider them to be equivalent and sets forth below how these tests are sometimes described and how they differ.

Generally, a profit-sacrifice test asks whether the scrutinized conduct is more profitable in the short run than any other conduct the firm could have engaged in that did not have the same (or greater) exclusionary effects. If the conduct is not more profitable, the firm sacrificed short-run profits and might have been investing in an exclusionary scheme, seeking to secure monopoly power and recoup the foregone profits later.

One can apply a version of the no-economic-sense test in a similar fashion, comparing the non-exclusionary profits from the conduct to the profits the firm would have earned from alternative, legal conduct in which it would have engaged (the "but-for" scenario).[43] If the non-exclusionary profits are greater, the conduct would make economic sense without exclusionary effects and thus be legal; if the non-exclusionary profits are less, the conduct would not make economic sense and thus potentially be illegal.

However, as often described, another variation of the no-economic-sense test asks whether the conduct in question contributed any profit to the firm apart from its exclusionary effect. As long as the conduct is profitable apart from its exclusionary effect, it would pass this variation of the no-economic-sense test, regardless of whether any other conduct would have been more profitable or the extent of any harm to competition.

The profit-sacrifice and no-economic-sense tests seek to establish objective standards by which to identify conduct that is likely to damage the competitive process, as opposed to merely aggressive competition. The tests draw on the Supreme Court's predatory-pricing jurisprudence.[44] A cornerstone of those cases is a 1975 law review article by Professors Areeda and Turner, in which they argued that "predation in any meaningful sense cannot exist unless there is a temporary sacrifice of net revenues in the expectation of greater future gains."[45]

That concept, and subsequent academic commentary suggesting that an action's likely economic effects are key to assessing liability under section 2,[46] played a significant role in several decisions construing section 2, including *Aspen Skiing*,[47] *Matsushita Industrial*

[43] *See* Werden, *supra* note 35, 420–22.

[44] *Id.* at 16–17.

[45] Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697, 698 (1975); *see also id.* (asserting that "the classically-feared case of predation has been the deliberate sacrifice of present revenues for the purpose of driving rivals out of the market and then recouping the losses through higher profits earned in the absence of competition").

[46] *See, e.g.*, ROBERT H. BORK, THE ANTITRUST PARADOX 144 (1978) ("Predation may be defined . . . as a firm's deliberate aggression against one or more rivals through the employment of business practices that would not be considered profit maximizing except for the expectation either that (1) rivals will be driven from the market, leaving the predator with a market share sufficient to command monopoly profits, or (2) rivals will be chastened sufficiently to abandon competitive behavior the predator finds inconvenient or threatening."); Janusz A. Ordover & Robert D. Willig, *An Economic Definition of Predation: Pricing and Product Innovation*, 91 YALE L.J. 8, 9–10 (1981) ("[P]redatory behavior is a response to a rival that sacrifices part of the profit that could be earned under competitive circumstances, were the rival to remain viable, in order to induce exit and gain consequent additional monopoly profit.").

[47] Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 608 (1985) (noting that defendant "elected to forgo . . . short-term benefits because it was more interested in reducing competition in the Aspen market over the long run").

*Co., Ltd. v. Zenith Radio Corp.*,[48] *Brooke Group*,[49] and several lower court decisions.[50] For instance, pricing below cost is an objectively measurable standard and indicates that the pricing makes no economic sense in the short term and, accordingly, is likely to be serving other ends, which might include exclusion of competitors. Similarly, the *Trinko* Court, while not expressly adopting the no-economic-sense test, identified the *Aspen Skiing* defendant's "willingness to forsake short-term profits to achieve an anticompetitive end" as a key element of the liability finding.[51]

Although, as discussed above, there are variations on the profit-sacrifice and no-economic-sense tests, proponents of all variations maintain that the tests are consistent with the Supreme Court's long-standing emphasis on protecting the competitive process and avoiding the chilling of procompetitive conduct.[52] For instance, while acknowledging that the tests have been "criticized by numerous commentators who are concerned that [they] will result in false negatives,"[53] one proponent nevertheless contends that the policy tradeoffs are justified:

> The sacrifice test does not purport to condemn all conduct that might create market power or reduce economic welfare. Rather, the test rests on the judgment that market-wide balancing tests, which in theory could condemn all welfare-reducing conduct, will in practice prove to be an inferior legal standard because of their greater difficulty in administration and their perverse incentive effects.[54]

Supporters of the tests also recommend them on grounds that firms can use them to assess the legality of proposed actions before acting and that courts should be able to apply them relatively easily.[55] Even supporters

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[48] 475 U.S. 574, 588–89 (1986) (explaining that an "agreement to price below the competitive level requires the conspirators to forgo profits that free competition would offer them" in the hope of obtaining "later monopoly profits").

[49] 509 U.S. 209, 224 (1993) (holding that low prices are not illegal under section 2 absent "a dangerous probability[] of recouping [the] investment in below-cost prices").

[50] *See, e.g.*, Covad Commc'ns Co. v. Bell Atl. Corp., 398 F.3d 666, 675 (D.C. Cir. 2005) ("[I]n order to prevail upon [a refusal-to-deal] claim [plaintiff] will have to prove [defendant's] refusal to deal caused [defendant] short-term economic loss."); Morris Commc'ns Corp. v. PGA Tour, Inc., 364 F.3d 1288, 1295 (11th Cir. 2004) ("[A]nticompetitive conduct . . . is conduct without a legitimate business purpose that makes sense only because it eliminates competition." (internal quotation marks omitted) (quoting Gen. Indus. Corp. v. Hartz Mountain Corp., 810 F.2d 795, 804 (8th Circuit 1987))); Neumann v. Reinforced Earth Co., 786 F.2d 424, 427 (D.C. Cir. 1986) ("[P]redation involves aggression against business rivals through the use of business practices that would not be considered profit maximizing except for the expectation that (1) actual rivals will be driven from the market, or the entry of potential rivals blocked or delayed, so that the predator will gain or retain a market share sufficient to command monopoly profits, or (2) rivals will be chastened sufficiently to abandon competitive behavior the predator finds threatening to its realization of monopoly profits."); William Inglis & Sons Baking Co. v. ITT Cont'l Baking Co., 668 F.2d 1014, 1030–31 (9th Cir. 1981) (stating that, in order to violate section 2, conduct "must be such that its anticipated benefits were dependent upon its tendency to discipline or eliminate competition and thereby enhance the firm's long-term ability to reap the benefits of monopoly power").

[51] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 409 (2004).

[52] *See, e.g.*, ANTITRUST MODERNIZATION COMM'N, *supra* note 9, at 91–92; *General Approaches to Defining Abusive/Monopolistic Practices—Roundtable, in* 2006 ANNUAL PROCEEDINGS OF THE FORDHAM COMPETITION LAW INSTITUTE 577–79 (Barry E. Hawk ed., 2007) (Werden).

[53] A. Douglas Melamed, *Exclusionary Conduct Under the Antitrust Laws: Balancing, Sacrifice, and Refusals to Deal*, 20 BERKELEY TECH. L.J. 1247, 1257 (2005).

[54] *Id.*; *see also* Werden, *supra* note 35, at 433 ("The no economic sense test is predicated on the proposition that some potentially harmful conduct must be tolerated to avoid even greater harms from chilling risk taking and aggressively competitive conduct.").

[55] *See* Jan. 31 Hr'g Tr., *supra* note 10, at 135 (Rubinfeld) (asserting that the profit sacrifice test is "easier to operationalize"); July 18 Hr'g Tr., *supra* note 42, at 32 (Pate) (stating that "some variation of a price-cost comparison . . . is going to be necessary if objectivity is going to be brought to the inquiry"); Melamed, *supra* note 8, at 393 ("Perhaps most important, the sacrifice test provides simple, effective, and meaningful guidance to firms so that they will know how to avoid antitrust liability without steering clear of procompetitive conduct."); Werden, *supra* note 35, at 433.

acknowledge, however, that these tests can be difficult to apply in some circumstances, for instance "in cases involving simultaneous benefits for the defendant and cost increases for rivals."[56]

Some panelists criticized these tests for focusing only indirectly on consumers and preferred that section 2 be construed to focus directly on consumer welfare.[57] Other panelists made similar points, emphasizing the potential of these tests to result in false negatives, allowing conduct that harms consumers to escape liability under section 2.[58]

The profit-sacrifice test also has been criticized for its potential to result in false positives, condemning procompetitive investments and product innovation. Almost all substantial investments—from building a new factory to new-product development—involve a short-term sacrifice of current revenue in expectation of future increased revenues resulting from taking business from competitors. The test is criticized because it "does not adequately distinguish anticompetitive 'sacrifice' from procompetitive investment"[59] and may condemn clearly procompetitive conduct.[60] As one commentator

[56] Melamed, *supra* note 53, at 1261; *see also* Werden, *supra* note 35, at 421 ("The utility of the no economic sense test ultimately is apt to vary, depending mainly on the feasibility of determining whether the challenged conduct would make no economic sense but for its tendency to eliminate competition. That determination should be feasible in the vast majority of cases, but it might not be if the conduct generates legitimate profits as well as profits from eliminating competition.").

[57] *See, e.g.*, May 1 Hr'g Tr., *supra* note 9, at 67 (Kolasky) (stating that the profit-sacrifice test "focuses . . . too much attention on whether the conduct makes sense from the standpoint of the alleged monopolist as opposed to what is its effect on the consumer"); Sherman Act Section 2 Joint Hearing: Business Testimony Session Hr'g Tr. 35, Jan. 30, 2007 (Edlin).

[58] *See, e.g.*, May 1 Hr'g Tr., *supra* note 9, at 77 (Baker) ("If the profit sacrifice or no economic sense test differs from the reasonableness analysis, it is doing so in order . . . to put a thumb on the scales in favor of defendants."); July 18 Hr'g Tr., *supra* note 42, at 25 (Pitofsky) (stating that he is "uncomfortable" with the profit-sacrifice test because it focuses on the monopolist rather than the consumer); *see also* Gavil, *supra* note 12, at 71 ("As an economic matter, 'sacrifice' is not relevant either to the defendant's market power or the fact that its conduct resulted in actual exclusion or consumer harm."); Jonathan M. Jacobson & Scott A. Sher, *"No Economic Sense" Makes No Sense for Exclusive Dealing*, 73 ANTITRUST L.J. 779, 786 (2006) ("[M]ost importantly, the no economic sense and profit sacrifice tests still do not ask the correct question—that is, whether the practice is likely to aid consumers or to hurt them."); Salop, *supra* note 8, at 345–46, 357–63 (stating that the profit-sacrifice test is a highly imperfect and generally biased predictor of the impact of the conduct on competition and consumer welfare). *But see* Werden, *supra* note 35, at 428 ("Theoretical possibilities [of false negatives] should be given little weight in formulating antitrust policy or any other legal rules of general application.").

[59] Herbert Hovenkamp, Antitrust and the Dominant Firm: Where Do We Stand? 12 (n.d.) (unpublished manuscript), *available at* http://www.ftc.gov/os/comments/section2hearings/hovenkamppaper.pdf ("One particular problem with sacrifice tests is that most substantial investments involve a short term 'sacrifice' of dollars in anticipation of increased revenue at some future point. . . . Likewise, product innovations are always costly to the defendant, and their success may very well depend on their ability to exclude rivals from the market . . . ."); *cf.* Carl Shapiro, Exclusionary Conduct, Testimony Before the Antitrust Modernization Commission 4 (Sept. 29, 2005), *available at* http://govinfo.library.unt.edu/amc/commission_hearings/pdf/Shapiro_Statement.pdf (endorsing a safe harbor for "investment in new and superior production capacity" and "unadorned product improvement" even though such investment could in theory deter entry by rivals or induce the exit of rivals, thereby leading to higher prices).

[60] *See, e.g.*, Jan. 31 Hr'g Tr., *supra* note 10, 113–14 (Gilbert) ("[A] profit sacrifice test . . . doesn't . . . make any sense to innovation" because "innovation almost always involves a profit sacrifice" which is called "investing in research and development. . . . [Moreover], if [innovation] really works, [it] probably excludes competitors. . . . [P]roducing a really good mousetrap" means that "other mousetraps can't compete."); Elhauge, *supra* note 8, at 274 (noting that the sacrifice test fails for the fundamental reason that sacrificing short-term profits to make the sort of investments that enable one to destroy one's rivals is ordinarily not a sign of evil but the mark of capitalist virtue); Popofsky, *supra* note 4, at 462 (noting that the profit-sacrifice test "could deem unlawful conduct that impedes rivals only because it improves the attractiveness of the defendant's product and has no other exclusionary property"); Salop, *supra* note 8, at 314 (observing that "the profit-sacrifice standard may well be more likely to condemn a cost-reducing investment that leads to market power than would the consumer welfare effect standard").

puts it,

> [P]ublic policy should encourage firms that want to invest in activities that consumers value in order to gain future sales from their rivals. However, because such actions by definition reduce present profits, a blind application of a "profit sacrifice" test could condemn almost any competitive behavior. When a test could potentially challenge a wide array of core competitive behaviors, it becomes dangerous.[61]

In addition, although these tests are based in part on their purported ease of administration, critics claim that they are difficult to implement in practice.[62] For instance, some critics maintain that the tests are inappropriate for analyzing exclusive-dealing arrangements, which make economic sense for the defendant "precisely because they lessen competition by rivals for the affected business."[63] These critics contend that there is no practical way to separate the economic benefits to a defendant from the exclusionary impact on rivals.[64] Another contends that these tests conflict with the sham-litigation doctrine; costly litigation might be permissible under the sham-litigation doctrine yet fail the no-economic-sense or profit-sacrifice tests.[65] Still others express concern that some misleading and deceptive conduct with no efficiency justification might involve little or no profit sacrifice.[66]

Yet another potential problem with these tests is that they may open the door to plaintiffs hypothesizing any number of alternative courses of action that may, especially with the benefit of hindsight, have been more profitable for defendant. However, there may be legitimate reasons why a firm does not pursue the most profitable course of action, including simple unawareness of the options. No defendant should be required to show that it maximized profits among all conceivable choices. Hinging antitrust liability on such second guessing raises serious concerns that such a standard would undermine rather than promote the goal of economic growth and increased consumer welfare.

The Department believes that a profit-sacrifice test that asks whether conduct is more profitable in the short run than other less-exclusionary conduct the firm could have undertaken raises serious concerns and should not be the test for section 2 liability.

**The Department believes that a profit-sacrifice test should not be the test for section 2 liability.**

The Department further concludes that the

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[61] Dennis W. Carlton, *Does Antitrust Need to Be Modernized?*, J. ECON. PERSP., Summer 2007, at 155, 170. *But see* Gregory J. Werden, *Identifying Single-Firm Exclusionary Conduct: From Vague Concepts to Administrable Rules*, *in* 2006 FORDHAM COMPETITION LAW INSTITUTE 509, 528 (Barry E. Hawk ed., 2007).

[62] *See, e.g.*, May 1 Hr'g Tr., *supra* note 9, at 69 (Jacobson) ("[I]t is a very, very difficult test to administer."); *id.* at 77 (Baker) (noting "tremendous problems with administrability"); Elhauge, *supra* note 8, at 293 ("The general problem is that the efforts to modify the profit-sacrifice test to avoid its substantive defects necessarily require distinguishing between profits earned desirably (even if it excludes rivals) and profits earned undesirably . . . . Not only does it beg the question of what the criteria of desirability are, it also eliminates any administrability benefit by converting the test from one based on actual profits to one based on the desirability of how those profits were acquired."); Gavil, *supra* note 12, at 55 (contending that "all forms of the but-for test are objectionable on procedural grounds"); Salop, *supra* note 8, at 321, 323 & n.50 (noting that there is debate over the proper way to implement the standard, including what the benchmark should be and how to determine what profits are due to the lessening of competition compared with other causes).

[63] Sherman Act Section 2 Joint Hearing: Exclusive Dealing Session Hr'g Tr. 59, Nov. 15, 2006 (Jacobson).

[64] *See id.*; Jacobson & Sher, *supra* note 58, at 781 (Analyzing exclusive dealing only under a no-economic-sense or profit-sacrifice test is "unintelligible" because "there is no way to separate the economic benefit to the defendant from the exclusionary impact on rivals. The relevant question for exclusive dealing is not whether it 'makes economic sense' (because it so frequently does), but whether, on balance, the specific arrangements at issue are likely to raise prices, reduce output, or otherwise harm consumers. The no economic sense test declines that inquiry.").

[65] *See* Popofsky, *supra* note 4, at 463.

[66] *See, e.g.*, Susan A. Creighton et al., *Cheap Exclusion*, 72 ANTITRUST L.J. 975, 985–86 (2005). *But see* Werden, *supra* note 35, at 425–26.

no-economic-sense test should not be the exclusive test for section 2 liability. As even its proponents recognize, there are difficulties using it in all circumstances. Assessing what portion of an act's anticipated profits is exclusionary, as opposed to non-exclusionary, is apt to be difficult in many cases. Also, the test arguably does not work well for exclusionary conduct involving little cost to defendant. The Department also agrees with those who are concerned that this test might allow businesses too much freedom to engage in conduct likely to harm competition, because conduct could be protected even if it contributed virtually no profits (for example, only $1 of profit) apart from its exclusionary effect but caused tremendous harm to the competitive process. And to the extent that the test relies on a comparison to a but-for scenario, there may be situations where the but-for scenario either is not clear or would take much effort to establish.

Although the Department does not recommend the no-economic-sense test as a necessary condition for liability in all section 2 cases, it believes that the test may sometimes be useful in identifying certain exclusionary conduct.[67] The test can also serve as a valuable counseling tool by highlighting the need for businesses to think carefully about why they are pursuing a particular course of conduct. If conduct does not make economic sense at the time it is undertaken except for its exclusionary effect on competition, it likely will be difficult to defend.[68]

> **Although the Department does not recommend the no-economic-sense test as a necessary condition for liability in all section 2 cases, it believes that the test may sometimes be useful in identifying certain exclusionary conduct.**

### C. Equally Efficient Competitor Test

The equally efficient competitor test addresses some of the concerns with open-ended balancing by requiring that "the challenged practice is likely in the circumstances to exclude from defendant's market an equally or more efficient competitor."[69] If a plaintiff makes such a showing, "defendant can rebut by proving that although it is a monopolist and the challenged practice exclusionary, the practice is, on balance, efficient."[70] This test is based on the rationale "that a firm should not be penalized for having lower costs than its rivals and pricing accordingly."[71]

The equally efficient competitor test also draws on principles similar to those underlying the Supreme Court's predatory-pricing jurisprudence, under which a price is deemed predatory only if it is reasonably calculated to exclude a rival that is at least as efficient as the defendant. As Judge Posner explains, "It would be absurd to require the firm to hold a price umbrella over less efficient entrants. . . . [P]ractices that will exclude only less efficient firms, such as the monopolist's dropping his price nearer to (but not below) his cost, are not actionable, because we want to encourage efficiency."[72] Courts have referred to the

[67] *See* Werden, *supra* note 35, at 418.

[68] *See, e.g.*, May 1 Hr'g Tr., *supra* note 9, at 55 (McDavid) ("[A]s someone who does not think there is a single standard, I do think [profit sacrifice] is [an] appropriate test, but I do not think it is *the* appropriate test." (emphasis added)); *id.* at 64 (Calkins) ("Everybody . . . would agree that the no economic sense question is a good [one]" for an attorney to ask a client, but it is not the only question.); *id.* at 63–64 (Willig) (stating that the no-economic-sense test is another way of asking whether there is a sound business rationale for the conduct); *id.* at 66 (Kolasky) (agreeing that "focusing on profit sacrifice and whether the conduct makes economic sense is . . . a very useful question to ask your clients"); Nov. 29 Hr'g Tr., *supra* note 17, at 202 (Crane) (stating that the no-economic-sense test presents difficulties as a starting point but it makes some sense as a defense); Hovenkamp, *supra* note 59, at 13 (stating that the no-economic-sense test offers a good deal of insight into the question of when aggressive actions by a single firm go too far, but it can lead to erroneous results unless complicating qualifications are added).

[69] RICHARD A. POSNER, ANTITRUST LAW 194–95 (2d ed. 2001).

[70] *Id.* at 195.

[71] Herbert Hovenkamp, *Exclusion and the Sherman Act*, 72 U. CHI. L. REV. 147, 154 (2005).

[72] POSNER, *supra* note 69, at 196.

concept of an equally efficient competitor in a number of cases involving predatory pricing and bundled discounts.[73]

Proponents of this test point out that it is designed to allow firms to take full advantage of their efficiency and protects competition offered by efficient rivals. Moreover, it is useful because it allows firms to assess their conduct at the outset based on something they should be able to evaluate—their own costs.[74]

Critics of the test assert that there are a number of problems with it, however. First, they challenge the basic premise of the test—that section 2 should focus only on the exclusion of competitors as efficient as the alleged monopolist. They contend that "entry [by] even a less efficient rival can stimulate competition and lower prices if an incumbent dominant firm is charging monopoly prices."[75] These critics contend that this is especially true in the case of nascent competition where an equally efficient competitor standard "could lead to false negatives . . . and pose a significant threat of under-deterrence."[76] In markets where competition is just starting to emerge, they contend, it is inappropriate to compare the efficiency of new rivals with that of the monopolist.

Second, the test has also been criticized as difficult to administer. Exactly what constitutes an equally efficient competitor is not always evident, and the test is especially difficult to apply outside the pricing context.[77] For example, it is not clear whether a firm that produces a single product as efficiently as a defendant in a tying case would qualify as an equally efficient competitor if it does not produce the other product(s) involved in the tie. In the multi-product setting, a firm may be equally efficient with respect to one product but not with respect to all the products. A diversified firm may enjoy superior efficiencies in joint production and marketing, as compared to a firm that is arguably as efficient with respect to the one target product. Thus, it may be difficult to conclude that a firm would be equally efficient based on the analysis of only the one targeted product. Moreover, it is difficult to measure and compare efficiencies in multi-product cases where there are joint costs. Similarly, the concept of an equally efficient competitor may be difficult to apply in the exclusive-dealing context, where a firm's efficiency may depend on how it distributes its products.

The Department believes that whether conduct has the potential to exclude, eliminate,

[73] *See, e.g.*, LePage's Inc. v. 3M, 324 F.3d 141, 155 (3d Cir. 2003) (en banc) (observing that "even an equally efficient rival may find it impossible to compensate for lost discounts on products that it does not produce" (quoting AREEDA & HOVENKAMP, *supra* note 2, ¶ 749, at 83–84 (Supp. 2002))); Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039, 1063 (8th Cir. 2000) (stating that above-cost market-share discounts were not unlawful where evidence showed customers switched to competitors offering better discounts); Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 232 (1st Cir. 1983) (Breyer, J.) (noting that, if a firm prices below "avoidable" or "incremental" cost, equally efficient competitors cannot permanently match the price and stay in business); Ortho Diagnostic Sys., Inc. v. Abbott Labs., Inc., 920 F. Supp. 455, 466 (S.D.N.Y. 1996) ("[B]elow-cost pricing, unlike pricing at or above that level, carries with it the threat that the party so engaged will drive equally efficient competitors out of business, thus setting the stage for recoupment at the expense of consumers.").

[74] *See* Sept. 12 Hr'g Tr., *supra* note 9, at 14–15 (Lowe) (acknowledging that efficient competitor is not the only test that can be used and that there may be more than one test applicable to any particular case, but that it is a useful principle because it allows dominant firms to assess their conduct based on their own costs).

[75] Gavil, *supra* note 12, at 59; *see also, e.g.*, June 22 Hr'g Tr., *supra* note 28, at 124 (Brennan) (noting that "inefficient competitors hold down price"); Salop, *supra* note 8, at 328 ("The fundamental problem with applying the equally efficient entrant standard . . . is that the unencumbered (potential) entry of less-efficient competitors often raises consumer welfare.").

[76] Gavil, *supra* note 12, at 61; *see also* June 22 Hr'g Tr., *supra* note 28, at 73 (Bolton) (expressing concern over exclusion of entrants that offer nascent competition); Gavil, *supra* note 12, at 59–61; Hovenkamp, *supra* note 71, at 154.

[77] *See* Nov. 29 Hr'g Tr., *supra* note 17, at 140–41 (Ordover) (observing that "what it means to be an equally efficient competitor is subject to debate"); Melamed, *supra* note 8, at 388 ("[I]t is not clear what it means to exclude only a less-efficient rival, especially when firms and products are heterogenous."); *infra* Chapter 6, Part I(C).

or weaken the competitiveness of equally efficient competitors can be a useful inquiry and may be best suited to particular pricing practices.[78] The Department does not believe that this inquiry leads readily to administrable rules in other contexts, such as tying and exclusive dealing.

**Whether conduct has the potential to exclude, eliminate, or weaken the competitiveness of equally efficient competitors can be a useful inquiry and may be best suited to particular pricing practices.**

### D. Disproportionality Test

In their *Trinko* merits brief, the Department and the FTC advised the Supreme Court that, in the absence of a conduct-specific rule, conduct is anticompetitive under section 2 when it results in "harm to competition" that is "disproportionate to consumer benefits (by providing a superior product, for example) and to the economic benefits to the defendant (aside from benefits that accrue from diminished competition)."[79] Under the disproportionality test, conduct that potentially has both procompetitive and anticompetitive effects is anticompetitive under section 2 if its likely anticompetitive harms substantially outweigh its likely procompetitive benefits.

Properly applied, the disproportionality test reduces the need to precisely balance procompetitive and anticompetitive effects, which, as described above, is a difficult and costly task. In addition, it allows firms the freedom to compete vigorously without undue fear of antitrust liability based on an after-the-fact determination that their conduct had small negative effects on static competition. The disproportionality test reduces the risks of chilling procompetitive conduct but prohibits conduct that will significantly harm competition and consumer welfare.

The justification for this test arises from the principles discussed in chapter 1. It expressly focuses on prohibiting conduct that harms competition, not just individual competitors. It seeks to provide reasonable clarity for firms over a wide range of activity. It seeks to reduce administrative costs. Further, it recognizes that the cost of legal rules that erroneously condemn procompetitive conduct likely will be higher and more persistent than the cost of rules that erroneously exonerate anticompetitive conduct.

To be sure, the disproportionality test is not without its difficulties and may not be easy to apply in some instances. As the enforcement agencies acknowledged in their *Trinko* brief, applying the test "'can be difficult,' because 'the means of illicit exclusion, like the means of legitimate competition, are myriad.'"[80]

Moreover, as one commentator cautions, disproportionality "is hardly an inherently certain formula."[81] In the most difficult cases—those involving significant harm and smaller, but still significant, efficiencies—there is some ambiguity. As one commentator queries, "Is 55–45 percent 'disproportionate' enough? Or do proponents of the test think 75–25 percent is more what they have in mind."[82]

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[78] *See* Hovenkamp, *supra* note 71, at 153 (stating that "[t]he 'equally efficient rival' test has found widespread acceptance in predatory pricing cases"); *see also, e.g.*, Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 223 (1993) (identifying the relative "cost structure" of competitors as a source of the safe harbor for above-cost pricing in predatory-pricing cases); Areeda & Turner, *supra* note 45, at 709–18, 733 (recognizing that, in the predatory-pricing context, prices at or above average variable cost exclude less efficient firms while minimizing the likelihood of excluding equally efficient firms).

[79] Brief for the United States & the Federal Trade Commission as Amici Curiae Supporting Petitioner at 14, Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004) (No. 02-682), *available at* http://www.usdoj.gov/atr/cases/f201000/201048.htm. In the brief, the Department and the FTC also argued that the no-economic-sense test should apply to the specific conduct at issue—a refusal to deal.

[80] *Id.* at 14 (quoting United States v. Microsoft Corp., 253 F.3d 34, 58 (D.C. Cir. 2001) (en banc) (per curiam)).

[81] Gavil, *supra* note 12, at 64.

[82] *Id.*; *see also* Herbert Hovenkamp, *Signposts of Anticompetitive Exclusion: Restraints on Innovation and Economies of Scale*, *in* 2006 FORDHAM COMPETITION LAW INSTITUTE 409, 412 (Barry E. Hawk ed., 2007) (acknowledging that "phrases such as 'disproportionate to the resulting benefits' are marshmallows, covering

This issue is critical. Failure to ensure that courts condemn only conduct that has an adverse effect on competition that is substantially disproportionate to any benefits could render this test tantamount to the burdensome, open-ended effects-balancing test discussed above.

Importantly, the standard likely can be readily applied in a number of cases because either the harm or the benefit is clearly predominant.[83] A trivial benefit should not outweigh substantial anticompetitive effects. At the same time, if the benefits and harms are comparable or close to comparable, then the conduct should be lawful under this test.

The Department recognizes that the disproportionality test imposes a higher burden on a plaintiff than the effects-balancing test. If there is procompetitive justification for the challenged conduct, the test requires the plaintiff to demonstrate that the harm to competition substantially outweighs the benefits. The Department believes that this higher liability threshold is in keeping with the Supreme Court's repeated insistence that section 2 should not be construed in a way that chills procompetitive conduct, yet it also prohibits conduct where significant anticompetitive harm appears likely.

At the same time, as Professor Hovenkamp states in endorsing this test, its "formulation is not intended to give a complete definition of" conduct that is anticompetitive under section 2, but rather is "only a starting point for the development of specific rules for specific types of conduct."[84] The Department believes that conduct-specific tests and, where appropriate, safe harbors enable more effective enforcement while providing businesses with greater certainty, are most administrable by the agencies and courts, and reduce the risk of erroneous determinations. Conduct-specific tests are particularly important because, as Professor Hovenkamp notes, "our level of concern and our administrative capabilities vary considerably among the list of practices that antitrust tribunals have identified as exclusionary."[85] The Department, therefore, will continue to work to develop conduct-specific tests and safe harbors. However, in general, the Department believes that, when a conduct-specific test is not applicable, the disproportionality test is likely the most appropriate test identified to date for evaluating conduct under section 2.

**The Department will continue to work to develop conduct-specific tests and safe harbors. However, in general, the Department believes that, when a conduct-specific test is not applicable, the disproportionality test is likely the most appropriate test identified to date for evaluating conduct under section 2.**

## IV. Conclusion

There was no consensus at the hearings, and there is currently no consensus among commentators, that a single test should be used to define anticompetitive conduct for purposes of section 2. Although many of the proposed tests have virtues, they also have flaws. The Department believes that none currently works well in all situations.

Thus, as will be seen in subsequent chapters, the Department believes different types of conduct warrant different tests, depending upon, among other things, the scope of harm implicated by the practice; the relative costs of false positives, false negatives, and enforcement; the ease of application; and other administrability concerns. An important goal for any test is to identify conduct that harms competition while enabling firms effectively to evaluate the legality of their conduct before it is undertaken.

very much or very little depending on one's ideology or fundamental beliefs").

83 *See* Gavil, *supra* note 12, at 77 ("[M]ost cases will be weeded out before trial for weaknesses related to the plaintiff's assertions with respect to monopoly power or effects. To the extent a small number of cases proceed any further, most will be decided based on lopsided evidence—lots of harm and little or no efficiency, or little harm and substantial efficiency.").

84 Hovenkamp, *supra* note 82, at 412.

85 *Id.*

**The Department believes different types of conduct warrant different tests, depending upon, among other things, the scope of harm implicated by the practice; the relative costs of false positives, false negatives, and enforcement; the ease of application; and other administrability concerns.**

In deciding individual cases, courts would be well served to consider the appropriate allocation of burdens of proof and production. In applying legal standards, courts should determine whether the conduct at issue warrants employing a conduct-specific test. In general, the Department believes that when a conduct-specific test is not utilized, the disproportionality test is likely the most appropriate test identified to date for evaluating conduct under section 2.

Adopting conduct-specific tests is in keeping with modern Supreme Court section 2 jurisprudence. In the last twenty-five years, the Court has adopted conduct-specific tests for both predatory pricing and predatory bidding and has avoided articulating a general test applicable to all section 2 cases. Instead, the Court has set forth unifying principles—including protecting the competitive process and avoiding chilling procompetitive conduct—from which conduct-specific tests can be derived. The Department believes that the Court's approach is appropriate and recommends further development of conduct-specific tests to guide the continued evolution of section 2 jurisprudence.

# The Moist Snuff Case

**CONWOOD COMPANY, L.P. V. UNITED STATES TOBACCO CO.,**
NO. 5:98-CV-108-R (W.D. Ky. filed April 22, 1998)

Jury verdict in favor of plaintiff

JUDGMENT: by Judge Thomas B. Russell the Ct enters jgm in favor of plas Conwood, et al in the amt of $1,050,000,000, treble the jury verdict of $350,000,000 dismissing case (faxed: all counsel) [Entry Date: 3/29/00] (KJI) Modified on 03/29/2000 (Entered: 03/29/2000)

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The following lower court papers in the case may be found on the Unit 16 web page:

Complaint, Conwood Company, L.P. v. United States Tobacco Co., No. 5:98-cv-108-R (W.D. Ky. filed Apr. 22, 1998)

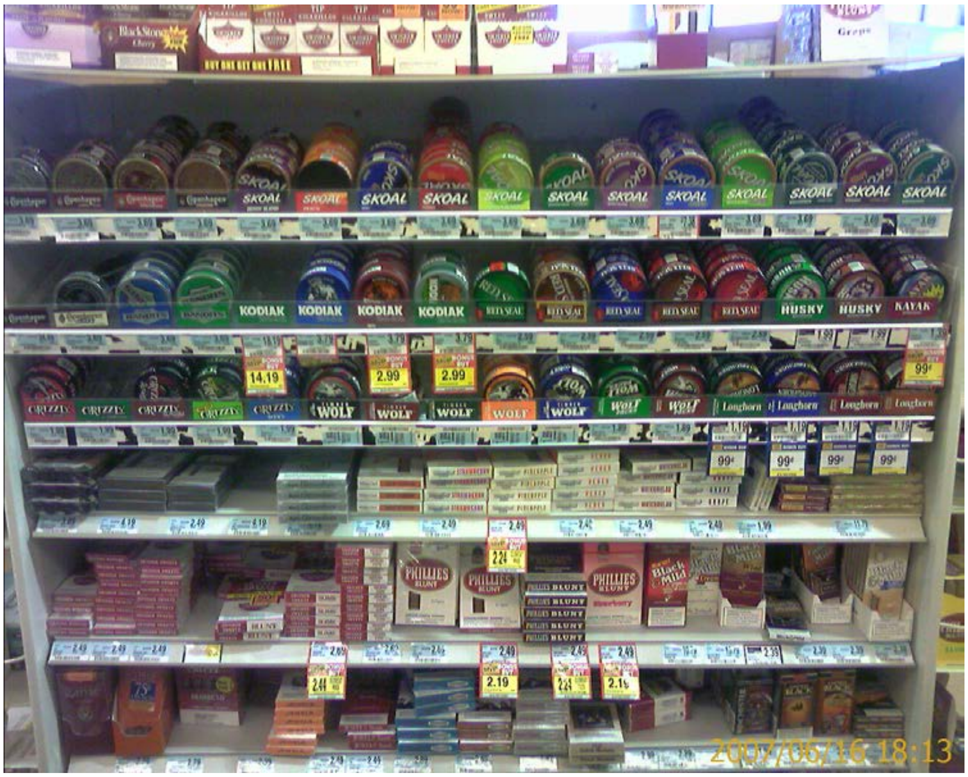
Memorandum, Opinion and Order denying defendant's motion for summary judgment (W.D. Ky. Feb. 17, 2000)

Memorandum Opinion denying defendants' motion for jmol (W.D. Ky. Aug. 10, 2000) (2000 WL 33176054)

Memorandum Opinion granting plaintiff's motion for permanent injunctive relief (W.D. Ky. Aug. 10, 2000) (2000 WL 33176057)

Memorandum Opinion re supersedeas bond (W.D. Ky. Aug. 10, 2000)

Example of a Moist Snuff In-Store Display



*RECOMMENDED FOR FULL-TEXT PUBLICATION*
Pursuant to Sixth Circuit Rule 206

ELECTRONIC CITATION: 2002 FED App. 0171P (6th Cir.)
File Name: 02a0171p.06

# UNITED STATES COURT OF APPEALS

## FOR THE SIXTH CIRCUIT

CONWOOD COMPANY, L.P.; CONWOOD SALES COMPANY, L.P.,
*Plaintiffs-Appellees,*

*v.*

UNITED STATES TOBACCO COMPANY; UNITED STATES TOBACCO SALES AND MARKETING COMPANY, INC.; UNITED STATES TOBACCO MANUFACTURING COMPANY, INC.; UST, INC.,
*Defendants-Appellants.*

No. 00-6267

Appeal from the United States District Court
for the Western District of Kentucky at Paducah.
No. 98-00108—Thomas B. Russell, District Judge.

Argued: November 27, 2001

Decided and Filed: May 15, 2002

Before: CLAY and GILMAN, Circuit Judges; EDGAR, Chief District Judge.*

## COUNSEL

**ARGUED:** Ernest Gellhorn, LAW OFFICE OF ERNEST GELLHORN, Washington, D.C., for Appellants. Mark C. Hansen, KELLOGG, HUBER, HANSEN, TODD & EVANS, Washington, D.C., for Appellees. **ON BRIEF:** Ernest Gellhorn, LAW OFFICE OF ERNEST GELLHORN, Washington, D.C., Neal R. Stoll, James A. Keyte, SKADDEN, ARPS, SLATE, MEAGHER & FLOM, New York, New York, John S. Reed, Ridley M. Sandidge, Jr., Lynn K. Fieldhouse, REED, WEITKAMP, SCHELL & VICE, Louisville, Kentucky, for Appellants. Mark C. Hansen, Neil M. Gorsuch, KELLOGG, HUBER, HANSEN, TODD & EVANS, Washington, D.C., L. Clifford Craig, TAFT, STETTINIUS & HOLLISTER, Cincinnati, Ohio, Richard C. Roberts, WHITLOW, ROBERTS, HOUSTON & STRAUB, Paducah, Kentucky, for Appellees.

## OPINION

CLAY, Circuit Judge. Defendants-Appellants, United States Tobacco Company, United States Tobacco Sales and Marketing Company, Inc., United States Tobacco Manufacturing Company, Inc., and UST, Inc. (herein collectively referred to as "USTC") appeal from the March 29, 2000 order, after trial by jury, entering judgment in favor of Plaintiffs, Conwood Company, L.P. and Conwood Sales Company, L.P. ("Conwood") for Defendants' violations of

* The Honorable R. Allan Edgar, Chief United States District Judge for the Eastern District of Tennessee, sitting by designation.

the Sherman Anti-Trust Act, 15 U.S.C. § 2. Conwood alleged that USTC violated the Act by using its monopoly position to exclude competitors from the moist snuff market. We **AFFIRM**.

## BACKGROUND

### Procedural History

On April 22, 1998, Conwood filed an eight-count complaint against USTC alleging the following causes of action: (1) Unlawful Monopolization, in violation of § 2 of the Sherman Act; (2) Violations of § 43(a) of the Lanham Act; (3) Tortious Interference with contract; (4) Tortious Interference with prospective advantage; (5) Violations of the Kentucky Revised Statute, § 365.050; (6) Product Defamation; (7) Unjust Enrichment; and (8) Conversion/Trover. USTC filed counterclaims for conversion and violations of the Lanham Act and Sherman Act.

In November 1999, USTC moved for summary judgment as to Conwood's federal claims and dismissal without prejudice as to the pendent state law claims. USTC also filed a motion in limine to exclude the testimony of Conwood's expert witness, Dr. Richard Leftwich, and moved separately to exclude Leftwich's damages study and future testimony during trial. The district court denied USTC's summary judgment motion on February 17, 2000. On February 23, 2000, the district court also denied USTC's motions with respect to Leftwich.

In February 2000, the case proceeded to trial. Before the case went to the jury, Conwood agreed to dismiss the state law claims and both parties agreed to dismiss their respective Lanham Act claims asserted against one another. The jury deliberated for four hours, returning a $350 million verdict in favor of Conwood. The district court entered judgment on March 29, 2000, and therein trebled the amount of the award to $1.05 billion, pursuant to 15 U.S.C. § 15(a). The jury also ruled in favor of Conwood on USTC's conversion and Sherman Act claims.

Conwood moved for a permanent injunction, pursuant to 15 U.S.C. § 26, to prevent USTC from, among other things, removing or eliminating any competitors' advertising material in retail stores, without the prior consent of the retailer. The district court granted the motion on August 10, 2000. USTC moved for judgment as a matter of law, or for a new trial or reduction in damages, arguing that its conduct was not exclusionary, competition was not harmed and that Conwood had not established causation and damages. The district court denied the motion on August 10, 2000. On September 11, 2000, USTC filed this timely notice of appeal challenging the district court's (1) February 17, 2000 denial of its motion for summary judgment; (2) February 23, 2000 order denying its motion to exclude the damages study and testimony of Leftwich; (3) March 29, 2000 judgment on the jury verdict; (4) August 10, 2000 order denying its motion for judgment as a matter of law, or in the alternative for a new trial or reduction of damages; and (5) August 10, 2000 order granting Conwood's motion for permanent injunctive relief.

**Facts**

Both Conwood and USTC are manufacturers of moist snuff, a finely chopped smokeless tobacco that the user consumes by placing a small amount between the gum and cheek. The product is sold in small round cans, at a price of between $1.50 and $3. USTC produces the industry staples "Skoal" and "Copenhagen." Conwood's brands include "Kodiak" and "Cougar."

USTC's predecessor, Duke Trust, started the moist snuff industry in 1822, with its Copenhagen brand. In 1911, a judicial decree broke up the Duke Trust monopoly, which spawned three companies: American Snuff Company (Conwood's predecessor); USTC; and "Helme" (which is now known as Swisher International Group, hereinafter, "Swisher"). American Snuff Company changed its name to Conwood sometime during the 1950s. Conwood and Swisher were involved for many years in the "dry snuff" market. For sixty years, USTC was the sole manufacturer of moist snuff. Swisher and Conwood entered the moist snuff market in the late 1970s. The only other competitor in the moist snuff market is Swedish Match ("Swedish"). Thus, there are only four competitors in the moist snuff market in the United States.

After Conwood, Swisher, and Swedish entered the market, USTC's market share, which at one point was virtually 100 percent, declined. By 1990, the four manufacturers sold 28 different brands of moist snuff and USTC's market share was approximately 87 percent. During the 1990s, market growth accelerated in the moist snuff industry, and USTC's market share continued to drop. At trial, one of Conwood's expert witnesses, Morton Kamien, a professor at Northwestern University's Kellogg Graduate School of Business, testified that USTC currently controls 77 percent of the moist snuff market; Conwood controls approximately 13 ½ percent of the market and Swedish and Swisher comprise approximately 6 percent and 4 percent of the market, respectively.

In 1999, total moist snuff sales amounted to $1.68 billion. Also, in 1999, USTC earned approximately $813 million in revenues before taxes, interest and amortization. The company has the highest profit margin of any public company in the country. Kamien testified that because USTC is one of the most profitable companies in the country, and because of the amount of profit at stake in the moist snuff market, it "would be a ripe opportunity for other firms to come in and try to get into the market . . . ." However, there have been no new entrants in the market since 1990. In addition, although USTC declined in market share about 1 percent per year between 1979 and 1999, Kamien testified that had there been true competition in the moist snuff industry, the decline would have gone much faster. He found it remarkable that while USTC's market share decreased, the company raised its prices. Testimony revealed that USTC had raised its prices approximately 8 to 10 percent per year between 1979 and 1998.

**The Importance of In-store Advertising**

Moist snuff is generally sold from racks. The racks have gravity fed slots or facings, from which consumers may select a can of the product. Each facing is filled with cans of a single brand of moist snuff. In addition to dispensing cans, the racks also provide "point of sale" ("POS") advertising, generally carried out by a "header card"—a cardboard sign attached to the front of the rack. The header card may contain such information as the name of the brand of moist snuff, any promotions running with the product, and a picture of the product.

The parties agree that POS in-store advertising is critical in the moist snuff industry because unlike with other products, such as soft drinks or snacks, tobacco advertising is restricted. Tobacco products cannot be advertised on TV or radio, and some places have restrictions on other forms of advertising outside of a retail store, such as on billboards. Further, the number of people who use smokeless tobacco products is relatively small in relation to those who consume other tobacco products. Thus, according to Harold Price, Swedish's vice president of sales and marketing, the point at which the buyer makes his purchase decision is the optimal time to convince the buyer to purchase a particular brand of moist snuff. Price testified that the "single most important" tool for advertising is the merchandise rack, "because that's where we have the greatest opportunity and the last point to reach the consumer before [the consumer] makes [his or her] purchase decision."

**Exclusive Racks, Category Management and CAP**

Conwood showed at trial that beginning in 1990, USTC pursued strategies, emanating from high-level management, to exclude competition in the moist snuff market.

According to trial testimony, USTC had been able to convince "a number of major retailers" to allow it to have "exclusive racks" in their stores. An "exclusive rack" refers to one manufacturer supplying a rack to display its moist snuff products and those of all other manufacturers. Kroger's Steven Luckett testified that while his store permits each moist snuff company to have its own rack, an advantage of allowing only one rack to store all similar products is uniformity. It also allows retailers to stack products in a manner that looks more attractive and neat. According to Alan Hart, a former USTC salesman, less than 10 percent of stores carried USTC racks exclusively, and of those that did "most all of them" did so because the store authorized it. Several retailers testified that they requested exclusive racks. In fact, Mary Stevens, who managed a Kiwi store in Billings, Montana, testified that she used only a Conwood rack.[1]

During the 1990s, many retailers adopted the practice of category management. This practice varies from store to store, and involves managing product groups and business units and customizing them on a store-by-store basis to satisfy customer demands. The process can determine the quantity of items a store sells. For instance, it allows retailers, based on such data as sales volume, to determine which items should be allocated more shelf space. Manufacturers support the efforts of retailers by presenting to them products or a combination of products that are more profitable and "plan-o-grams" describing how, and which, products should be displayed. At Wal-Mart, Swedish and USTC were involved with category management, which entailed suggesting which items should be on the racks. Swisher at one point was also involved in the process.

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[1] USTC also points out that in 1996, Wal-Mart asked it and other moist snuff manufacturers to design a rack for the store to use for its moist snuff products. (J.A. at 492.) Conwood decided not to participate in the contest. *Id.* USTC's design won. *Id.* Swisher also won similar competitions for exclusive rack systems in K-Mart and Tom Thumb stores. (J.A. at 2859, 518-19, 1447-48.)

As part of the category management process, retailers review plan-o-gram information provided by the manufacturer and compare the products they suggest be sold to the retailer's own independent analysis. The process is designed to ensure the best selling products are included in the plan-o-gram. Larry Luckett, who decides which moist snuff products will be sold at Kroger Company, testified that any supplier trying to use category management practices to control competition, in his store anyway, would be "committing suicide." USTC points out that no retailer testified that the company required shelf space allocations equal to its market share. Apparently, Wal-Mart rejected such a request from USTC.

However, according to Conwood, around 1990, USTC perceived it as a threat in the moist snuff market and took steps to eliminate it as a competitor and to "reject competition on the merits." USTC's president, Vincent Gierer, testified that around that time his company was losing market share and Conwood's volume was increasing. In the mid-1990s Conwood and Swedish introduced "price value" or half-priced brands of moist snuff. To show that USTC believed that such "price valued" products would erode its profits, Conwood points to a 1996 internal USTC report in which the company stated that one of its goals was to "[m]inimze the growth in [price value] we have been experiencing over the past five years to the point where USTC can still grow the market and achieve desired growth for USTC." The report stated that USTC would "need to be more aggressive where [price value] has a higher share of the segment and will actively pursue strategies to limit the growth of the price value market segment."

Conwood also claims that USTC, in its role as category manager, deliberately provided false information to stores to exclude competitors from the market. For instance, David Waller, a wholesale distributor, testified that USTC has provided "skewed" national sales figures to retailers that do not always represent local product movement in stores. A report drafted by a division manager in Houston also shows that USTC sometimes provided false information to retailers to get them to maintain USTC's poor selling items while dropping competitors' products. Conwood employees also testified that USTC provided false information to retailers, such as by inflating actual sales data.

According to Conwood expert witness Robert Blattberg, an expert on category management and a professor of retailing at Northwestern's Kellogg Graduate Business School, many retailers consider moist snuff a small category and give it little attention. By "small," Blattberg explained that it is only consumed by about seven percent of the population, almost all male. However, it is a highly profitable item on a linear foot basis because it takes up so little space. He testified that no store, not even Wal-Mart, according to him the largest retailer in the world, has anyone solely devoted to the management of moist snuff. From reviewing USTC documents, he testified that USTC employees understood that retail category managers did not know as much as USTC did about pricing, product knowledge and profitability of the products. He stated that manufacturers often have access to data that retailers do not, such as Nielsen data, which tracks product movement. He stated that because of their time constraints, retailers are most likely to delegate the task of category management with respect to such items as moist snuff. He testified that when a retailer does delegate category management responsibilities to a manufacturer, the latter has significant responsibility. The retailer will look to the manufacturer to provide such information as assortment recommendations for which items to stock, consumer information, sales, and which stores are stocking what items. He further testified that a retailer will rely on a large manufacturer to be its category captain because if a manufacturer controls 75 or 80 percent of the market many retailers will assume that the manufacturer will and can devote the resources to the category to help build it. For instance, Blattberg pointed to documents in which a USTC representative stated that "most retailers want the top dog running things because the dominant share of market customers will look to us for leadership."

Swedish's McClure also testified that "[t]here's only one category manager in the moist snuff business" – USTC. He also stated that while he would like to compete for the job of category manager, his company does not have shelf presence, consumer base or money. He also testified that USTC had not used its position fairly, had used its power "to keep [Swedish's] products off the shelf, and once it's there to get rid of it . . . ."

Terry Williams, Conwood's national sales manager, testified that in 1997 he was informed by one retailer that in order to obtain extra facings or a facing for a new item, the retailer first would have to consult with USTC. He also testified that before 1997, Conwood's market share in Wal-Mart was approximately 12 percent, but by the time of trial it was 6.5 percent. He explained that USTC's exclusive racks and its restrictions on Conwood's distribution began in Wal-Mart around 1997.

There is also documentary evidence that USTC sought to use its position as category manager to control and limit the number of price value products introduced in stores and to control the merchandising and POS placements in stores. In one 1997 report, a USTC regional vice president stated that "[i]t is imperative that we continue with this Category Management action plan to eliminate competitive products." In another document, a 1998 letter to David Untiedt, USTC national accounts director, a USTC employee stated that his biggest competitive concern with several stores in the Washington state area was the "availability of [Swedish's] Timberwolf [brand] and price differential between" that product and USTC's. The letter went on to state that "[a]lthough we control the merchandising and the POS placements, which will make the consumer awareness of the price differential difficult, some of the Circle K shoppers are always looking for a bargain." After reviewing this document, Blattberg testified that USTC apparently realized that customers were looking for a bargain, and that limiting the amount of POS and information makes it more difficult for the consumer to find price value brands. In yet another document Blattberg discussed, a USTC chain accounts manager in North Carolina wrote "Our objective with exclusive vending rights with this and other chains is to control expanded competitive distribution and competitive POS . . . we will continue to focus on merchandising rights to promote the growth of our product line and inhibit competitive growth . . . to the best of our ability." Blattberg testified that the obvious objective in having exclusive vending rights, according to the letter, is to reduce the amount of competitive items that can be offered.

According to Blattberg, documentary evidence showed that USTC intended to use its position as category captain to "control the number of price value product introductions." Blattberg testified that after reviewing numerous documents drafted by USTC staff, he saw instances where USTC provided misleading information to retailers, including falsely reporting that some of their products were selling better than their competitors in an effort to thwart competition. He testified that by limiting the availability of the price value brands, USTC limits the choices for consumers. He also testified that it limits the ability of competitors to enter the market because it limits what the consumer can see. He stated that USTC's practices were inconsistent with the concept of category management.

Kamien also testified that USTC's conduct harmed consumers by limiting variety and raising prices. He produced a chart showing that for every 10 percent increase in USTC facings, retail prices for moist snuff rose by $.07. A Wal-Mart manager testified that after USTC eliminated competitors' POS and facings, the number of other moist snuff items available to the store's customers declined.

Conwood introduced numerous documents drafted over several years by various USTC personnel, including chain accounts managers and others, that indicate USTC may have used its exclusive vending rights to hurt competition. *See e.g.*, J.A. at 2182 ("objective with exclusive vending rights with this and other chains is to control expanded competitive distribution and competitive P.O.S. Department . . . . We will continue to focus on merchandising rights to . . . inhibit competitive growth (to the best of our ability));" J.A. at 2185 ("We stressed in our Department Meeting the importance of cutting competitive distribution. In many stores, especially supermarkets, distribution of competitive brands is much too high . . . ."); J.A. at 2375 ( "Even though Conwood does not like the fact that we sometimes house their product in our vending, I have encountered more and more retailers that are surprised when I include the comp[etitions'] products. I feel it is better for them to be lost in our vending th[a]n to have their own and no point of sale on the vendor."); J.A. at 2401 ("Our objective is to control the smokeless home, . . . provide facings for competitive, control facings and positioning, and make our presence larger via P.O.S."); J.A. at 2523 ("With arrogance and grace, I have taken a personal vendetta against the Conwood Reps. in my areas. I am devoting an extra effort toward eliminating as many laggard Conwood brands at retail as possible . . . Since I am offering a cash counter payment for exclusive UST vending on our 2908 displays, I am giving Kodiak . . . [a Conwood brand] one facing . . . .").

In 1998, USTC introduced its Consumer Alliance Program ("CAP"), which entails granting retailers a maximum discount of .3% for providing USTC with sales data, and participating in USTC promotion programs, and/or giving the best placement to USTC racks and POS. According to Conwood, however, CAP is another means by which USTC excludes competition. For example, in "a monthly competitive letter" dated March 27, 1998, a USTC employee stated that the CAP "has become a great incentive in securing space for our vendors and for the elimination of competition products."

There was testimony that the CAP can be used to exclude competitive POS advertising, and that USTC was extremely successful in signing up retailers to enter into these agreements. In the first couple of months of the program, USTC was able to sign 37,000 retailers to the CAP, which represents 80 percent of its overall volume in moist snuff sales.

**Unauthorized Removal of Conwood Racks**

According to Conwood, when USTC sales representatives restocked or rearranged their own displays, they would routinely discard hundreds of thousands of Conwood racks and their accompanying POS. William Rosson, Conwood's Chairman, testified that after 1990, Conwood spent $100,000 a month on replacement racks. Rosson testified that the company had "monumental problems" keeping their moist snuff on the shelf. A Conwood sales representative testified that when displays were removed, Conwood was successful in restoring them about 95 percent of the time. Rosson testified that about 50 percent of sales representative's staff time was spent repairing racks destroyed by USTC representatives. Because two to three months would sometimes pass before a sales representative could return to the same store, Conwood lost sales even when it was able to restore racks.

Conwood also asserts that USTC would remove its POS and racks under the guise that retailers had given it permission to do so. Conwood argues that any permission to remove its products was done under a ruse of organizing or straightening stores. It argues that USTC supervisors trained their staff to take advantage of inattentive store clerks, apparently so that they could destroy Conwood's racks and headers in retail stores. For instance, Shawn Ulizio, a former USTC employee testified that most clerks did not understand or care that there were different manufacturers of snuff products. Another former USTC sales representative testified that after he got permission from a store manager, he would remove Conwood racks and put Conwood's products in USTC racks. Former USTC representative Lawrence Borrowdale testified that he was instructed, apparently by his supervisor, that if a competitor's rack was in the way, he should remove it. Borrowdale testified that on occasion he would remove competitors' racks and bag up their fresh products and place them under a counter. Several other former USTC employees gave similar testimony. Kamien testified that the documentary evidence showed that the problem of USTC removing competitors' racks was widespread over a period of time.

One Conwood employee testified that except for moist snuff, he never encountered problems with his displays regarding any Conwood product. He testified that he would place moist snuff racks in stores only to return later to have the displays gone and any remaining Conwood brands stuffed in USTC's rack. Another Conwood employee gave similar testimony. He also stated that once the USTC representative in his area told him that he intended to "bury" him. Later, he witnessed that same representative breaking down his rack one day, while USTC's regional vice president, then a USTC department manager, observed. Conwood did not encounter this problem with its displays of smokeless tobacco products in markets in which USTC did not compete.

Gayleen Rusk, who manages an Amoco Pronto Express, testified that she had experienced a USTC sales representative removing Conwood's racks and putting the products in the USTC rack. She testified that when she first started working at the store and did not know any better, she would allow it. Upon learning that the USTC representative was not supposed to bother competitors' racks, she would tell him not to do so when he visited the store. She stated that he would then come when she was not on duty and remove Conwood's rack anyway. Regarding the effect of not having Conwood brands in her store, Amoco manager Rusk stated that when customers request the items, they do not have them to sell. According to Conwood representative Brett Jeffery, when he told the USTC representative to stop removing his racks, Conwood's sales "dramatically increased." One former USTC representative, who witnessed the removal and destruction of Conwood's POS and racks stated that it had an effect on sales. According to him, no exposure meant no sale. Three other store witnesses also testified that they had seen or experienced USTC representatives removing Conwood racks.

According to USTC, however, retailers rely on manufacturers and wholesaler representatives to perform certain merchandising tasks for them, such as cleaning and rearranging items where a retailer may require more space to add or expand a section. USTC claims that during the 1990s, its more than 600 sales personnel visited 8 to 10 retail stores per day, totaling more than 7 million sales calls. These visits may involve, among other things, removing a competitor's products, racks, or POS, but only at the retailer's direction. USTC also points out that three of the former USTC employees that said that they removed Conwood racks and/or displays at the direction of their supervisors testified that they did so with the retailer's permission. Further, one had not worked for USTC since 1987, before the challenged conduct began. USTC concedes, however, that four witnesses testified that they removed racks and POS materials without retailer authorization. Further, Conwood sales representatives testified that their USTC counterparts told them they had orders from their supervisors to eliminate Conwood racks or facings, and in some cases, their compensation or bonuses depended on such rack destruction.

**Damages**

Rosson testified that had Conwood not been subjected to USTC tactics, it would have had a national market share of approximately 22 to 23 percent. Rosson testified that he had carefully tracked Conwood's market share over the past 20 years. Conwood's actual market share in its first 10 years in the moist snuff industry was 11 percent. In the next decade, starting from 1990, that figure increased by roughly 2.5

percent. Rosson testified that the lack of growth that occurred during the second decade largely resulted from USTC's tactics. He testified that his numbers are based on his studying markets where the company had a foothold and those in which it did not. In places where the company had a "foothold," i.e., a relatively high market share in a given area, it saw its market share increase during the 1990s to a market share above 20 percent. Rosson testified that each additional point (one percent) of market share translates into approximately $10 million in annual profits.

Williams testified concerning Conwood's market share with respect to the ten retail locations for which USTC offered evidence at trial. In those locations where USTC did not have rack exclusivity, Conwood's moist brands market share was well above its national average. For those locations where USTC had rack exclusivity, Conwood's market share was below its national average. Conwood argues that from these figures, a jury could have concluded that in unimpeded competition, Conwood's market share would have been approximately 25 percent instead of 13.5 percent nationally.

Finally, to prove damages, Conwood relied on the expert testimony of Professor Richard Leftwich of the University of Chicago Graduate School of Business, who is recognized as an expert on business valuation and lost profits. Leftwich apparently tested Rosson's hypothesis that Conwood's market share increased in areas in which it did not face USTC exclusivity.

Using a regression analysis, Leftwich found a statistically significant difference between states in which Conwood had a foothold and those in which it did not. Under Leftwich's model, in states where Conwood had a market share in 1990 of 20 percent or more, the market share grew on average an additional 8.1 percent from 1990 to 1997. In states where Conwood's market share in 1990 was at least 15 percent, it grew an additional 6.5 percent. In states below these thresholds, Conwood's growth was considerably lower. As the district court noted:

> Leftwich applied a regression analysis to test Conwood's hypotheses. He determined that Conwood's share in a state in 1990 is statistically related to the change in Conwood's market share between 1990 and 1997. The regression model predicts that where Conwood had a higher market share (e.g. 15-20%) in 1990, Conwood's market share grew during the period 1990 to 1997. In contrast, in states where Conwood had a lower market share, the regression predicts that its share would grow very little.

(J.A. at 87-88.)

Leftwich then determined that Conwood's low market growth was due to USTC's behavior. Leftwich's model also found that increases in USTC's exclusionary behavior in a state reduced Conwood's share of sales by a statistically significant amount. He found that Conwood's damages as a result of USTC's actions amounted to a figure between $313 million and $488 million, depending on whether Conwood's market share would have grown by 6.5 percent or 8.1 percent. The jury awarded damages of $350 million.

## DISCUSSION

### I.

This Court reviews a district court's denial of a motion for judgment as a matter of law pursuant to Fed. R. Civ. P. 50(b) *de novo*. *Williams v. Nashville Network*, 132 F.3d 1123, 1130 (6th Cir. 1997) (citing *K & T Enterprises, Inc. v. Zurich Ins. Co.*, 97 F.3d 171, 175 (6th Cir.1996)). "In a federal question case, the standard of review for a Rule 50 motion based on sufficiency of the evidence is identical to that used by the district court. The evidence should not be weighed, and the credibility of the witnesses should not be questioned." *Williams*, 132 F.3d at 1130-31. Further, the evidence is viewed in the light most favorable to the non-movant, and all reasonable inferences are drawn in that party's favor. *Id*. at 1131. This Court should grant the motion only if "reasonable minds could not come to a conclusion other than one favoring the movant." *Id*. Our task also embodies assuring that the district court "indulge[d] all presumptions in favor of the validity of the jury's verdict," and "refrain[ed] from interfering with [the] jury's verdict unless it [was] clear that the jury reached a seriously erroneous result." *Id*. (citing *Brooks v. Toyotomi Co.*, 86 F.3d 582, 588 (6th Cir.1996)).

This court considers the district court's decision to admit or exclude expert testimony for abuse of discretion, recognizing, of course, that such review calls for deference to the district court's decision. *See Clay v. Ford Motor Co.*, 215 F.3d 663, 666 (6th Cir. 2000) (citing *General Elec. Co. v. Joiner*, 522 U.S. 136, 138-139, 143 (1997)). Thus, we will reverse a district court only where we are left with a definite and firm conviction that it committed a clear error of judgment. *Singleton v. United States*, 277 F.3d 864, 870 (2002) (citing *Trepel v. Roadway Express, Inc.*, 194 F.3d 708, 716 (6th Cir.1999)).

## II.

USTC argues that the evidence presented at trial amounted to no more than "insignificant" tortious behavior and acts of ordinary marketing services. It contends that tortious activity cannot form the basis for liability under the Sherman Act unless "that activity is pervasive and accompanied by other anti-competitive conduct." USTC also argues that Conwood failed to show that it was foreclosed from the market, was unable to compete for shelf space, that competition among moist snuff suppliers was injured, or, generally, that any harm alleged was caused by anything other than competition itself. It contends that its category management services and promotional programs are common marketing practices. These services, among other things, (1) enhance demand for USTC's products and help to ensure that retailers use shelf space efficiently, (2) build consumer loyalty, and (3) improve presentation of the products. USTC states that trial testimony showed that, during the relevant period, retailers retained control of shelf space allocation, and which racks and POS materials were used. Further, during the relevant period (1990-1998), it argues that market output increased, its competitors' market shares doubled, and Conwood's sales and profits grew.

Conwood argues that the evidence in this case was sufficient to support the jury's verdict. Conwood contends that the jury heard and rejected USTC's argument that its conduct was ordinary "demand enhancing" business behavior. It argues that the evidence showed an "orchestrated USTC campaign to eliminate rival distribution and promotion with no competitive justification." Conwood argues that while USTC points to increased sales in the moist snuff market, it ignores the fact that in the "but for world of unimpeded competition, consumers and Conwood would have done substantially better." We agree with Conwood, and despite USTC's arguments in support of its position, we believe there was sufficient evidence to support the jury's verdict.

**III**.

A claim under § 2 of the Sherman Act requires proof of two elements: (1) the possession of monopoly power in a relevant market; and (2) the willful acquisition, maintenance, or use of that power by anti-competitive or exclusionary means as opposed to "growth or development resulting from a superior product, business acumen, or historic accident." *Aspen Skiing Co. v. Aspen Highlands Skiing Corp*., 472 U.S. 585, 595-96 (1985); *Re/Max Int'l, Inc. v. Realty One, Inc.*, 173 F.3d 995, 1016 (6th Cir. 1999) (citing *United States v. Grinnell Corp*., 384 U.S. 563, 570-71 (1966)). "To establish the offense of monopolization a plaintiff must demonstrate that a defendant either unfairly attained or maintained monopoly power." *Potters Med. Ctr. v. City Hosp. Ass'n,* 800 F.2d 568, 574 (6th Cir. 1986) (citation omitted)*; Beverage Mgmt., Inc. v. Coca-*

*Cola Bottling Corp.*, 653 F.Supp. 1144, 1151 (S.D. Ohio 1986). "Monopoly power consists of 'the power to control prices or exclude competition.'" *Potters,* 800 F.2d at 574 (citing *Grinnell*, 384 U.S. at 571). "An attempted monopolization [under § 2] occurs when a competitor, with a dangerous probability of success, engages in anti-competitive practices the specific design of which are, to build a monopoly or exclude or destroy competition." *Smith v. N. Michigan Hosps., Inc.*, 703 F.2d 942, 954 (6th Cir. 1983) (citations and internal quotation marks omitted). In a § 2 case, "only a thorough analysis of each fact situation will reveal whether the monopolist's conduct is unreasonably anti-competitive and thus unlawful." *Byars v. Bluff City News Co.*, 609 F.2d 843, 860 (6th Cir. 1979) (citations omitted); *see also Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 467 (1992) ("This Court has preferred to resolve antitrust claims on a case-by-case basis, focusing on the particular facts disclosed by the record.") (citations and internal quotation marks omitted). Moreover, in order for a "completed" monopolization claim to succeed, the plaintiff must prove a general intent on the part of the monopolist to exclude; while by contrast, to prevail on a "mere"attempt claim, the plaintiff must prove a specific intent to "destroy competition or build a monopoly." *Tops Markets, Inc. v. Quality Markets, Inc.*, 142 F.3d 90, 101 (2d Cir. 1998). However, "no monopolist monopolizes unconscious of what he is doing." *Aspen*, 472 U.S. at 602. Thus, "[i]mproper exclusion (exclusion not the result of superior efficiency) is always deliberately intended." *Id*. at 603 (citation omitted).

The first step in any action brought under § 2 of the Sherman Act is for the plaintiff to define the relevant product and geographic markets in which it competes with the alleged monopolizer, and with respect to the monopolization claim, to show that the defendant, in fact, possesses monopoly power. *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 268-69 (2d Cir. 1979). "A geographic market is defined as an area of effective competition." *Re/Max*, 173 F.3d at 1016 (citation omitted). "[I]t is the locale in which consumers of a product or service can turn for alternative sources of supply." *Id*.

In the instant case, USTC does not challenge that it has monopoly power; nor is there an issue as to the relevant product (moist snuff) and geographic markets (nationwide).[2] On appeal, USTC contends that Conwood has failed to establish whether USTC's power was acquired or maintained by exclusionary practices as opposed to its legitimate business practices, and a superior product. *Aspen*, 472 U.S. at 595-97. In determining whether conduct may be characterized as exclusionary, "it is relevant to consider its impact on consumers and whether it has impaired competition in an unnecessarily restrictive way." *Aspen*, 472 U.S. at 605. "If a firm has been attempting to exclude rivals on some basis other than efficiency, it is fair to characterize its behavior as predatory [or exclusionary.]" *Id.* However, merely because an entity has monopoly power, does not bar it from taking advantage of its scale of economies because of its size. *Id*. at

[2]Whether a company has monopoly or market power "may be proven directly by evidence of the control of prices or the exclusion of competition, or it may be inferred from one firm's large percentage share of the relevant market." *Tops Market,* 142 F.3d at 97-98 (citation omitted); *see also Re/Max*, 173 F.3d at 1016 (citation omitted). "[T]he material consideration in determining whether a monopoly exists is not that prices are raised and that competition is excluded, but that power exists to raise prices or to exclude competition when it is desired to do so." *Byars*, 609 F.2d 843, 850 (citations omitted). Courts have increasingly leaned toward using circumstantial evidence as a shortcut to determine whether monopoly power exists. *Re/Max*, 173 F.3d at 1016. Such circumstantial evidence may encompass a high market share within a defined market. *Id.* at 1018. At trial there was evidence that USTC enjoyed 74 to 77 percent market power nationwide in the moist snuff industry. As previously stated, USTC neither challenges this finding nor argues that it does not possess monopoly power. To that end, we agree with USTC that the monopolization and attempt to monopolize claims are coterminous inasmuch as USTC concedes monopoly power. *See Northeastern Tel. Co. v. American Tel. and Tel. Co.*, 651 F.2d 76, 85 (2d Cir. 1981) (explaining that where *ability* to exclude entry and control prices is present, the two offenses are coterminous).

597. Such advantages "are a consequence of size and not the exercise of monopoly power." *Id*.

USTC contends that none of the practices Conwood complains of amount to antitrust violations, but are no more than isolated sporadic torts. We disagree. Conwood presented evidence that beginning in 1990 USTC began a systematic effort to exclude competition from the moist snuff market. Conwood presented sufficient evidence that USTC sought to achieve its goals of excluding competition and competitors' products by numerous avenues. Conwood principally complains that USTC (1) removed racks from stores without the permission of store management and discarded and/or destroyed these racks, while placing Conwood products in USTC racks in an effort to bury Conwood's products and reduce their facings; (2) trained their "operatives to take advantage of inattentive store clerks with various 'ruses' such as obtaining nominal permission to reorganize or neaten the moist snuff section," in an effort to destroy Conwood racks; (3) misused its position as category manager by providing misleading information to retailers in an effort to dupe retailers into believing, among other things, that USTC products were better selling so that retailers would carry USTC products and discontinue carrying Conwood products; and (4) entered into exclusive agreements with retailers in an effort to exclude rivals' products.

Isolated tortious activity alone does not constitute exclusionary conduct for purposes of a § 2 violation, absent a significant and more than a temporary effect on competition, and not merely on a competitor or customer. *See* 3A Areeda & Turner, Antitrust Law, ¶ 782(a), at 272 (2002). Business torts will be violative of § 2 only in "rare gross cases." *Id*. As USTC recognizes, however, this is not to say that tortious conduct may never violate the antitrust laws. *See e.g., Byars*, 609 F.2d at 854 n.30 (holding that acts by defendant, a wholesale periodical distributor, against a smaller company attempting to compete against it, may be deemed exclusionary, including removing plaintiff's periodicals from sales racks at various retail outlets, covering up plaintiff's periodicals on racks so that prospective buyers could not see them, and disparaging plaintiff, his financial condition and the magazine's financial condition); 3A Areeda & Turner, *supra*, ¶ 782(a) at 272. Moreover, merely because a particular practice might be actionable under tort law does not preclude an action under the antitrust laws as well. *Id*. at 271. "'Anticompetitive conduct' can come in too many different forms, and is too dependent upon context, for any court or commentator ever to have enumerated all the varieties." *Caribbean Broad. Sys. Ltd. v. Cable & Wireless PLC,* 148 F.3d 1080, 1087 (D.C. Cir. 1998) (reversing district court's dismissal of complaint and holding that radio station owner stated § 2 Sherman Act claim where defendants' anti-competitive conduct consisted of making misrepresentations to advertisers and the government in order to protect their monopoly).

USTC contends that the rack and POS removal activity was isolated and sporadic. It contends that the record identifies a *de minimis* number of improper incidents. USTC points out that it has 600 sales personnel which made approximately 8 to 9 million sales calls during the 1990s. It argues that the district court "disregarded the fact that conduct and circumstances "differed greatly from chain to chain and store to store." *See In re Airport Car Rental Antitrust Lit.*, 474 F.Supp. 1072 (N.D. Cal. 1979) (holding that rental car company would be required to prove damages on airport by airport basis for each airport for which plaintiff sought damages by reason of its exclusion).

In the instant case, the district court rejected USTC's argument, essentially describing it as impractical. At issue in this case are 300,000 separate retail establishments across the country. We believe the district court correctly determined that to have required the parties to investigate activity at specific retail establishments would have been so costly as to have effectively ended this suit, despite substantial evidence of anti-competitive activity. In addition, "in an action for damages for violation of the antitrust laws plaintiff is [not] limited to recover only for specific items of damage which he can prove with reasonable certainty. On the contrary, the trier of the facts may make a just and reasonable estimate . . . based on relevant data and may act upon probable and inferential . . . proof." *Elyria-Lorain Broad. Co. v. Lorain Journal Co.*, 358 F.2d 790, 793 (6th Cir. 1966) (citation omitted).

It is undisputed that POS advertising and a manufacturer's ability to sell its moist snuff from its own racks are critical to success in the moist snuff market. *See Byers*, 609 F.2d at 860 (explaining that only a case-by-case analysis of each fact situation will determine whether the monopolist's conduct is anti-competitive). Because of restrictions on advertising in the tobacco industry, and the critical nature of POS advertising in the relevant market, efforts by USTC, a conceded monopolist, to exclude Conwood's racks and POS advertising from retail locations through any means other than legitimate competition could certainly support Conwood's § 2 Sherman Act claim. *See Aspen*, 472 U.S. at 605. Conwood presented evidence that USTC sales representatives continuously removed and discarded Conwood POS and racks after 1990 without store authorization. While the number of witnesses who actually testified was limited, the acts testified to were widespread. Douglas Hyaneck, a Conwood district manager, testified that when he served as a sales representative, he had trouble with rack removals in his stores in the northern Michigan area. He also stated that from the time he became a district manager until 1998, 40 to 50 percent of his sales staff's time was spent replacing racks. Gary Ryan, another Conwood sales representative in the Sikeston, Missouri area, says that about 1,200 of his racks were removed. He stated that the problem continued even after a new USTC sales representative was hired in his area. Both men testified that their racks were removed by USTC sales representatives. John Falevsky, a Conwood sales representative in the Milwaukee, Wisconsin and Southeastern Wisconsin area, and Sales Representative Jeffrey Dring also testified about rampant incidents of rack removal by USTC representatives in their areas. Falevsky testified that he once approached his USTC counterpart about the matter and was told that the latter's bonus depended on how many Conwood racks he could get out of the stores. There is no indication that any of these acts were authorized by the stores at which they occurred. Morever, Rosson, Conwood's Chairman, testified that he would receive estimates that as much as 50 percent of his employees' time was being spent on repairing damaged or discarded racks. He stated that some months, beginning in 1990, Conwood was spending as much as $100,000 a month to replace racks, which constituted as many as 20,000 racks a month being replaced. USTC did not challenge any of this evidence at trial. Construing the evidence in the light most favorable to Conwood, these incidents were neither sporadic nor isolated. *Cf. Abcor Corp. v. AM Int'l, Inc.*, 916 F.2d 924, 931 (4th Cir. 1990) (holding that "'sporadic activity' identified by the plaintiffs does not amount to an antitrust violation").

In terms of retailer testimony, Gayleen Rusk, who manages an Amoco Pronto Express, testified that she had experienced a USTC sales representative removing Conwood's racks and putting its products in the USTC rack. She testified that she allowed it to happen when she first started working at the store because she did not know any better. Upon learning that the USTC representative was not supposed to bother competitors' racks, she would tell him not to do so when he visited the store. She stated that he would then come when she was not on duty and remove Conwood's rack. Three other store witnesses also testified that they had seen or experienced USTC representatives removing Conwood racks.

Conwood also alleged that USTC used its role as category captain and/or manager to exclude competition. USTC points out that retailers testified that they alone, not USTC, determined and controlled what racks and POS were used in their stores. Conwood's Rosson admitted that he could not name one store that gives final decision-making power over its snuff section to his company's competitors. Other retailers verified this assertion. Kroger's Luckett testified that USTC did not receive all the facings in the plan-o-grams that it requested and that Kroger's retains ultimate authority about product placement. Retailer Paul McGuire also testified that he welcomed input from suppliers but retained final authority about product placement.

However, there was other evidence, which USTC ignores, that USTC used its position as category manager to exclude competition by suggesting that retailers carry fewer products, particularly competitor's products; by attempting to control the number of price value brands introduced in stores; and by suggesting that stores carry its slower moving products instead of better selling competitor products. Much of the evidence Conwood highlights was documentary, interpreted by experts. However, that evidence is nevertheless probative of USTC's intent to exclude competition.[3]

In one such instance, Blattberg opined that an e-mail sent by a USTC regional vice president and USTC director of national accounts showed that the company abused its position of category manager. The e-mail stated that USTC believed it could continue to be the category captain in certain stores in the Texas area, and "we may be able to control the number of price value product introductions and their pursuit of a private label brand." (J.A. at 1610.) Blattberg testified that the significance of this document is that it shows that USTC planned to control competition. It shows USTC

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[3] USTC complains that Conwood was allowed to rely on numerous hearsay documents that detailed conduct that is routinely rejected as not being very probative of anti-competitive intent and that showed nothing more than statements about competitive objectives. However, experts are entitled to rely on documents, even hearsay documents that are otherwise inadmissible. *Kingsley Associates, Inc. v. Del-Met, Inc.*, 918 F.2d 1277, 1286-87 (6th Cir. 1990) (holding that Federal Rules allow experts to base their opinions on hearsay and other evidence otherwise inadmissible at trial).

intended to control the number of price value brands and other products, which he stated meant that if USTC could convince retailers not to stock those items, the result would be to prevent rapidly growing or lower priced items from entering the marketplace. He testified that this is not consistent with the concept of category management, which is based on trust.

As for other abuses, Blattberg noted that the 1997 weekly activity report from a USTC division manager in Houston to a department manager stated that the company was receiving pressure from retailers to drop "Flavor Packs" in accounts where USTC was discontinuing competitive brands due to slow movement. (J.A. at 2559.) The report states:

> Last week at Fiesta Supermarkets, I was able to get them to drop all competitive brands (12 total) and keep only Redwood and Kodiak. The buyer argued with me that we should be dropping Flavor Packs too because FP are selling less than most of the products we discontinued despite our counter displays. We were able to maintain our counter display and the product, but he makes a very valid point that we are not being total [sic] honest with our partners when we sell them on share for space concept if we don't include our poor selling brands in the mix. I am afraid that we are using up our partnerships and good will when we talk about partnerships and sell our concept only to turn right around and ask them to go against what we just convinced them was in their best interest just to keep Flavor Packs in account.

*Id*. Blattberg testified that this document shows that USTC tried to gerrymander the data to this retailer. (J.A. at 1614.) Again, he opined that such practices violate the trust central to a category management relationship. Further, such evidence counters USTC's argument that only retailers controlled facing decisions.

Conwood does not appear to challenge USTC's role as category manager *per se*, but rather the manner in which it used its position as a monopolist providing category management services, i.e., to exclude it from competition. *See Aspen*, 472 U.S. at 605 (explaining that excluding rivals on a basis other than efficiency may be characterized as predatory or anti-competitive); *see also Eastman Kodak*, 504 U.S. at 483 (holding that under the willful-maintenance-of-monopoly power prong, defendant's liability in § 2 Sherman Antitrust claim turned on whether defendant could present a "valid business reason[] for its exclusionary conduct).[4] As explained above, Conwood presented evidence that the

[4]To the extent that USTC complains that evidence of its unlawful anti-competitive conduct, and its lawful conduct to take advantage of scale of economies, offer category management services or engage in other promotional activity in general were commingled, the district court properly instructed the jury that USTC could not be held liable for conduct that was part of the normal competitive process. The jury is deemed to have followed these instructions. *Aspen*, 472 U.S. at 604-05. In addition to that argument, USTC also contends that Conwood has failed to show that its practices foreclosed competition. It further contends that its exclusive dealing arrangements with retailers cannot be invalid, absent a "particularized showing of unreasonableness." *See. e.g., Tri-State Rubbish, Inc. v. Waste Mgmt., Inc.*, 998 F.2d 1073, 1080 (1st Cir. 1993) (explaining that a complaint that alleges, *inter alia*, no more than exclusive dealing arrangements may be susceptible to dismissal for failure to state a claim). However, Conwood's claim is broader than merely challenging the exclusive agreements USTC entered into with retailers for exclusive racks. As explained in the text of this opinion, among other things, Conwood presented evidence that USTC pervasively destroyed Conwood's racks, and used its monopoly power to misrepresent sales activity of moist snuff products for purposes of obtaining exclusive racks and to bury competitors' products therein, all of which affected competition in the moist snuff market. Moreover, Conwood's claims are distinguishable from those asserted in several of the cases USTC cites, wherein plaintiffs alleged that exclusive arrangements violated § 3 of the Clayton Act, 15 U.S.C. § 14 or other sections of the antitrust statutes. *See e.g., Omega Envtl., Inc. v. Gilbarco, Inc.*, 127 F.3d 1157, 1162 (9th Cir. 1997) (holding that "[o]nly those arrangements whose 'probable' effect is to 'foreclose competition in a substantial share of the line of commerce affected' violate Section 3").

category management program was used to place USTC racks exclusively in retail stores and hide competitor products in its racks. *See e.g.*, J.A. at 2375 ("Even though Conwood does not like the fact that we sometimes house their product in our vending, I have encountered more and more retailers that are surprised when I include the competition's products. I feel it is better for them to be lost in our vending then to have their own and no point of sale on the vendor.").

USTC's chairman Gierer testified that if his company's "goal . . . was to go into a store and reduce . . . competitive facings, then that shouldn't have happened. That's not a legitimate goal." Yet, Gierer later admitted that his company had endorsed a "strategy of eliminating competitive distribution." (J.A. at 2024.) Despite USTC's claims that its actions amounted to no more than competition and that "everybody does it," Gierer admitted that he was embarrassed by some of the testimony presented at trial, especially the testimony of Mr. Untiedt, USTC's director of national accounts, who apparently could not answer whether it was appropriate to mislead retailers. Gierer further testified that as a result of the evidence presented at trial, he was going to conduct an investigation into his company's practices. Gierer essentially admitted that the activities about which Conwood complains, particularly the misrepresentations to retailers to obtain exclusive vending, was not competitive conduct spurred by efficiency. Moreover, USTC has failed to offer any valid business reason for its representatives' pervasive destruction of Conwood racks. Instead, it merely has chosen to argue that such destruction can never form the basis for an antitrust claim.

The evidence Conwood presented in this case regarding USTC's exclusionary conduct must be considered in the context of Conwood's theory. *See Caribbean Broad. Sys.,* 148 F.3d at 1087. The theory Conwood advanced at trial is that USTC engaged in a concerted effort, directed from the highest levels of a national monopoly, to shut Conwood out from effective competition through the elimination of its racks and

POS advertising, all in the unusual moist snuff market, where POS is the central marketplace battleground. *See e.g., R.J. Reynolds Tobacco Co. v. Phillip Morris Inc.*, 60 F. Supp. 2d 502 (M.D.N.C. 1999) (granting preliminary injunction barring cigarette manufacturer in § 2 action from implementing program with retailers that would allow its product to hold most visible position in sales racks; and noting that in cigarette market product visibility and advertising at the point of purchase are essential to remaining competitive). There was ample documentary and testimonial evidence supporting this theory. The jury could have found, and apparently did find, that USTC's pervasive practice of destroying Conwood's racks and POS materials and reducing the number of Conwood facings through exclusive agreements with and misrepresentations to retailers was exclusionary conduct without a sufficient justification, and that USTC maintained its monopoly power by engaging in such conduct. Therefore, the district court did not err in holding that there was sufficient evidence for a jury to find willful maintenance of monopoly power.

## IV.

USTC argues that Conwood has failed to show that it or competition was harmed in the national moist snuff sales market. It argues that there was no injury to competition because the number of moist snuff brands actually increased during the 1990s, including the price-value products. It also argues that no injury to competition in the moist snuff market is shown because during the same period, other tobacco products decreased. USTC argues that where the market has actually expanded, there can be no showing of injury to competition. Further, USTC argues that Conwood has failed to show injury. It argues that during the relevant period, Conwood's market share actually increased. It also argues that there were other factors in the market, such as retailers' choices not to display Conwood's racks and POS, that caused Conwood's injury.

Conwood counters that it produced expert testimony showing that USTC's exclusion of rivals' POS racks and facings caused an increase in prices, reduced sales and limited choice. It also claims that but for USTC's actions, the market would have grown more. Finally, it argues that the fact that its own profits increased during the relevant period is not dispositive of the issue of injury.

The antitrust laws are intended to protect competition, not competitors. *See Andrx Pharmaceuticals, Inc. v. Biovail Corp. Intern.*, 256 F.3d 799, 812 (D.C. Cir. 2001) (citation omitted); *Tennessean Truckstop, Inc. v. NTS, Inc.*, 875 F.2d 86, 88 (6th Cir. 1989) (citations and internal quotation marks omitted). To prevail, a "[p]laintiff[] must prove antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful." *Valley Prods. Co., Inc. v. Landmark, A Division of Hospitality Franchise Sys., Inc.*, 128 F.3d 398, 402 (6th Cir. 1997) (citation omitted). Specifically, to recover damages, an "antitrust plaintiff must show (1) that the alleged violation tends to reduce competition in some market and (2) that the plaintiff's injury would result from a decrease in that competition rather than from some other consequence of the defendant's actions." *Id.* An antitrust plaintiff bears the burden of showing that the alleged violation was a material cause of its injury, a substantial factor in the occurrence of damage or that the violation was the proximate cause of the damage. *See Ezzo's Inv., Inc. v. Royal Beauty Supply, Inc.*, 243 F.3d 980, 990 (6th Cir. 2001). As this Court stated,

> [a]lthough a plaintiff need not show that the defendant's wrongful actions were the sole proximate cause of his injuries, the causal link must be provided as a matter of fact and with a fair degree of certainty. To be one of several causes is not enough. The evidence linking the violation to the injury must be more precise than that needed to establish the amount of damages.

*Id*.

USTC first argues that Conwood failed to show harm to competition in the market because output increased and new products were introduced into the market. There was evidence at trial that total market output increased in the moist snuff industry during the relevant period. Between 1990 and 1999, overall sales volume of moist snuff increased 16 million pounds. Also, during this period, new products entered the market, and by 1999, there were 40 brands of moist snuff, 24 of which came from USTC competitors. (J.A. at 474-76.) In *Omega Envtl., Inc. v. Gilbarco, Inc*., 127 F.3d 1157 (9th Cir. 1997), the Ninth Circuit held that antitrust plaintiffs had failed to produce "credible evidence to support their contention" that the defendant's actions had "deterred entry into this market," because during the relevant period industry output in the relevant market had substantially expanded. *Id*. at 1164; *see also Campus Ctr. Discount Den, Inc. v. Miami Univ*., No. 96-4002, 1997 WL 271742, at *2 (6th Cir. May 21, 1997) (holding that convenience store plaintiff failed to state a claim under the antitrust laws because it failed to show that any alleged anti-competitive conduct on behalf of the defendant reduced overall demand for convenience store market).

Conwood, however, argues that the issue is whether the market would have grown more absent USTC's antitrust violation. In *Brook Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), the evidence showed that following the defendant's alleged predation, output in the relevant market and market shares for others grew. *Id*. at 233-34. The Court stated, however, that the fact that the defendant's entry in the market did not restrict output was not dispositive. *Id*. at 234. "One could speculate . . . that the rate of growth would have tripled, instead of doubled [absent the] alleged predation." *Id*. at 234. However, the Court stated that there was no evidence that this was so. *Id*.

In the instant case, Kamien, Conwood's expert, testified that as a result of USTC's exclusionary conduct, the consumer suffered by having to pay higher prices, and that there was less variety in the market. (J.A. at 525.) The district court noted that much of the evidence regarding injury to competition was based, in part, on Kamien's testimony, which the jury obviously believed. Thus, although output in the moist snuff market grew, there was evidence showing that USTC's actions caused higher prices and reduced consumer choice, both of which are harmful to competition. *See Brook Group*, 509 U.S. at 234. Conwood's market share did grow slightly between 1990 and 1998; however, growth during that period, which was about 2.5 percent, stands in stark contrast to the growth in market share of approximately 11 percent that Conwood experienced in the ten years prior to 1990. In addition, Swedish's chairman also testified that USTC's activity restricted its growth. He testified that USTC used its power "to keep [Swedish's] products off the shelf, and once it's there to get rid of it . . . ." Thus, there was sufficient evidence that during the relevant period, the growth of two of the three other manufacturers of moist snuff aside from USTC slowed, and that the restricted growth resulted from USTC's conduct. In addition, Kamien testified that since 1990, no new firm had entered the moist snuff market, which he found odd because of the high amount of potential profit at stake in that market and the fact that USTC was the most profitable company in the country. He further testified that had there been true competition in the moist snuff market, USTC's market share, which dropped approximately 1 percent per year between 1979 and 1990, would have fallen much faster. We believe that construing the evidence in the light most favorable to Conwood, as we must, it was sufficient to show that competition suffered during the relevant period. *Williams*, 132 F.3d at 1131.

USTC also argues that its conduct was not the "necessary predicate" of any injury Conwood suffered, and thus Conwood cannot recover under the antitrust laws. USTC argues that any injury Conwood suffered was the result of retailers' decisions to enter into contracts with it and others to serve as category managers. For support, USTC primarily relies on *Valley Products,* 128 F.3d 398. In that case, a plaintiff who made and sold soap for use in hotels and motels under franchises granted by defendants brought suit under the Clayton Act, 15 U.S.C. § 15, when plaintiff was denied permission to continue using on its items logos owned by the defendants. *Id*. at 400-01. The defendants had ended their agreement with plaintiff after it granted two other manufacturers "preferred supplier status," which meant they alone could place the trademarks owned by one of the defendants on their amenities. *Id.* This Court affirmed the district court, which found that the plaintiff had not shown an antitrust injury. *Id.* at 400. This Court noted that to show antitrust injury, the plaintiff must show more than economic injury. *Id.* at 402. The Court stated that an analysis of the "the directness or indirectness of the injury was appropriate." *Id.* at 403. The Court noted that an injury does not exist for purposes of antitrust suits if it does not flow directly from the antitrust violation. *Id.* The Court found no injury because the violation alleged was not the "necessary predicate" of the plaintiff's injury. *Id*. at 404. The injury did not flow directly from the defendants' actions, but rather, the plaintiff's loss of sales resulted from the cancellation of the agreement to use the trademarks, which defendants had a right to do, and not from any anti-competitive activity.

USTC argues in this case that Conwood's injury flowed from the retail agreements that granted exclusive rights to USTC and to others at the expense of Conwood. This argument is unconvincing because there was evidence that Conwood's injury flowed directly from USTC's unauthorized removal and destruction of its racks and POS. Conwood's Rosson also testified that USTC's activity restricted its growth. There was evidence that USTC and not retailers controlled facing decisions and that in making those decisions, USTC sales representatives purposely attempted to bury Conwood's products in USTC racks. (*See e.g.*, J.A. at 2375.) Further, there was evidence that USTC misrepresented the sales activity of its own products to retailers in order to increase the number of facings of its slower moving products despite the fact that other brands by its competitors, including those of Conwood, were better selling. Such activity encompasses the anti-competitive acts about which Conwood complains. Thus, there was sufficient evidence showing that Conwood's injury did flow from USTC's anti-competitive activity. *Valley Products,* 128 F.3d at 404. Further, while the link between the injury and violation must be "proved as a matter of fact and with a fair degree of certainty," it need not be the "sole proximate cause." *See Ezzo's,* 243 F.3d at 990. In sum, there was sufficient evidence for a jury to find that USTC's anti-competitive activity harmed competition in the moist snuff market and Conwood; and USTC is not entitled to judgment as a matter of law on this ground.

## V.

USTC challenges the district court's decision to allow Leftwich to testify as to the damages sustained by USTC's conduct. USTC argues that the district court made no findings regarding the admissibility of Leftwich's report under *Daubert v. Merrell Dow Pharm., Inc*., 509 U.S. 579 (1993). USTC argues that Leftwich's methodology fails because it was constructed solely for this case. USTC also argues that Leftwich's study did not attempt to segregate the effects of other factors that could have contributed to Conwood's low sales in some states, and it made no attempt to test whether the slow growth in certain states was causally linked to any of USTC's conduct. Thus, USTC argues the study did not and could not fit the case at hand.

As a preliminary matter, Conwood argues that USTC waived any challenge to Leftwich's testimony because after the district court ruled that Leftwich's testimony was admissible on a preliminary basis, the court explained that USTC could contest Leftwich's testimony at trial. Conwood asserts that because USTC failed to object to Leftwich's testimony at trial, it has waived our review of the district court's decision to allow Leftwich to testify. We disagree.[5]

USTC filed a motion in limine challenging the admissibility of Leftwich's testimony, and the district court correctly concluded that its admissibility was governed by the Supreme Court's opinion in *Daubert*. *See Nelson v. Tennessee Gas Pipeline Co.*, 243 F.3d 244, 250 (6th Cir. 2001). The district court considered USTC's arguments regarding admissibility under Fed. R. Evid. 702, pertaining to the admissibility of expert witnesses, and found that "Leftwich's testimony satisfies *Daubert*." (J.A. at 90.) USTC also argued that Leftwich's testimony should be excluded under Rule 403 because it lacked probative value and would mislead the jury.[6] Specifically, USTC challenged the factual assumptions that Leftwich tested. The district court held that it could not at that time say that Leftwich's assumptions had no basis in fact, but that USTC might prove differently at trial. In *United States v. Brawner*, 173 F.3d 966 (6th Cir. 1999), we held that where a trial court has made a definitive ruling on the record of the evidentiary issues to be decided, and has not indicated that the ruling is subject to other circumstances or evidence, then counsel need not renew the objection at the time the evidence is offered at trial to preserve the error for appeal. *Id*. at 970; *see also* Fed. R. Evid. 103(a)(2) (holding that once a

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[5] However, apparently for the first time on appeal, USTC argues that Leftwich's regression model cannot be tested, is not subject to ascertainable rate of error and has no basis in the literature. These arguments were not raised below and may not be asserted now on appeal. *See White v. Anchor Motor Freight, Inc*., 899 F.2d 555, 559 (6th Cir. 1990) (noting that this Court reviews the case presented to the district court, and not a better one fashioned on appeal, and will not decide issues the parties failed to litigate before the district court).

[6] Fed. R. Evid. 403 provides: "Although relevant, evidence may be excluded if its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, or by considerations of undue delay, waste of time, or needless presentation of cumulative evidence."

court makes a *definitive* ruling on the record to either admit or exclude evidence, at or before trial, a party need not renew an objection at trial to preserve any alleged error for appeal). In the instance case, the district court's opinion unequivocally stated that "Leftwich's testimony satisfies *Daubert*." Moreover, after Conwood rested its case, USTC moved for judgment as a matter of law challenging the assumptions of Leftwich's damages theory. We therefore do not believe that USTC waived appellate review of Leftwich's damages theory.[7]

USTC does not challenge Leftwich's qualifications as an expert, but only his testimony and damages study. Pursuant to Rule 702 of the Federal Rules of Evidence, "[i]f scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise . . . ." Fed. R. Evid. 702. In *Daubert*, the Supreme Court "established a general gatekeeping [or screening] obligation for trial courts" to exclude from trial expert testimony that is unreliable and irrelevant. *Hardyman v. Norfolk & W. Ry. Co.*, 243 F.3d 255, 260 (6th Cir. 2001) (citation and internal quotation marks omitted). The district court must determine whether the evidence "both rests on a reliable foundation and is relevant to the task at hand." *Id*. (citation omitted). In assessing relevance and reliability, the district court must examine "whether the expert is proposing to testify to (1) scientific knowledge that (2) will assist the trier of fact to understand

[7] We also note that even if USTC had failed to adequately preserve this issue, we would still review it for plain error, and USTC would only be entitled to relief if we determined that its "substantial rights" had been affected. *Brawner*, 173 F.3d at 970 (citations omitted). Regardless of whether we review the issue for plain error or for abuse of discretion, as we explain in the text of this opinion, we believe that the district court did not err in allowing Leftwich to testify regarding the damages Conwood sustained.

or determine a fact in issue.*"* *Jahn v. Equine Servs., PSC*, 233 F.3d 382, 388 (6th Cir. 2000) (citations omitted). This involves a preliminary inquiry as to whether the reasoning or methodology underlying the testimony is scientifically valid and whether that reasoning or methodology properly can be applied to the facts in issue. *Id.* (citation and internal quotation marks omitted). Some of the factors that may be used in such an inquiry include: (1) whether the theory or technique has been tested and subjected to peer review and publication, (2) whether the potential rate of error is known, and (3) its general acceptance. *Hardyman*, 243 F.3d at 260. "This inquiry is a flexible one, with an overarching goal of assessing the 'scientific validity and thus the evidentiary relevance and reliability' of the principles and methodology underlying the proposed expert testimony." *United States v. Langan*, 263 F.3d 613, 621 (6th Cir. 2001) (citation omitted). "[A] trial judge must have considerable leeway in deciding in a particular case how to go about determining whether particular expert testimony is reliable." *Kumho Tire Co., LTD v. Carmichael*, 526 U.S. 137, 152 (1999); *see also Jahn,* 233 F.3d at 388 (explaining that *Daubert* made clear that Rule 702 relaxes the "traditional barriers" to admitting opinion testimony).

USTC presents no reasoned basis for us to find that the district court abused its discretion in determining that Leftwich's methodology was sufficiently reliable or relevant to survive a *Daubert* challenge. USTC asserts two principal challenges to Leftwich's study and testimony. USTC claims that Leftwich did not relate any of Conwood's loss to specific bad acts by USTC and failed to account for other factors that could have had a negative effect on Conwood's sales. Leftwich used a regression analysis to test Rosson's hypothesis that Conwood's growth was suppressed most in states where it had only a small market share when USTC began its exclusionary practices. He also tested whether the intensity of USTC's misconduct increased in or around 1990. Rosson testified that once his company reached a 15 percent market share, USTC's exclusive vending practices were not as effective.

Leftwich employed three methods to test Conwood's claims: regression analyses, a yardstick test and a before-and-after test. All three are generally accepted methods for proving antitrust damages. *See e.g., Petruzzi's IGA Supermarkets, Inc. v. Darling-Delaware Co.,* 998 F.2d 1224, 1238 (3d Cir. 1993) (explaining that if performed properly multiple regression analysis is a reliable means by which economists may prove antitrust damages); *Eleven Line, Inc. v. North Texas State Soccer Ass'n,* 213 F.3d 198, 207 (5th Cir. 2000) (noting that the two most common methods of quantifying antitrust damages are the "before and after" and "yardstick" measures of lost profits).[8]

Leftwich found a statistically significant difference in Conwood's market share between those states in which Conwood had a foothold and those in which it did not. In those states in which Conwood enjoyed a market share of 15 and 20 percent or more, Conwood grew in share, between 1990 and 1997, on an average of 6.5 percent and 8.1 percent, respectively. He concluded that but for USTC's exclusionary acts, Plaintiff's market share would have grown by these same amounts in non-foothold states. Contrary to USTC's arguments, the record indicates that Leftwich ruled out the possibility that the statistical relationship was caused by factors other than USTC's conduct. We find particularly relevant the undisputed evidence that Leftwich examined the

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[8] "The before and after theory compares the plaintiff's profit record prior to the violation with that subsequent to it [and] the yardstick test . . . consists of a study of the profits of business operations that are closely comparable to the plaintiff's." *Eleven Line, Inc*., 213 F.3d at 207 n.17. A regression analysis looks at the relationship between two variables. *Rollins v. Fort Bend Independent School Dist.*, 89 F.3d 1205, 1210 n.6 (5th Cir. 1996). The point of a regression analysis is to determine whether the relationship between the two variables is statistically meaningful. *Engineering Contractors Ass'n of South Florida Inc. v. Metropolitan Dade County*, 122 F.3d 895, 917 (11th Cir. 1997).

possible explanations that USTC's own expert suggested as possible explanations for Conwood's low market share. Leftwich testified that he tested all "plausible explanations" for his results for which he had data. Employing a regression analysis, Leftwich analyzed whether these other factors could explain Conwood's laggard growth in non-foothold states and concluded that they could not.

Leftwich also employed a before-and-after test to investigate Conwood's claims. Specifically, he tested whether the relationship between Conwood's share of moist snuff sales in a state and the rate of growth in Conwood's share of sales in that same state was the same or different for the seven year period before 1990 as it was for the seven year period after 1990. He found that Conwood's moist snuff market share did not grow significantly more in foothold states in the seven year period before 1990. Thus, there was no correlation in the pre-1990 period between Conwood's foothold status and market share growth rate.

Further, Leftwich employed a yardstick test to examine whether in the related loose leaf tobacco market, in which USTC does not participate, Conwood would always grow more in states where they started out with a high market share. He did not find a statistically significant relationship in Conwood's increase in market share in the loose leaf market between 1990 and 1997 and its share in 1990. In other words, where Conwood enjoyed a high market share or foothold in 1990 in the loose leaf market, it did not necessarily grow more in the period between 1990 and 1997.

USTC complains that Leftwich failed to take into account any USTC "bad act." However, this is not completely accurate. Using USTC's expert's own regression model, Leftwich used sworn affidavits compiled from 241 Conwood sales representatives detailing USTC's unethical activity in their areas. He used this information to construct three alternate measures of USTC's bad acts by state. (J.A. at 4415.) Thus, his damages study was relevant to the issues of this case. *See Jahn v. Equine Servs*, PSC, 233 F.3d 382, 388 (6th Cir. 2000) (testimony is relevant where there is a valid connection to the pertinent inquiry).

USTC also complains that Leftwich's regression analysis ignored other market variables that could have caused Conwood's harm. However, as explained above, Leftwich ruled out all plausible alternatives for which he had data. Moreover, he accounted for all variables raised by USTC's own expert. In any event, "[i]n order to be *admissible* on the issue of causation, an expert's testimony need not eliminate all other possible causes of the injury." *Jahn*, 233 F.3d at 390 (emphasis added); *see also Bazemore v. Friday*, 478 U.S. 385, 400 (1986) (failure to include variables will normally affect the analysis' probativeness, not its admissibility). In sum, after reviewing the record and giving due deference to the district court's decision, we believe that the district court did not abuse its discretion in concluding that Leftwich's study satisfied *Daubert* and allowing him to testify, subject to vigorous cross examination and an opportunity for Defendant to introduce countervailing evidence of its own. *See Daubert*, 509 U.S. at 596 (holding that "[v]igorous cross-examination, presentation of contrary evidence, and careful instruction on the burden of proof are the traditional and appropriate means of attacking shaky but admissible evidence") (citation omitted).

Finally, USTC contends that Rosson's testimony regarding damages and Leftwich's study were speculative and failed to support the damages awarded. We disagree. USTC essentially argues that a more rigorous standard of proof of damages was warranted. However, it is undisputed that USTC did not object to the jury instructions regarding damages. The jury was instructed that it could not award damages for injuries caused by other factors. As juries are presumed to follow the instructions given, we reject USTC's argument that Conwood failed to disaggregate the injury caused by USTC as opposed to that caused by other factors. *See Aspen*, 472 U.S. at 604-05.

In addition, an award of damages may be awarded on a plaintiff's estimate of sales it could have made absent the antitrust violation. *J. Truett Payne Co., v. Chrysler Motors Corp*., 451 U.S. 557, 565 (1981). While USTC demands a more exacting standard, "[t]he vagaries of the marketplace usually deny us sure knowledge of what plaintiff's situation would have been in the absence of the defendant's antitrust violation." *Id*. at 566. "The antitrust cases are legion which reiterate the proposition that, if the fact of damages is proven, the actual computation of damages may suffer from minor imperfections." *South-East Coal Co. v. Consolidation Coal Co.,* 434 F.2d 767, 794 (6th Cir. 1970) (citation omitted).

We believe that there was sufficient evidence to support the jury's award of damages in this case. There was testimony that absent USTC's unlawful conduct, Conwood would have achieved market share in the mid-20s. For instance, Rosson testified that had Conwood not been subjected to USTC tactics, it would have had a national market share of approximately 22 to 23 percent. Rosson testified that he had carefully tracked the growth of Conwood's market share over the past 20 years, and its sharp decline in the 1990s was largely due to USTC's tactics. Williams, Conwood's national sales manager, also testified that in those stores where USTC practiced rack exclusivity, Conwood's market share was well below its national average. Such evidence supported Leftwich's damages analysis, and he estimated that Conwood's damages ranged between $313 million and $488 million. The jury awarded damages well within that range. Although USTC argues that there was evidence that undermined Rosson's testimony regarding whether USTC's conduct caused Conwood's injury, the jury heard all of the evidence presented to it, and apparently found other testimony supporting the award of damages more credible. *South-East Coal Co.,* 434 F.2d at 794 (explaining that whether plaintiff's losses resulted from defendants' conduct or other market factors was for the jury to determine, as was witness credibility). In sum, we believe that there was sufficient evidence to sustain the award in this case.

## CONCLUSION

The district court did not err in submitting this case to the jury and denying USTC's motion for judgment as a matter of law. Conwood presented sufficient evidence that USTC's conduct rose above isolated tortious activity and was exclusionary without a legitimate business justification. The evidence also sufficiently showed that USTC's actions injured Conwood and competition in the moist snuff market. Finally, the district court did not abuse its discretion in admitting the testimony of Conwood's damages expert, subject to cross examination and presentation of countervailing evidence. Therefore, we **AFFIRM**.

**UST INC.**
Form 10-K For the fiscal year ended December 31, 2003

*Note*: In 2003, UST was the parent company of United States Tobacco Company.

**Other Matters (pp. 61-62)**

On March 15, 2004, the Company announced significant steps to resolve antitrust actions filed against it as a result of the Conwood Litigation (see below). In connection with the actions, the Company recorded $280 million pretax charge associated with the following: (1) the resolution of an antitrust action brought by a smokeless tobacco competitor, Swedish Match North America, Inc. (2) an agreement for a proposed resolution of antitrust actions, subject to court approval, by indirect purchasers in 11 states and the District of Columbia, and (3) the decision to settle other indirect purchaser actions not covered by such agreement. The settlement agreement in the smokeless tobacco competitor action requires the Company to pay $200 million and transfer its cigar operation to Swedish Match during 2004. Included in the $280 million above is a charge of $40 million, reflecting the fair value of the cigar operation, which approximates its book value. The proposed settlement of the indirect purchaser actions (see Contingencies note) covered by the subject agreement requires the Company to issue coupons to adult consumers redeemable on future purchases of its moist smokeless tobacco products, as well as pay all administrative costs and attorneys' fees. In addition, the Company intends to pursue settlement of other indirect purchaser actions not covered by this agreement on substantially similar terms. Included in the $280 million above, the Company recorded a charge of $40 million, which represents the best estimate of the total costs to resolve indirect purchaser actions.

In March 2000, a Kentucky jury rendered a verdict against the Company, awarding $350 million in compensatory damages to Conwood Company, L.P., for its claims under federal antitrust laws that the Company had engaged in exclusionary and anticompetitive conduct in the marketing and promotion of moist smokeless tobacco products. The verdict, when entered as a judgment, was subject to trebling under federal antitrust laws to $1.05 billion plus interest and other costs. On January 13, 2003, the Supreme Court of the United States declined to hear the Company's appeal and let stand the $1.05 billion antitrust award, plus interest and other costs, against the Company. As a result, the Company included a $1.261 billion pretax charge in its net loss for 2002.

In January 2003, the Company paid the antitrust award in the amount of $1.262 billion, which included additional interest charges for 2003. The Company utilized funds held in restricted deposits in the amount of $1.242 billion and $19.7 million of additional cash in satisfaction of the award.

Given the size of the award in the Conwood litigation in 2002 and the antitrust settlement charges recorded in 2003, the Company recognizes that these matters had a material adverse effect on its consolidated financial position in the respective years. However, in light of the Company’s ability to satisfy these matters primarily with accumulated funds, the Company does not expect the payments of the judgment and settlements to have a material adverse effect on the Company’s dividend policy or its ability to implement its strategic business plans.

# DOJ Microsoft Case

**UNITED STATES V. MICROSOFT CORP.**
87 F. Supp. 2d 30 (D.D.C. 2000),
*aff'd in part, rev'd in part, and remanded*,253 F.3d 54 (D.C. Cir. 2001)

The required reading on this case is A. Douglas Melamed & Daniel Rubinfeld, *U.S. v. Microsoft: Lessons Learned and Issues Raised*, in Antitrust Stories 287 (Eleanor M. Fox & Daniel A. Crane eds., 2007). It may be found on Dan Rubinfeld's publications web site or here for a direct link.

I much rather would have you read the complaint, the various opinions on liability and remedy, the appeal briefs and opinion, and the consent settlement—which collectively are well over 500 pages—so we will have to settle on the 25-page Melamed-Rubinfeld chapter.

One thing , however, that should not be missed is the videotape of Bill Gates' deposition. It is on YouTube. See some short excerpts here.

All of these materials may also be linked through the Unit 16 web page of AppliedAntitrust.com.

# FTC Intel Monopolization Case

PROTECTING AMERICA'S CONSUMERS

100 YEARS

MAIN MENU SEARCH

# FTC Challenges Intel's Dominance of Worldwide Microprocessor Markets

## FTC Charges Anticompetitive Tactics Have Stifled Innovation and Harmed Consumers

FOR RELEASE

December 16, 2009

**TAGS:** Competition

The Federal Trade Commission today sued Intel Corp., the world's leading computer chip maker, charging that the company has illegally used its dominant market position for a decade to stifle competition and strengthen its monopoly.

In its complaint, the FTC alleges that Intel has waged a systematic campaign to shut out rivals' competing microchips by cutting off their access to the marketplace. In the process, Intel deprived consumers of choice and innovation in the microchips that comprise the computers' central processing unit, or CPU. These chips are critical components that often are referred to as the "brains" of a computer.

According to the FTC complaint, Intel's anticompetitive tactics were designed to put the brakes on superior competitive products that threatened its monopoly in the CPU microchip market. Over the last decade, this strategy has succeeded in maintaining the Intel monopoly at the expense of consumers, who have been denied access to potentially superior, non-Intel CPU chips and lower prices, the complaint states.

"Intel has engaged in a deliberate campaign to hamstring competitive threats to its monopoly," said Richard A. Feinstein, Director of the FTC's Bureau of Competition. "It's been running roughshod over the principles of fair play and the laws protecting competition on the merits. The Commission's action today seeks to remedy the damage that Intel has done to competition, innovation, and, ultimately, the American consumer."

The FTC's administrative complaint charges that Intel carried out its anticompetitive campaign using threats and rewards aimed at the world's largest computer manufacturers, including Dell, Hewlett-Packard, and IBM, to coerce them not to buy rival computer CPU chips. Intel also used this practice, known as exclusive or restrictive dealing, to prevent computer makers from marketing any machines with non-Intel computer chips.

In addition, allegedly, Intel secretly redesigned key software, known as a compiler, in a way that deliberately stunted the performance of competitors' CPU chips. Intel told its customers and the public that software performed better on Intel CPUs than on competitors' CPUs, but the company deceived them by failing to disclose that these differences were due largely or entirely to Intel's compiler design.

Having succeeded in slowing adoption of competing CPU chips over the past decade until it could catch up to competitors like Advanced Micro Devices, Intel allegedly once again finds itself falling behind the competition – this time in the critical market for graphics processing units, commonly known as GPUs, as well as some other related markets. These products have lessened the need for CPUs, and therefore pose a threat to Intel's monopoly power.

Intel has responded to this competitive challenge by embarking on a similar anticompetitive strategy, which aims to preserve its CPU monopoly by smothering potential competition from GPU chips such as those made by Nvidia, the FTC complaint charges. As part of this latest campaign, Intel misled and deceived potential competitors in order to protect its monopoly. The complaint alleges that there also is a dangerous probability that Intel's unfair methods of competition could allow it to extend its monopoly into the GPU chip markets.

According to the FTC's complaint, Intel's anticompetitive tactics violate Section 5 of the FTC Act, which is broader than the antitrust laws and prohibits unfair methods of competition, and deceptive acts and practices in commerce. Critically, unlike an antitrust violation, a violation of Section 5 cannot be used to establish liability for plaintiffs to seek triple damages in private litigation against the same defendant. The complaint also alleges that Intel engaged in illegal monopolization, attempted monopolization and monopoly maintenance, also in violation of Section 5 of the FTC Act.

To remedy the anticompetitive damage alleged in the complaint, the FTC is seeking an order which includes provisions that would prevent Intel from using threats, bundled prices, or other offers to encourage exclusive deals, hamper competition, or unfairly manipulate the prices of its CPU or GPU chips. The FTC also may seek an order prohibiting Intel from unreasonably excluding or inhibiting the sale of competitive CPUs or GPUs, and prohibiting Intel from making or distributing products that impair the performance–or apparent performance–of non-Intel CPUs or GPUs.

The Commission vote approving the administrative complaint was 3-0, with Commissioner William E. Kovacic recused, and Commissioner J. Thomas Rosch issuing a separate statement in which he concurs in part and dissents in part from the Commission vote.

Chairman Leibowitz and Commissioner Rosch issued a statement outlining the rationale for bringing the case under Section 5 of the FTC Act, which can be found on the FTC's Web site and as a link to this press release. In his concurring and dissenting statement, Commissioner Rosch described the legal principles that limit an FTC Act Section 5 claim in this case, and the problems that could result from adding follow-on Sherman Act Section 2 claims. A copy of the Commissioner's statement also can be found on the FTC's Web site and as a link to this press release.

Under the recently implemented rule expediting the Part 3 administrative hearing process, this matter is tentatively scheduled to be heard before an Administrative Law Judge on September 15, 2010, at 10:00 a.m.

**NOTE:** The Commission issues a complaint when it has "reason to believe" that the law has been or is being violated, and it appears to the Commission that a proceeding is in the public interest. The issuance of a complaint is not a finding or ruling that the respondent has violated the law. The complaint marks the beginning of a proceeding in which the allegations will be ruled upon after a formal hearing.

The FTC's Bureau of Competition works with the Bureau of Economics to investigate alleged anticompetitive business practices and, when appropriate, recommends that the Commission take law enforcement action. To inform the Bureau about particular business practices, call 202-326-3300, send an e-mail to antitrust@ftc.gov, or write to the Office of Policy and Coordination, Room 394, Bureau of Competition, Federal Trade Commission, 600 Pennsylvania Ave, N.W., Washington, DC 20580. To learn more about the Bureau of Competition, read "Competition Counts" at http://www.ftc.gov/competitioncounts.

(FTC File No.: 061-0247)
(Intel.final.wpd)

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**Statement of Chairman Leibowitz and Commissioner Rosch**
*In the Matter of Intel Corporation*
*Docket No. 9341*

After a multi-year investigation, extensive discussions within the Commission – including an unprecedented four Commission meetings – and multiple meetings with Intel Corporation ("Intel") and other interested parties, the Commission has voted unanimously to challenge an alleged course of conduct undertaken by Intel. Broadly speaking, the complaint alleges that Intel fell behind in the race for technological superiority in a number of markets and resorted to a wide range of anticompetitive conduct, including deception and coercion, to stall competitors until it could catch up. If the allegations in the complaint are true, Intel's actions over a period of years and continuing up until today have diminished competition and harmed consumers.

The complaint challenges Intel's conduct as an unfair method of competition, both in violation of the Sherman Act and also as a "stand-alone" violation of Section 5 of the FTC Act, i.e. as an unfair method of competition independent of the Sherman Act.[1] We focus this statement on the stand-alone Section 5 unfair method of competition claim because liability under that standard has the potential to protect consumers while at the same time limiting Intel's susceptibility to private treble damages cases.

Despite the long history of Section 5, until recently the Commission has not pursued free-standing unfair method of competition claims outside of the most well-accepted areas, partly because the antitrust laws themselves have in the past proved flexible and capable of reaching most anticompetitive conduct. However, concern over class actions, treble damages awards, and costly jury trials have caused many courts in recent decades to limit the reach of antitrust. The result has been that some conduct harmful to consumers may be given a "free pass" under antitrust jurisprudence, not because the conduct is benign but out of a fear that the harm might be outweighed by the collateral consequences created by private enforcement. For this reason, we have seen an increasing amount of potentially anticompetitive conduct that is not easily reached under the antitrust laws, and it is more important than ever that the Commission actively consider whether it may be appropriate to exercise its full Congressional authority under Section 5.

It has been understood for many years that Section 5 extends beyond the borders of the antitrust laws, and its broad reach is beyond dispute. Indeed, that broad authority is woven into the very framework of the Commission itself. When Congress passed the Federal Trade Commission Act in 1914, it specifically decided to create an agency that has broad jurisdiction to stop unfair methods of competition, and it balanced that broad authority by limiting the remedies available to the Commission.

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[1] Federal Trade Commission Act, 15 U.S.C. § 45. The complaint also includes a claim that Intel's conduct constituted an unfair act or practice in violation of Section 5.

Congress enacted Section 5 in light of court decisions whose reach had limited the effectiveness of the Sherman Act in contravention of Congressional intent.[2] Thus, Section 5 was clearly a Congressional effort to bolster enforcement and provide protection for competition and consumers beyond the parameters of the Sherman Act. In fact, the Court's *Sperry & Hutchinson* holding regarding the broad sweep of Section 5 authority was based in part on the clear legislative history of the statute. *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 239-44 (1972). For example, Senator Cummins, one of the bill's main proponents, was asked on the Senate floor "why, if unfair competition is in restraint of trade, [are we] attempting to add statute to statute and give a further remedy for the violation of the [Sherman Act]?" Senator Cummins replied that the concept of "unfair competition" seeks:

> to go further [than "restraints of trade"] and make some things offenses that are not now condemned by the antitrust law. That is the only purpose of Section 5 – to make some things punishable, to prevent some things, that can not [sic] be punished or prevented under the antitrust law.[3]

Echoing this point, he later described Section 5 as a new substantive law that would involve the Commission in activities beyond the enforcement of antitrust law.[4] Many other legislators similarly expressed their intent and understanding that Section 5 would extend beyond the Sherman Act. *See, e.g.,* 51 CONG. REC. 14,333 (1914) (statement of Sen. Kenyon, remarking that the proposed federal trade commission "can take hold of matters that not in themselves are sufficient to amount to a monopoly or to amount to restrain [sic] of trade"); 51 CONG. REC. 14,329 (1914) (statement of Sen. Nelson, stating that the FTC Act "can be used in a lot of cases where there is no trust or monopoly"); 51 CONG. REC. 12,135 (1914) (statement of Sen. Newlands, observing that although "[a]ll agree that while the Sherman law is the foundation stone of our policy on [appropriate business conduct], additional legislation is necessary").

Of course, even though the Commission has broad authority under Section 5, the Commission is well aware of its duty to enforce Section 5 responsibly. We take seriously our mandate to find a violation of Section 5 only when it is proven that the conduct at issue has not only been unfair to rivals in the market but, more important, is likely to harm consumers, taking into account any efficiency justifications for the conduct in question. Section 5 is clearly broader than the antitrust laws, but it is not without boundaries, and the Commission will clearly describe and stay within those boundaries if this case comes before it to review.

Finally, the Commission recognizes that lengthy trials create uncertainty in the marketplace, and that this uncertainty has the potential to be particularly disruptive given the rapid pace of innovation in high-technology markets. In addition, Intel itself has a

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[2] *See generally*, *Rambus, Inc.*, Dkt. No. 9302, slip op. at 2-5 (Aug. 2, 2006) (concurring statement of then Commissioner Leibowitz), *available at* http://www.ftc.gov/os/adjpro/d9302/060802rambusconcurringopinionofcommissionerleibowitz.pdf

[3] 51 CONG. REC. 12,454 (1914) (statement of Sen. Cummins).

[4] *Id.* at 12,613 (statement of Sen. Cummins).

legitimate interest in seeing this matter resolved quickly. The Commission is fully committed to a speedy resolution of this action. We are bringing this case under the Commission's recently adopted Part 3 rules of practice, and we expect that a trial on the merits will begin within nine months, and a Commission decision will be issued within twenty months. This schedule is substantially more rapid than the far lengthier process usually followed in federal court antitrust litigation.

**Concurring and Dissenting Statement of Commissioner J. Thomas Rosch**
*In the Matter of Intel Corporation*
*Docket No. 9341*

**I.**

I concur in the issuance of a Section 5 complaint challenging an alleged course of conduct by Intel Corporation ("Intel") to maintain monopoly power in the markets for central processing units ("CPUs") in computers and at least near-monopoly power in markets for computer graphics products. In accordance with Section 5, I have concluded that there is reason to believe that the alleged course of conduct occurred and that issuance of a pure Section 5 complaint challenging that alleged conduct would be in the public interest. *See* 15 U.S.C. § 45(b) (authorizing the Commission to file a complaint where (1) it has "reason to believe" an antitrust violation has occurred, and (2) where "it shall appear to the Commission that a proceeding by it in respect thereof would be to the interest of the public"). The Supreme Court has held that Section 5 is broader than the Sherman or Clayton Acts, which can be enforced by both private and public plaintiffs. *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 239 (1972). However, the reach of Section 5, like any other statute, is not unlimited. I think the Commission can and should define those limitations as they apply to this case.

In my view, there are four considerations that warrant the application of Section 5 here. First, this is not a case where harm to competition can easily be segregated from harm to competitors. The markets alleged in this case and Intel's alleged position in those markets are extraordinarily concentrated: the CPU markets are duopoly markets in which Intel and Advanced Micro Devices ("AMD") are the only meaningful participants; the graphics products markets are likewise highly concentrated markets in which Intel, AMD, and Nvidia Corporation ("Nvidia") are the only meaningful competitors. Significantly, Intel has monopoly power in the CPU markets and near-monopoly power in the computer graphics product markets and, judging from the allegations in the complaint, the entry barriers surrounding these markets are remarkably high. Under those unique circumstances, the oft-repeated admonition that the Sherman and Clayton Acts protect competition, not competitors, and the federal courts' attendant disinclination to protect competitors in cases brought under those statutes, do not fit well. If the firm with monopoly or near-monopoly power (here, allegedly Intel) engages in an exclusionary and unjustifiable course of conduct that hurts its only competitor in the CPU markets (here, allegedly AMD) or its only two competitors in the computer graphics product markets (here, allegedly AMD and Nvidia), given the uncommonly high entry barriers, that exclusionary conduct harms competition too, by inhibiting those rivals from constraining the exercise of monopoly power.

Second, although Intel's alleged conduct led to higher prices in the CPU markets, that alleged conduct can still be within the Commission's Section 5 powers even if Intel cannot be said to have caused price increases. To be sure, most conventional Section 2 cases alleging monopoly maintenance or attempted monopolization rise or fall on proof of higher prices – if for no other reason than that kind of injury is easiest to measure. But that is not the only kind of consumer injury with which a law enforcement agency like the Commission should be concerned. The Commission must also be concerned with whether a course of conduct by a firm with monopoly power reduces consumer choice by reducing alternatives. That is true whether the "consumer" suffering the reduction in choice is an original equipment manufacturer ("OEM") or an end user of computer equipment that buys equipment from the OEM. Thus, if and to the extent that an exclusionary course of conduct by a firm with monopoly power results in that less measurable form of consumer injury, Section 5 is the most appropriate vehicle for the analysis, and the Commission, with its expertise and experience, is the most appropriate plaintiff to make that determination.

Third, the complaint here alleges that Intel engaged in an exclusionary course of conduct. That is a claim with clearly identifiable elements that most logically resides in the Commission's Section 5 authority. Simply put, in my view it is improper to slice and dice each constituent part of the alleged course of conduct to determine whether it, standing alone, had the purpose or effect to hinder competition and injure consumers in violation of Section 2: the constituent parts did not stand alone, and both their effects on Intel's few alleged rivals and their consequent impact on consumer choice can only be assessed by examining the effects of Intel's alleged course of conduct as a whole. Although a number of courts have disparaged "course of conduct" claims made under Section 2 as mere "monopoly broth" claims or claims that "0 plus 0 plus 0 equal 1," that militates in favor of the Commission exercising its discretion and expertise to use Section 5 to reach such a course of conduct. Indeed, under those circumstances, a Section 5 "course of conduct" claim may be viewed much as the "invitation to collude" cases that the Commission has pursued as pure Section 5 cases in order to reach conduct that the Sherman Act may not otherwise reach. Lest there be any misunderstanding, Intel must be given the opportunity to show that any injury to competition or to consumers was offset by efficiencies that it reasonably could have achieved only by engaging in the conduct causing those consequences. But that defense does not justify altogether eschewing a course of conduct claim under Section 5.

Fourth, I believe that Intel's intent here is relevant in assessing its liability. The Second Circuit, for example, has held that a respondent's state of mind is not only relevant, but must be taken into account, to determine whether the respondent's conduct constitutes an "unfair method of competition" under Section 5. *E.I. DuPont de Nemours & Co. v. FTC*, 729 F.2d 128, 138-40 (2d Cir. 1984). Properly read, I think that *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985), holds that such an intent would be relevant in a Section 2 case. *Id.* at 610-11 (defendant's practices "support[ed] an inference that [the defendant] 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"). Yet some Section 2 cases have said that an analysis of the defendant's intent is irrelevant in a Section 2 case. Indeed, it can be argued that the Commission's antitrust expertise and experience makes it a more dispassionate and superior judge of that evidence than a lay jury in a Section 2 case.

## II.

Although I concur in the issuance of a complaint based on pure Section 5 claims, I respectfully dissent insofar as the complaint also contains Section 2 "tag-along" claims. To be clear, my reasons for doing so are not based on the fact that I lack a "reason to believe" that a Section 2 violation has occurred; instead, I dissent from the addition of the Section 2 claims on public policy grounds.

First, I see no advantage to adding the Section 2 claims. To be sure, there is favorable Section 2 case law that supports each constituent part of the course of conduct that is pled. More specifically, there is Section 2 case law condemning the use of loyalty discounts and kit pricing by a firm with monopoly power, *LePage's Inc. v. 3M*, 324 F.3d 141, 154-57, 162-63 (3d Cir. 2003) (en banc); *Masimo Corp. v. Tyco Health Care Group, L.P.*, 2009 U.S. App. LEXIS 23765, *6-8 (9th Cir. Oct. 28, 2009); the use of deception by such a firm, *United States v. Microsoft Corp.*, 253 F.3d 34, 76-77 (D.C. Cir. 2001) (en banc); refusals to deal, *Aspen Skiing Co.*, 472 U.S. at 603-10, including refusals to license by such a firm, *Image Tech. Servs. v. Eastman Kodak Co.*, 125 F.3d 1195, 1216, 1218-20 (9th Cir. 1997); raising rivals' costs, *United States v. Delta Dental*, 943 F. Supp. 172, 179-82 (D.R.I. 1996) (most favored nations clause case brought under the Sherman Act, albeit Section 1); and product degradation by such a firm, *C.R. Bard, Inc. v. M3 Sys., Inc.*, 157 F.3d 1340, 1369-72 (Fed. Cir. 1998). Indeed, there is authority in the Section 2 case law for a course of conduct claim. *Microsoft Corp.*, 253 F.3d at 78; *Caldera, Inc. v. Microsoft Corp.*, 72 F. Supp. 2d 1295, 1318 (D. Utah 1999). But there is no reason why that case law cannot be invoked to support a Section 5 course of conduct claim where the Commission alleges that a course of conduct by a firm with monopoly power constitutes an "unfair method of competition."

Second, it cannot be said that including the Section 2 claims (as opposed to a clearly defined Section 5 course of conduct claim) means that the outcome of this litigation will provide more predictability to the business community by somehow providing better notice of the type of conduct that the antitrust laws preclude. *See Boise Cascade Corp. v. FTC*, 637 F.2d 573, 582 (9th Cir. 1980) (rejecting the use of Section 5 where it would "blur" Sherman Act distinctions that were "well-forged"); *DuPont*, 729 F.2d at 138-39 (expressing concern that application of Section 5 might upset settled antitrust principles and thus lead to unpredictability); *Official Airline Guides, Inc. v. FTC*, 630 F.2d 920, 927 (2d Cir. 1980) (same). Intel maintains that the Section 2 case law respecting these constituent elements of its alleged course of conduct is favorable to it. If and to the extent that is true, it cannot be said that the relevant Section 2 case law is settled and predictable. A well-defined Section 5 course of conduct claim can provide just as much guidance.

Third, and most importantly, the collateral consequences of including any Section 2 claims are very unfavorable for both Intel and the Commission. Intel currently faces the treble damage suits filed by the New York Attorney General under Section 2 in the United States District Court in Delaware in addition to a number of Section 2 treble damage class actions that have been filed there. The Commission should not enable those plaintiffs to free ride off of the Commission's work. Nor should it put itself in a position where an unfavorable outcome in those cases may be cited against it. Neither of those consequences can occur if the Commission proceeds solely under Section 5: the Delaware treble damage actions cannot proceed under Section 5 because only the Commission has the power to enforce Section 5. Indeed, it can be argued that where, as here, private litigation is pending under Section 2, as a matter of policy the Commission should not spend public resources on a duplicate claim.

Beyond that, as my colleagues, Chairman Leibowitz and more recently Commissioner Kovacic have pointed out, the Supreme Court has steadily been "shrinking" the ambit of the Sherman Act both procedurally and substantively. *See, e.g.*, *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 558-61 (2007); *Credit Suisse Sec. (USA) v. Billing*, 551 U.S. 264, 281-82 (2007). By all accounts, these changes are, partially at least, due to the Court's concern about the Sherman Act's application by juries and generalist federal district courts. Regardless of whether one shares that concern about private Sherman Act enforcement, it is undeniable that this jurisprudence "slops over" to public enforcement. That is so because insofar as the federal agencies prosecute their cases under the Sherman Act, they must proceed under the same statutes that private plaintiffs invoke. That consequence, however, can be minimized – if not avoided altogether – if the Commission proceeds under Section 5 alone. Thus, although I have also concluded that there is reason to believe that the alleged conduct also violates Section 2 the Sherman Act, I have concluded that insofar as this case proceeds on the basis of any Sherman Act "tag-along" claims, the Commission acts contrary to the public interest.

PROTECTING AMERICA'S CONSUMERS



# FTC Settles Charges of Anticompetitive Conduct Against Intel

## Provisions are Designed to Foster Competition in the Computer Chip Business

FOR RELEASE

August 4, 2010

The Federal Trade Commission approved a settlement with Intel Corp. that resolves charges the company illegally stifled competition in the market for computer chips. Intel has agreed to provisions that will open the door to renewed competition and prevent Intel from suppressing competition in the future.

The settlement goes beyond the terms applied to Intel in previous actions against the company and will help restore competition that was lost as a result of Intel's alleged past anticompetitive tactics. At the same time, the settlement will leave the company room to innovate and offer competitive pricing.

"This case demonstrates that the FTC is willing to challenge anticompetitive conduct by even the most powerful companies in the fastest-moving industries," said Chairman Jon Leibowitz. "By accepting this settlement, we open the door to competition today and address Intel's anticompetitive conduct in a way that may not have been available in a final judgment years from now. Everyone, including Intel, gets a greater degree of certainty about the rules of the road going forward, which allows all the companies in this dynamic industry to move ahead and build better, more innovative products."

The FTC settlement applies to Central Processing Units, Graphics Processing Units and chipsets and prohibits Intel from using threats, bundled prices, or other offers to exclude or hamper competition or otherwise unreasonably inhibit the sale of competitive CPUs or GPUs. The settlement also prohibits Intel from deceiving computer manufacturers about the performance of non-Intel CPUs or GPUs.

The FTC settlement goes beyond those reached in previous antitrust cases against Intel in a number of ways. For example, the FTC settlement order protects competition and not any single competitor in the CPU, graphics, and chipset markets. It also addresses Intel's disclosures related to its compiler – a product that plays an important role in CPU performance. The settlement order also ensures that manufacturers of complementary products such as discrete GPUs will be assured access to Intel's CPU for the next six years.

The FTC sued Intel in December 2009 alleging that the company used anticompetitive tactics to cut off rivals' access to the marketplace and deprive consumers of choice and innovation in the microchips that comprise computers' central processing unit, or CPU. These chips are critical components that often are referred to as the "brains" of a computer. The action also challenged Intel's conduct in markets for graphics processing units and other chips.

The FTC alleged that Intel's anticompetitive practices violated Section 5 of the FTC Act, which is broader than the antitrust laws and prohibits unfair methods of competition and deceptive acts and practices in commerce. Unlike an antitrust violation, a violation of Section 5 cannot be used to establish liability for plaintiffs to seek triple damages in private litigation against the same defendant.

Under the settlement, Intel will be prohibited from:

- conditioning benefits to computer makers in exchange for their promise to buy chips from Intel exclusively or to refuse to buy chips from others; and
- retaliating against computer makers if they do business with non-Intel suppliers by withholding benefits from them.

In addition, the FTC settlement order will require Intel to:

- modify its intellectual property agreements with AMD, Nvidia, and Via so that those companies have more freedom to consider mergers or joint ventures with other companies, without the threat of being sued by Intel for patent infringement;
- offer to extend Via's x86 licensing agreement for five years beyond the current agreement, which expires in 2013;
- maintain a key interface, known as the PCI Express Bus, for at least six years in a way that will not limit the performance of graphics processing chips. These assurances will provide incentives to manufacturers of complementary, and potentially competitive, products to Intel's CPUs to continue to innovate; and
- disclose to software developers that Intel computer compilers discriminate between Intel chips and non-Intel chips, and that they may not register all the features of non-Intel chips. Intel also will have to reimburse all software vendors who want to recompile their software using a non-Intel compiler.

The FTC vote approving the proposed settlement order was 4-0, with Commissioner William E. Kovacic recused. The order will be subject to public comment for 30 days, until September 7, 2010, after which the Commission will decide whether to make it final. Comments should be sent to: FTC, Office of the Secretary, 600 Pennsylvania Avenue, N.W., Washington, DC 20580. To submit a comment electronically, please click on: https://ftcpublic.commentworks.com/ftc/intel/.

**NOTE:** A consent agreement is for settlement purposes only and does not constitute an admission of a law violation. When the Commission issues a consent order on a final basis, it carries the force of law with respect to future actions. Each violation of such an order may result in a civil penalty of up to $16,000.

The FTC's Bureau of Competition works with the Bureau of Economics to investigate alleged anticompetitive business practices and, when appropriate, recommends that the Commission take law enforcement action. To inform the Bureau about particular business practices, call 202-326-3300, send an e-mail to antitrust@ftc.gov, or write to the Office of Policy and Coordination, Room 383, Bureau of Competition, Federal Trade Commission, 600 Pennsylvania Ave, N.W., Washington, DC 20580. To learn more about the Bureau of Competition, read "Competition Counts" at http://www.ftc.gov/competitioncounts.

100 YEARS

PROTECTING AMERICA'S CONSUMERS

MAIN MENU SEARCH

# FTC Approves Modified Intel Settlement Order

FOR YOUR INFORMATION

November 2, 2010

Following a public comment period, the Federal Trade Commission has approved a modified settlement order resolving charges that Intel Corp. illegally stifled competition in the market for computer chips. The FTC Order will open the door to renewed competition and prevent Intel from suppressing competition in the future.

After considering public comments, the FTC modified the proposed order to allow Intel to manufacture and sell a chip that it had in development before the proposed order was negotiated, but that would violate that order because it does not contain a required interface. The FTC modified the order to allow Intel to ship this product until June 2013. All future generations of this chip must fully comply with all specifications of the final Order.

The Commission vote approving the final Order was 4-0-1, with Commissioner William E. Kovacic recused. The Order can be found on the FTC's website and as a link to this press release. The FTC also authorized the staff to send letters to members of the public who commented on the proposed order, issued in August 2010. (FTC Docket No. 9341; the staff contact is Richard Feinstein, Bureau of Competition, 202-326-3658; see press release dated August 4, 2010, at http://www.ftc.gov/opa/2010/08/intel.shtm. Copies of the public comments can be found at http://www.ftc.gov/os/comments/intelcorp/index.shtm.)

Copies of the documents mentioned in this release are available from the FTC's website at http://www.ftc.gov and from the FTC's Consumer Response Center, Room 130, 600 Pennsylvania Avenue, N.W., Washington, DC 20580. Call toll-free: 1-877-FTC-HELP.

(FYI 46.2010.wpd)

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