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Monopoly and Competition: Tilting the Law Towards a More Competitive Economy

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MONOPOLY AND COMPETITION: TILTING THE LAW TOWARDS A MORE COMPETITIVE ECONOMY

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The big antitrust case has earned the reputation of being unmanageable and untriable, a guzzler of scarce enforcement resources, a demoralizer of trial lawyers and litigating parties, and a blight on the credibility of the litigation process.[1] The need to address the causes of attenuation of the complex antitrust case, and related concerns,[2] led the President of the United States to issue Executive Order 12022 establishing the National Commission for the Review of Antitrust Laws and Procedures[3] (National Commission or Commission).

In essence, the President asked the Commission: What has gone wrong with the big antitrust case, and what should be done to correct the failings? What procedural and substantive revisions are necessary or appropriate to avoid runaway antitrust litigation and to deal more effectively

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[1] *See* NATIONAL COMMISSION FOR THE REVIEW OF ANTITRUST LAWS AND PROCEDURES, REPORT TO THE PRESIDENT AND THE ATTORNEY GENERAL 11-14 (Jan. 22, 1979) [hereinafter cited as COMMISSION REPORT], *reprinted in* 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 3-4.

The government case against IBM is in its eleventh year. United States v. International Bus. Mach. Corp., 69 Civ. 200 (S.D.N.Y., filed Jan. 17, 1969). The cereals case has passed its seventh anniversary. *In re* Kellogg Corp., [1970-1973 Transfer Binder] TRADE REG. REP. (CCH) ¶ 19,898, Dkt. 8883 (Complaint issued Apr. 26, 1972). The case against the major oil firms has passed its sixth anniversary. *In re* Exxon Corp., [1973-1976 Transfer Binder] TRADE REG. REP. (CCH) ¶ 20,388, Dkt. 8943 (Complaint announced July 17, 1973). The case against AT&T is in its sixth year. United States v. American Tel. & Tel. Co., No. 74-1698 (D.D.C., filed Nov. 20, 1974).

[2] The related concerns included a perceived need to make remedies in the complex antitrust case more effective, and to examine the desirability of the various exemptions from the antitrust laws. *See* Exec. Order No. 12022, § 2(a)(1), (2), 3 C.F.R. 155, 156 (1977), *amended by* Exec. Order No. 12052, 42 Fed. Reg. 15,133 (1978). The Executive Order as amended appears in COMMISSION REPORT, *supra* note 1, at 319, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 92.

[3] *See* note 2 *supra*. Among other things, the President charged the Commission to consider "revision of procedural and substantive rules of law" to expedite antitrust litigation, and in doing so, to reconsider the standards that govern attempts to monopolize under § 2 of the Sherman Act. COMMISSION REPORT, *supra* note 1, at 320, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 92.

and efficiently with the merits of the alleged violations, and relief if a violation is found?

My fellow Commissioners and I heard testimony addressed to these questions. Some who testified identified unbounded time as a major problem. They proposed that the trial judge actively manage the complex case and set an early date for commencement of the trial. We agreed, and adopted these recommendations.[4] Some who testified identified pressures on lawyers as a major problem; pressures to leave no stone unturned; pressures to strive towards endless complication and delay if delay benefits one's client. We agreed, and recommended that ethical codes and disciplinary rules should recognize that lawyers have a duty to the administration of justice to expedite, and that it is unethical to delay for the sake of delay. We recommended harsher penalties against attorneys for willful, dilatory practices.[5]

It was apparent, however, that the core problems reflected by the unusual duration of some of the most significant and visible antitrust cases lay much deeper than judicial management and lawyers' tactics. Most of these cases involve claims of monopolization and attempts to monopolize in violation of section 2 of the Sherman Act.[6] We asked whether the state of the substantive law of section 2 was a core problem and we heard testimony, shared views, and debated the desirability of changes in the substantive law. We made recommendations for revision of the substantive law.[7]

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[4] COMMISSION REPORT, *supra* note 1, at 27-40, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 8-11.

[5] COMMISSION REPORT, *supra* note 1 at 81-98, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 23-28. Bills pending in Congress would adopt some of the Commission's recommendations. Antitrust Procedural Improvements Act of 1979, S. 390, H.R. 4046-48 (96th Cong., 1st Sess.), 125 CONG. REC. 51345 (daily ed. Feb. 8, 1979).

[6] 15 U.S.C. § 2 (1976). Section 2 also prohibits combinations and conspiracies to monopolize, a provision not addressed in this article.

[7] It is not obvious that all of the problems of the big antitrust case will be solved by active judicial management, judicially imposed time limits, greater sensitivity of lawyers to their ethical obligations, and clarification or change of the substantive law. A strong case can be made for measures giving parties to complex litigation a much stronger incentive to expedite. Private plaintiffs already have an incentive — prospect of equitable relief and financial gain, both of which come, if at all, only at the end of the case. However, government attorneys, defendants' attorneys and defendants do not ordinarily have strong incentives to make them end the litigation as quickly as possible. As for government attorneys, the pressures and rewards must come from within the Department of Justice and the Federal Trade Commission. As for defendants, delay is now generally profitable; at least, it is seldom unprofitable. The law could be changed to make delay costly and to reward speed. One suggestion is to internalize the externalities: compute the costs of court, judge and jury (which the government now subsidizes), and require the private parties, or the dilatory private party if blame can be assessed, to pay these costs. Also, the law could deny a tax deduction for litigation expenses, including attorneys fees. Finally, the law could require a pass-through of certain profits (for example, profits exceeding the current commercial rate of interest) derived during the course of the litigation from practices found to be illegal. If the defendant in the big antitrust case has the financial incentive to expedite, there is hope that even the big antitrust case will be tried expeditiously. *See* Testimony of E. Fox on H.R.

Although our inquiry into the state of the law was triggered in part by a procedural question, we did not recommend substantive change for the sake of making trials shorter. Rather, we reviewed substantive law because our inquiry into the causes of attenuation led us to do so, and we recommended substantive change because we considered change important to the long-run health of the competition system. Procedural efficiency would be a welcome by-product.

There was remarkable consensus among members of the Commission on the direction substantive change should take. A significant majority perceived that the law on monopoly and attempts to monopolize has been moving away from principles central to a competition system; that it has been moving toward toleration of a more rigid, less competitive and less dynamic economy.[8] The purpose of this article is to articulate the salient principles that influenced the Commission's substantive recommendations on monopoly and attempts to monopolize, to set forth the Commission's particular recommendations in these two areas, and to articulate the underpinnings and applications of these recommendations.

Summary of Guiding Principles

In principle, the National Commission believed that competition, not government regulation and not private monopoly power, should govern markets. The Commissioners opposed protecting inefficient firms from competition, and also opposed protecting monopoly firms from the incursions of competition. The Commission expressed its commitment to free enterprise and competitive markets for economic, social and political reasons, stating:

> These concepts [of competitive markets] are central to our most basic social and political values. In addition to fostering consumer welfare and allocative efficiency, competition is closely linked to democratic principles of individual initiative, free association, and dispersion of economic power. They have been aptly described by the Supreme Court as representing 'fundamental national economic policy' and a 'charter of economic freedom' of constitutional dimensions. We believe these principles continue to have overriding validity.[9]

Applying these concepts of competition to the problems of monopoly and attempts to monopolize, the Commission made the following observations and recommendations. First, as to treatment of monopoly, the Com-

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3271, 4046-50, Hearings before the Subcommittee on Monopolies and Commercial Law of the Committee on the Judiciary, House of Representatives, 96th Congress, 1st Sess., at 108 (Sept. 27, 1979).

[8] *See* COMMISSION REPORT, *supra* note 1, at 141-77, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 40-49.

[9] COMMISSION REPORT, *supra* note 1, at 177-78, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 50. *See also* note 8 *supra*.

mission perceived that the law as interpreted by a number of lower courts has become indulgent towards monopoly. The Commission considered that a system grounded in competition is and should be inhospitable to monopoly. The Commission therefore recommended to Congress consideration of a monopoly law explicitly providing for dissipation of substantial, persistent monopoly power upon challenge by the government.[10] Second, the Commission observed that the law as interpreted by a number of lower courts has become indulgent towards single-firm exercises of market power. Even acts threatening to produce monopoly have been condoned if they appear to produce short-run static efficiencies. The National Commission believed that a competitive system must be vigilant to prevent attempts to monopolize and other uses of market power that chill or otherwise impair competition. Accordingly it proposed modification of the attempt-to-monopolize law to proscribe certain single-firm acts, including pricing strategies, that significantly threaten competition.[11] This article

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[10] The full text of the Commission recommendation in this regard is:

> The appropriate Congressional committees should undertake an inquiry aimed at strengthening the ability of the Sherman Act to deal with persistent monopoly power. Such an inquiry should be based on the following principles:
>
> a. the chief goal of the Sherman Act monopolization provision is the dissipation of persistent monopoly power;
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> b. persistent monopoly power can be presumed to be maintained through deliberate conduct that would violate traditional Sherman Section 2 standards;
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> c. the current litigation process under Sherman Section 2 does not effectively remedy persistent monopoly power, in part because the need to prove culpable conduct leads to much evidence not relevant to the proof of monopoly power or the nature of effective relief and creates strong incentives for the government to focus its resources on the liability stage of a monopolization proceeding rather than relief;
>
> d. the adoption of a standard enabling the government to obtain structural relief on a showing of persistent monopoly power without the need to prove culpable conduct would rationalize monopolization litigation in accordance with the preceding principles, but would also raise the following issues, which should be examined by Congress before any specific statutory change is enacted:
>
> 1. the definition of monopoly power to be applied in using the standard;
> 2. the type and scope of defenses to be permitted and the stage of the litigation at which they should be permitted;
> 3. whether efficiency considerations should be permitted to affect the availability of structural relief where anticompetitive conduct has created or maintained the monopoly; and
> 4. the advisability of adopting a conduct-free liability standard in view of possible disincentives to business growth or public perceptions of unfairness.

COMMISSION REPORT, *supra* note 1, at 141-42, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 40.

[11] The Commission recommended:

> The "dangerous probability of success" necessary to establish an attempt to monopolize under Section 2 of the Sherman Act should not be interpreted as requiring proof of a high probability of actual monopoly, but rather a determination of

discusses, first, the recommendations on monopoly, and second, the recommendations on attempts to monopolize.

I. Monopoly

Section 2 of the Sherman Act enjoins: No person "shall monopolize."[12] Under current interpretations of this section, a firm with monopoly power in a defined market runs afoul of section 2 of the Sherman Act if it has achieved or maintained its monopoly power by "willfulness" or impermissable conduct,[13] rather than by superior skill, foresight and industry.[14] There is little or no consensus as to the meaning of "willfulness," and judicial definitions range from mere aggressive operation of the monopoly firm to illegal use of monopoly power.[15] If, however, a firm is found to have willfully gained or maintained monopoly power and thus to have monopolized in violation of section 2, it is relatively well settled law that the monopoly power should be dissipated by mandatory injunction.[16]

This section will deal first with the relationship between the Executive Order and the Commission's study of monopoly, and, second, with the merits of the Commission's substantive proposal.

The Executive Order creating the National Commission directed it to study and make recommendations, within the framework of existing antitrust laws, regarding: "Revision of procedural and substantive rules of law needed to expedite the resolution of complex antitrust cases and development of proposals for making the remedies available in such cases more effective. . . ."[17] Within this framework the Commission considered whether substantive change in the monopoly law is desirable on the merits and whether desirable substantive change is likely to expedite case resolution and offer more effective remedies.

> whether the defendant has significantly threatened competition. Such determination should be based on the weighing of various factors including the defendant's intent, market power, and conduct. Additionally, evidence regarding the relationship of price to marginal cost properly should be considered in assessing pricing practices alleged to form the basis of an attempt, but proof that such prices were below marginal cost should not be a prerequisite to proof of a violation. In order to ensure uniform adoption of these standards, the Sherman Act should be amended to incorporate them.

Commission Report, supra note 1, at 141, 897 Antitrust & Trade Reg. Rep. (BNA) (Special Supp.) at 40.

[12] 15 U.S.C. § 2 (1976).

[13] "Willful" is used hereinafter to include both "bad intent" and "bad conduct."

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

[15] *Compare* United States v. Aluminum Co. of America, 148 F.2d 416, 431-32, (2d Cir. 1945), *and* Greyhound Comp. Corp. v. IBM Corp., 559 F.2d 488, 503-04 (9th Cir. 1977), *cert. denied,* 434 U.S. 1040 (1978), *with* Telex Corp. v. IBM Corp., 510 F.2d 894, 915-19 (10th Cir.), *cert. dismissed,* 423 U.S. 802 (1975); California Comp. Prod., Inc. v. IBM Corp., [1979-1] Trade Cas. (CCH) ¶ 62,713 at 77,975 (9th Cir. 1979); Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 274, 281 (2d Cir. 1979), *cert. denied,* 48 U.S.L.W. 3517 (1980).

[16] *See* United States v. United Shoe Mach. Corp., 391 U.S. 244, 250-52 (1968).

[17] Commission Report, *supra* note 1, at 320, 897 Antitrust & Trade Reg. Rep. (BNA) (Special Supp.) at 92.

The Commission's hearings on this issue opened with testimony by John J. Flynn, Professor of Law at the University of Utah. Professor Flynn testified that, in his view, monopoly status itself is an evil to be remedied. He urged:

> In my opinion, one of the most important substantive changes the Commission can consider is the elimination of the conduct requirement for proving monopolization in government cases. It is no revelation to this Commission that several recent monopolization cases have consumed and will continue to consume enormous amounts of time and resources. My impression of several of these and earlier cases is that upwards of one-third to one-half of the cost and delay of those cases could be avoided — without compromising the soundness of the results — by eliminating the conduct requirement.[18]

The Commission's attention thus was focused on the question: What is or should be the heart of a monopoly violation? If monopoly status is an evil to be remedied, the courts and the parties are trying a diversionary issue — willfulness. If the plaintiff has the burden of proving a monopolist's willfulness, the discovery period and the trial itself will tend to be far longer than that which would obtain if willfulness were ruled out as a necessary component of the case.[19]

Proof of willfulness does indeed tend to be a major burden of plaintiffs. In monopoly cases, the plaintiffs' lawyers seek as much evidence as they get of the defendant firm's evil intent and predation. They search for the proverbial smoking gun. If they have the financial resources, they leave no stone unturned; the more "evilness" they can find, the more likely they are to prove defendant's willfulness and thus to win the battle of the facts. They search the record of defendant's history, conduct and intent to show that defendant was impure and predatory and willed its monopoly and its competitors' demise.

Monopoly-sized defendants may welcome this focus. The spotlight is shifted from their monopoly status. They muster their forces to prove their "goodness." The trial of willfulness provides the opportunity for inordinate lapses of time, during which markets may change, personnel may change, administrations may change, and both fervor and stamina for prosecution may decline.

In the process millions of documents are exchanged;[20] thousands of

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[18] Prepared Statement of Professor John J. Flynn to the Commission (July 1978), at 3. The statement of and testimony by Professor Flynn to the Commission are cited at COMMISSION REPORT, *supra* note 1, at 171-74, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 45-49.

[19] *Contra*, testimony before the Commission of Professor Robert H. Bork, Sept. 13, 1978.

[20] In United States v. IBM, 69 Civ. 200 (S.D.N.Y., filed Jan. 17, 1969), pending in the United States District Court for the Southern District of New York, 30 million pages of documents were exchanged by the parties. COMMISSION REPORT, *supra* note 1, at 42, 897 ANTITRUST & TRADE REG. REP.(BNA) (Special Supp.) at 12.

depositions are taken;[21] and, at trial, tens of thousands of transcript pages supporting each party's contentions are filled.[22] When the parties rest, the evidence of willfulness is typically ambiguous. The case is likely to turn on the fact-finder's perception of whether the defendant was "bad," or "bad enough."

At the end of the process, the judge and the teams of lawyers are likely to be so exhausted that, if liability is found, relief becomes a tag-on issue, addressed as a question of appropriate punishment rather than as a central task to restore competition.

If "willfulness" is not a meaningful issue, then it is an expensive diversion. It imposes enormous costs of time and money in the short run. It threatens to impose the costs of monopoly in the long run, for the monopoly that is not proved predatory is validated, and the monopoly firm is left free to continue to take its economic toll. If "willfulness" is a diversionary issue, it should be eliminated as a necessary element of the plaintiff's case.

The Commission heard testimony[23] and deliberated on whether persistent monopoly power itself or only willful monopoly should offend the law. After debate, the National Commission recommended that Congress "should undertake an inquiry aimed at strengthening the ability of the Sherman Act to deal with persistent monopoly power."[24] Specifically, the Commission recommended that Congress consider the desirability of providing for a government civil right of action to seek dissipation of monopoly power upon proof that the monopoly exists and persists.[25] Willfulness or bad conduct would not be a requisite part of the case.[26] In so recom-

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[21] In *United States v. IBM*, 1,270 depositions were taken. *Id.* 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 12.

[22] As of the end of August 1979, the trial transcript in *United States v. IBM* was nearly 100,000 pages long. More than 7,000 objections had been made to testimony and documents, requiring a corresponding number of rulings on objections by the trial judge. *I.B.M. Brief Disputed By U.S. as Distorted,* The New York Times, Aug. 28, 1979, D4, Col. 1, 2.

[23] Professors Walter Adams, Phillip E. Areeda, John J. Flynn, Harvey J. Goldschmid, Louis B. Schwartz, and Oliver E. Williamson are among those who testified in support of an antimonopoly law. Professor Robert H. Bork was among those who testified against an antimonopoly law. Professor Thomas E. Kauper expressed deep concern that dissolution of a monopoly might leave the market no better off and testified also that conduct evidence will be relevant in proving market power and economies of scale. Commission Hearings, Sept. 13, 1978 and Oct. 17, 1978.

[24] *See* note 10 *supra.*

[25] *Id.* Dissenting views of Commissioners Hatch and Javits appear in the Appendix to the COMMISSION REPORT, *supra* note 1, at 349-55, 385-401, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 99-101, 109-15.

[26] The Commission's recommendation was limited in the following respects. First, the Commission did not contemplate that the recommendation would supersede existing law condemning anticompetitive conduct that produces or maintains monopoly. Second, the recommendation does not apply to natural monopoly. Third, the Commission did not address the question of a private right of action against substantial, persistent monopoly. Fourth, the recommendation calls for consideration of a civil right of action; criminality was not contemplated and was thought undesirable.

Although recent interpretations of § 2 do not run in this direction, *see* note 15 *supra*, § 2 mending, some Commissioners agreed with Professor Flynn that monopoly status itself is the evil to be remedied. Others believed that persistent monopoly status presumptively reflects deliberate anticompetitive conduct. Some believed both propositions to be true.[27] This author subscribes to the first view; that is, monopoly status is undesirable.

The remainder of this section addresses the proposition, reflected in the Commission's recommendation, that substantial, persistent monopoly power should be dissipated in appropriate ways that are likely to increase competition, efficiency and progressiveness.

Is Monopoly Undesirable?

"Hatred of monopoly is one of the oldest American political habits. . . ."[28] Monopoly is disliked for social, economic and political reasons. The deep roots of distrust of monopoly are reflected in Senator Sherman's exhortation in 1890: "If we will not endure a king as a political power we should not endure a king over the production, transportation and sale of any of the necessaries of life."[29] Monopoly is antithetical not only to general democratic goals of dispersion of power, but also to the

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could be construed to reach structural monopoly. Decisional support for the Commission's recommendation may be found in United States v. Aluminum Co. of America, 148 F.2d 416, 427-32 (2d Cir. 1945), *adopted in significant part in* American Tob. Co. v. United States, 328 U.S. 781, 813-14 (1946); United States v. United Shoe Mach. Corp., 110 F. Supp. 295 (D. Mass. 1953), *aff'd per curiam,* 347 U.S. 521 (1954); Borden Inc. [1976-79 Transfer Binder] TRADE REG. REP. (CCH) ¶ 21,490 (FTC 1978). *See* Northern Sec. Co. v. United States, 193 U.S. 197, 339, 351 (1904). *See also* 3 P. AREEDA & D. TURNER, ANTITRUST LAW ¶ 615 (1978) [hereinafter cited as AREEDA & TURNER].

The legislative history on point is not clear. Some portions support the view that the Sherman Act was intended to prohibit monopoly, and others do not.

Senator Edmunds, who was the principal drafter of the bill that became the law, said in the debates:

> I am in favor, most earnestly in favor, of doing everything that the Constitution of the United States has given Congress power to do, to repress and break up and destroy forever the monopolies. . .because in the long run, however seductive they may appear in lowering prices to the consumer for the time being, all human experience and all human philosophy have proved that they are destructive of the public welfare and come to be tyrannies, grinding tyrannies. . . .

21 CONG. REC. 2726 (1890).

Congressman Fithian of Illinois reinforced the view that even the innocent monopoly harms the consumer. Quoting a political economist, he said: "Whenever monopoly is dominant, the incentive for improvement and skill is deadened. It is only when competitors contend with each other for the favor of the consumer that they are stimulated to attract that consumer by presenting him with wares both skillfully and cheaply made." 21 CONG. REC. 4102 (1890).

On the other hand, Senator Hoar assumed that anyone who "got the whole business because nobody could do it as well as he could was not a monopolist. . . ." 21 CONG. REC. 3151 (1890).

[27] *See* COMMISSION REPORT, *supra* note 1, at 151-76, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 45-50.

[28] Letwin, *Congress and the Sherman Antitrust Law: 1887-1890,* 23 U. CHI. L. REV. 221, 226 (1956).

[29] *Quoted in* H. THORELLI, THE FEDERAL ANTITRUST POLICY 180 (1955).

consumer interest. It is for the latter reason that the antimonopoly principle enlists the support of microeconomists and others centrally concerned with the efficient functioning of markets.[30] This article deals, hereafter, only with the economic case against monopoly.

The economic case against toleration of persistent monopoly status is compelling. The monopoly firm has the power to, and will predictably, limit production and increase price. The consumer is hurt by scarcity, high price, and lack of alternatives. In addition, the monopolized market suffers from the absence of the dynamic competitive forces that constantly pressure firms in competitive markets to eliminate waste and to provide better and cheaper alternatives.

As Professors Areeda and Turner cogently make the case against monopoly:

> The evils of monopoly are largely independent of the manner in which it is achieved or maintained. Even innocently obtained monopoly can and likely will produce monopoly pricing. . . .
>
> To condemn monopolization is necessarily to abhor monopoly itself, the process of achieving it, or both. Chief Justice White and later Judge Learned Hand thought that mere monopoly was itself the object of statutory concern, although not necessarily unlawful on that account.[31]

Quoting Judge Learned Hand, Areeda and Turner state: "[T]here can be no doubt that the vice of restrictive contracts and of monopoly is really one, it is the denial to commerce of the supposed protection of competition."[32]

There is broad consensus, because of the acknowledged evils of monopoly, that the law should deter the creation of monopoly by prohibiting attempts to monopolize, anticompetitive mergers, and various uses of leverage. But if monopoly occurs in spite of laws that deter it, one must face the harder question of whether and when to dissipate existing monopoly.

There is likewise broad consensus that if the monopoly was wrongfully achieved or maintained, the courts can and should act to restore competition. The law so applied tends to deter anticompetitive acts. But where the monopolist cannot be proved culpable, consensus breaks down. Some express concern that dissipation of a "good" monopoly would be "unfair" to the winner of the race; that an antimonopoly law not predicated on bad acts will chill lawful competition by leading firms; and that dislocation costs and efficiency loss that may attend relief against monopoly are likely to outweigh the benefits of dissipation. It is argued also that an antimonopoly law is not needed because monopoly not supported by the government does not exist or is transient; and that such a law is not wise because it will prompt enforcers to gerrymander markets for the sake of

[30] *See, e.g.*, 3 AREEDA & TURNER, *supra* note 26, at ¶ 615.

[31] *Id.* at ¶ 614 at 35; ¶ 615 at 36-37.

[32] *Id.* at 37 (Footnote omitted).

trustbusting, bringing down the good with the bad.

We come to the second central question: What are the costs of dissipating monopoly, and will the benefits outweigh the costs. The question may be addressed by dealing with the objections to dissipation.

Unfairness

It is strenuously argued that dissipation of a "good" monopoly is simply unfair. Thus, a distinguished trial lawyer from Chicago, Fred H. Bartlit, testified before the Commission:

> I do not think we can emphasize too much the simple, fundamental reason for the conduct requirement. . . . And this has been said again and again and again, but it deserves repetition. It is not right to tell somebody to compete, to tell them to compete fairly, and when they compete fairly and win, to penalize them for it. This just is not sensible. And smart judges and smart legislators over a long period of time have felt comfortable with the [conduct] rule that has evolved. When somebody competes fairly and does a good job and does not push anybody around, then you do not punish him for it. That is a common sense rule.[33]

Thus personifying the corporation and portraying it as a human being punished for good works, Mr. Bartlit invoked the principle of fairness.

"Fairness," however, has more and different dimensions. "Fairness" must take account of the right of the consuming public to be free from the costs of monopoly, as well as the right to just rewards of those who invested their money, time or talents in a firm that "won" monopoly by being better than everyone else.[34] Beyond this narrow inquiry, the appropriate question is not whether the rewards are fair, but whether they are sufficient to provide the incentive to competitors to strive to be excellent. The scales of fairness would seem to tip in favor of protecting the consumer against the costs of persistent monopoly. A law against persistent monopoly gives rewards to the good performer while ultimately restoring to the public the benefits of competition.

A law against persistent monopoly is no more unfair — as Professor Turner pointed out some years ago — than the expiration of a patent after 17 years.[35] The law does not "turn" on the company that wins. Rather, it assumes the company's enjoyment of monopoly profits or a quieter life for substantial time. By the end of that time, market forces or, on their default, the law, should dissipate monopoly; the firm will have had a fair

[33] Testimony before the Commission, Sept. 13, 1978, at 96-97.

[34] Those who make the argument of unfairness generally assume that the firm that has reached monopoly status has done so either by predation or excellence. There are other alternatives. Monopoly may be achieved by luck or market failure. *See* O. WILLIAMSON, MARKETS AND HIERARCHIES (1975). Also, it may be achieved by various mixes of these factors.

[35] Turner, *The Scope of Antitrust and Other Regulatory Policies*, 82 HARV. L. REV. 1207, 1220 (1969) [hereinafter cited as Turner].

reward. Consumer welfare should be respected.

Disincentives

One might worry about possible disincentive effects of the antimonopoly principle. Will the near-monopoly firm pull its punches? Will it limit production and raise price as it nears the monopoly line? To the extent that a law undermines competitiveness or dampens incentives to do a better job, it has undesirable properties that must be weighed.

In considering the deterrent effect of a change in law, the proper concern is the incremental deterrent effect caused by the proposed change. It is therefore important to take account of the fact that a deterrent against activity that increases the market share of a near-monopolist is already built into existing law. Judge Learned Hand's teaching in *Alcoa* gives support to contentions that current law prohibits structural monopoly.[36] Moreover, there are acts, practices, and documents in nearly every monopoly-sized firm's past to which a potential plaintiff can credibly attribute willfulness, and thus make culpability fair grounds for litigation under current standards. The managers of the near-monopoly firm know today that there is a line the passing of which creates concern about litigation, damages and dissolution.

An antimonopoly law does increase the risk that monopoly will be dissipated by legal action if market forces fail to work. It could therefore increase the chances that a firm may so act as to avoid monopoly. But since monopoly, even if achieved, would be dissipated by litigation only if the monopoly is persistent and market forces fail, it is unlikely that a firm would withhold significant benefits to consumers only because of a change in law to make it more inhospitable to monopoly.[37]

Further, the argument that an antimonopoly statute handicaps a near-monopolist and deters competitive conduct by which it might achieve monopoly must be viewed in context. The goal endorsed is the best result for the market in the long run, not the best result for the monopolist. Constraints on a firm that impede achievement of monopoly are not unambiguously bad. Constraints that limit opportunities for near-monopolists may increase opportunities for non-monopolists by assuring them that the

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[36] *See* United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945); note 26 *supra*. *But see* note 15 *supra*.

[37] If monopoly is newly achieved, the successful competitor may be less likely to expect persistence and more likely to be a short-run profit-maximizer. If the monopoly should prove persistent and impervious, it is unlikely that the monopoly firm would at some arbitrary point begin to subdue its own competition to avoid dissipation. Professor Turner observed:

> If apart from cases involving plainly questionable conduct, divesiture policy is limited to substantial degrees of market power that have persisted for a considerable period of time (thus indicating the unlikelihood that anything other than direct action will provide a cure), it seems highly unlikely to me that any business firm would subdue its competitive efforts because of the possibility that it would be so successful for so long that divestiture would be applied.

Turner, *supra* note 35, at 1216.

market is open and holds rewards for their good performance, and may thereby increase and preserve competition in the long run. The possible costs of deterring competitive behavior of a near-monopolist are likely to be far outweighed by the benefits of deterring and eliminating monopoly.

The Costs of Relief

Will the economic costs of relief designed to dissipate monopoly be outweighed by its benefits? There are two possible elements of the cost of relief: long-term loss of efficiency (which would make the law counterproductive) and short-term dislocation costs. Significant dislocation costs would occur only in the case of restructuring. Such dislocation costs are by definition short-term, and should be acceptable if there are likely to be significant long-run benefits of competition.[38] As for long-term prospects, monopoly should not be dissipated except by relief likely to help the market operate more efficiently. The court should be able to devise such relief in virtually all cases of persistent monopoly not involving natural monopoly or a potentially obsoleting product.

Divestiture of separate functional parts of a monopoly firm is a possible remedy. Indeed, it may be the most efficient way to restore effective competition with relative speed. However, loss of significant firm efficiencies, where clearly threatened, would weigh heavily against divestiture. Moreover, if market forces such as those created by new technology are likely to dissipate the monopoly in the near term, divestiture may be an unnecessary intrusion.

The court, at the relief stage, should consider not only divestiture; it should consider various means of introducing dynamic competitive challenges. Especially where the monopoly firm is an outstanding performer and an organic whole, courts should give careful thought to new and innovative methods of introducing competition from outside sources, and to issuing injunctions tending to break down barriers to entry and to effective competition.[39] If an antimonopoly law is so applied, the costs of relief should be insignificant as compared with its benefits.

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[38] As Professor Turner said:

> As for the costs of restructuring, they might well be serious if there were any extensive campaign of atomization. But we are not talking about that. What is at issue is divestiture applied only to firms much larger than is necessary for economies of scale, and applied only if viable successor firms of efficient size can be created. With these limitations, the disruptive effects of divestiture would have short-run consequences only, and in my opinion the disruptive effects are usually exaggerated anyway.

Turner, *supra* note 35, at 1216.

[39] Possible judicial and legislative methods of dissipating monopoly power include: injunction against practices that have a tying or entrenching effect, compulsory licensing of certain critical technology that persistently barricades competition, disclosure regarding such critical technology, government funding of research and development by non-dominant firms, tax benefits that encourage private funding of research and development efforts by non-dominant firms, other government support of new competition against the monopoly firm, and lowered tariffs.

Transcience of Innocent Private Monopoly

Some who urge that predation should be a necessary element of the monopoly case argue that substantial, persistent innocent monopoly virtually never exists, and that therefore we should not bother to change or clarify the law. This argument — which urges that the plaintiff should be required to prove bad conduct because most monopolists are predatory — misses the point. If monopoly is antithetical to a competition system, then proof of persistent monopoly should make the case. To impose on the plaintiff a burden that is irrelevant not only makes a charade of our legal process but creates the very problem that gave birth to the National Commission: the needlessly attenuated case.

Most monopolies not predatorily gained and not supported and reinforced by government license or regulations are probably transient.[40] Nevertheless, a sound law should be in place for private monopolies that persist.[41]

Fear of Abuse of an Anti-Monopoly Law

Some observers fear that a clear antimonopoly law would be the worst of all possible worlds. Critics argue that the government will "poison the well" at trial by introducing evidence of bad conduct (defeating attempts at streamlining); that it will gerrymander markets to make every big firm look like a monopolist; and that it will thus posture itself for a massive break-up of big business.

This author does not share the permise that government antitrust enforcers are singleminded bureaucrats bent on trust-busting regardless of the public interest. There is truth to the statement that an antimonopoly law would not make all conduct evidence irrelevant. Nevertheless, there is little merit to the argument that attempts to streamline will be defeated in significant ways, or the argument that the government will gain and use power to gerrymander markets.[42]

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[40] Government protection of patent monopolies, which serves the important goal of inducing invention, is one way in which government intervention might facilitate or reinforce monopoly power. The alleged monopoly firms that do exist in markets that are not natural monopoly markets tend to be patent-intensive. Defendants IBM, Xerox and Eastman Kodak fall within this category.

[41] At the turn of the century, Judge (later Chief Justice) Taft remarked that the public is entitled to the benefits of competition even in the short run. United States v. Addyston Pipe & Steel Co., 85 F. 271, 284 (6th Cir. 1898), *modified and aff'd,* 175 U.S. 211 (1899). Rejecting the argument that "outside competition would soon cure [the] abuses [of monopoly]," he said:

> [This answer] would validate the most complete local monopoly of the present day. It may be. . .that local monopolies cannot endure long, because their very existence tempts outside capital into competition; but the public policy embodied in the common law requires the discouragement of monopolies, however temporary their existence may be. The public interest may suffer severely, while new competition is slowly developing.

Id.

[42] The court, not the government, determines relevant market. Therefore one should not

Rather, a change in law focusing monopoly litigation on monopoly status and its imperviousness to erosion by market forces should rationalize the trial of a monopoly case. The first question will be, as it should be, whether the defendant has monopoly power. Monopoly power presumes a well-defined market within which the defendant can raise price without a significant shift to substitutes. Of course the plaintiff, as always, will have the burden to prove such a well-defined market. By dealing directly with monopoly power, sound market definition will be encouraged and should result. Procrustean beds tailored to fit the defendant should not be tolerated. A proper respect for market power is critical.

Under a stronger antimonopoly law, some but much less conduct evidence would remain relevant. Evidence of recent conduct would be relevant to demonstrate existence of monopoly power, for the effective use of such power can prove its existence. Where conduct directly evidences existing power, it should be admitted. However, tailoring conduct evidence to proof of market power, and eliminating incentives to prove a monopoly firm "good" or "bad" in itself, should streamline both the discovery process and the trial and should sharpen the analytical framework for proof of the case.

Theory, practice, judicial administration, and above all a commitment to free and dynamic competition and consumer welfare, support the conclusion that substantial, persistent monopoly power should be dissipated by means designed to restore the efficient functioning of the market.

II. Attempts to Monopolize

The President specifically asked the National Commission to reevaluate the attempt-to-monopolize prohibition of section 2 of the Sherman Act. The Executive Order directed the Commission to make recommendations for "simplification of the standards required to establish attempted monopolization in suits brought by the United States under Section 2 of the Sherman Act."[43] The Commission's attention turned to two different and quite significant problems relating to the attempt prohibition. First, section 2 is the only provision of the Sherman Act dealing with single-firm acts.[44] Given strict constructionist interpretations of the attempt prohibition, there is an enormous gap in the Sherman Act that seems to leave unrestrained substantial anticompetitive single-firm acts that threaten a harmful result short of monopoly.[45] As a result, government challenges to

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worry unduly about attempts of litigators on either side to convince the judge to gerrymander the market.

[43] Commission Report, *supra* note 1, at 320, 897 Antitrust & Trade Reg. Rep. (BNA) (Special Supp.) at 92.

[44] The Federal Trade Commission has broader power than the Department of Justice to deal with anticompetitive single-firm acts. It enforces the Federal Trade Commission Act. Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45 (1976), prohibits unfair acts or practices.

[45] *See, e.g.*, Pennwalt Corp. v. Zenith Lab. Inc., [1979-2] Trade Cas. (CCH) ¶ 62,749 (E.D. Mich. 1979). *See also* Commission Report, *supra* note 1, at 144-49, 897 Antitrust &

unambiguously predatory unilateral conduct have proved unsuccessful.[46] Second, a second gap has been developing in the law governing single-firm conduct likely to produce or aggravate existing monopoly; namely, there is movement toward immunizing all pricing strategies, even those having both the purpose and effect of lessening competition, if the firm's prices do not fall below its short-run marginal or average variable costs.[47] If the attempt provision is construed so narrowly, most anticompetitive single-firm acts would enjoy Sherman Act immunity; a result clearly at odds with a pro-competition policy. Dealing with both problems, the Commission[48] proposed an amendment to the attempt provision of section 2.[49] This proposed amendment takes the form of two provisos, which are explained below.

The first proviso reaches acts that significantly threaten competition. In most jurisdictions, the attempt offense requires proof of two elements: a specific intent to monopolize a relevant market, and a dangerous probability of achieving monopoly.[50] The Commission's proposed two-part amendment deals only with the "dangerous probability of monopoly" element of the attempt offense. It does not suggest changing the traditional "intent" requirement, and thus would not interfere with the well-intentioned autonomy of firms.[51]

TRADE REG. REP. (BNA) (Special Supp.) at 41-44.

[46] United States v. Empire Gas Corp., 537 F.2d 296 (8th Cir. 1976), *cert. denied,* 429 U.S. 1122 (1977).

[47] *See* note 60-61 *infra.*

[48] Concerns or dissenting views were separately stated by Commissioners Hatch, Izard, Javits and McClory. Commissioners Kennedy and Morgan concurred in general concerns expressed by Commissioner Hatch, and Commissioner Wiggins expressed general agreement with Commissioner Javits. *See* COMMISSION REPORT, *supra* note 1, at 331-414, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 95-117.

[49] The amendment proposed would supplement existing § 2, adding to its language:

> Provided that, in determining whether a person has attempted to monopolize a part of a trade or commerce, (1) a dangerous risk of monopoly shall be held to exist upon a showing that the conduct alleged to constitute the attempt significantly threatens competition in any relevant market, as determined after an evaluation of the defendant's intent, the defendant's present or probable market power, and the anticompetitive potential of the conduct undertaken; and (2) the fact that a defendant's prices were not below either aveage variable cost or marginal cost shall not be controlling, but may properly be considered, in assessing the defendant's intent and the conduct at issue..

COMMISSION REPORT, *supra* note 1, at 145-49, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 50 (italics eliminated).

[50] *See* COMMISSION REPORT, *supra* note 1, at 145-49, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 42-44; Swift & Co. v. United States, 196 U.S. 375, 396 (1905). *But see* Lessig V. Tidewater Oil Co., 327 F.2d 459, 474 (9th Cir.), *cert. denied,* 377 U.S. 993 (1964) (minority rule; relevant market is not in issue and plaintiff need not establish probability of actual monopolization).

[51] Accordingly, the Commission's recommendation does not reach the single-firm acts of a non-monopolist undertaken to realize efficiencies, even if the act happens to exclude competitors and rigidify concentration.

A strong case can be made that proof of intent to harm competition should not be a necessary element of the case where the challenged conduct itself has a distinctly anticom-

Under the Commission's proposed proviso (1), willfully anticompetitive single-firm acts would be illegal if they "significantly threaten competition," whether or not they threaten monopoly as such.[52] Defendant's market power, defendant's intent, and the anticompetitive potential of defendant's conduct all would be factors consulted in predicting the probable impact of the conduct on competition.[53] The more egregious and unambiguously anticompetitive the conduct, the more probable the violation. Likewise, the greater the market power of the defendant, the more likely the violation.[54] Bad intent itself would not constitute a violation nor would it convert competitive conduct into a violation. However, evidence of defendant's intent tending to prove its strategy to eliminate or chill competition, combined with evidence of defendant's power to do so, would be evidence of probable adverse impact on competition.[55]

Application of this proposed rule of reason may be illustrated by the following example. IBM is one of a handful of manufacturers of general-purpose computers. Several firms, including IBM and Telex, compete in the related area of peripheral attachments to the IBM main frame computer. If, each time Telex makes a better quality peripheral, IBM should put the components of its peripheral attachments inside the main frame and remove or change the peripheral connection; if it should do so to stamp out Telex's competition and for no technological gain; and if this strategy chills entry and stifles competition in price or quality, IBM would offend the revised section 2. The offense would be complete whether or not IBM-compatible peripherals is a separate market. It would not be negated by proof that all peripherals comprise the relevant market and that IBM could not achieve monopoly in this broader market.[56] The

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petitive effect.

[52] *Compare* note 49 *supra with* Handler, Blake, Pitofsky & Goldschmid, *Note on Predatory Pricing and Attempt to Monopolize*, in TRADE REGULATION: CASES AND MATERIALS 181-87 (3d ed. Supp. 1979).

[53] *See* note 49 *supra*. The defendant's market power, intent, and the anticompetitive potential of its conduct have traditionally been factors used in measuring the reasonableness of trade restraints. *See, e.g.*, Board of Trade v. United States, 246 U.S. 231, 238 (1918); United States v. Terminal R.R. Ass'n, 224 U.S. 383, 395 (1912). *See also* National Soc. of Prof. Eng. v. United States, 435 U.S. 679 (1978).

[54] COMMISSION REPORT, *supra* note 1, at 148-49, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 43.

[55] Since threat to competition is the heart of the violation under the Commission's proposal, a violation would never be predicated solely upon evil intent. An evil intent without power to hurt competition would be no more of a violation after adoption of such an amendment than before.

A claim of harm to competition by a well-intentioned non-monopolist that, for example, charges long-term low prices because the firm is efficient, would not be an offense even if the low prices threaten the existence of inefficient competitors, because: (1) the specific intent element would be absent; and (2) long-term competitively low pricing is not an anticompetitive act, it is conduct the competition system encourages.

[56] Compare the facts in Telex Corp. v. IBM Corp., 367 F. Supp. 258 (D. Okla. 1973), *rev'd in part, aff'd in part,* and *rem'd in part,* 510 F.2d 894 (10th Cir.), *cert. dismissed,* 423 U.S. 802 (1975).

law would deal directly with a serious harm to competition, even though short of threatened monopoly. As a by-product, the trial would not bog down with a parade of witnesses and data tending to prove or disprove that the market is IBM-compatible peripherals.

The recommended change to achieve this result would replace the requirement of dangerous probability of monopoly with the lesser requirement that defendant's conduct "significantly threatens competition in any relevant market."[57] Thus, the main effect of the Commission's proviso (1) is to catch willful anticompetitive single-firm acts that significantly threaten competition even though they fall short of the brink of monopoly. The effect of the proviso is thus to close a loophole in the Sherman Act.[58]

The second proviso addresses anticompetitive pricing strategy.[59] Questions surrounding anticompetitive pricing strategy, which resulted in the Commission's second proviso, stand on a different footing. A new, bright-line rule on pricing behavior, proposed in a 1975 article by Professors Areeda and Turner,[60] now enjoys currency with many courts.[61] Under this

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[57] *See* note 49 *supra*.

[58] It is not clear that the gap in the Sherman Act was ever intended. In the Fifty-First Congress the congressmen used the word "monopoly" in such context as to suggest that it included "oligopoly" and "market power." *See, e.g.*, 21 CONG. REC. 2457 (1890) (remarks of Sen. Sherman); 21 CONG. REC. 2726 (1890) (remarks of Sen. Edmunds). The word "monopoly" became refined in its use over the years. As commonly used today, it refers to a single firm with monopoly power. Accordingly, firms with market power but not monopoly power may singly, or interdependently, engage in a broad range of acts that harm competition, and they are able to do so with impunity. *Cf.*, White Bag Co. v. International Paper Co., 579 F.2d 1384 (4th Cir. 1974) (dual distributors with less than near monopoly position can create price and product squeezes on competitors without violation of the Sherman Act). Attempting to close this loophole in the 1960's, the Supreme Court reached out to find "contracts" not central to restraints of trade simply for a jurisdictional base from which to condemn anticompetitive acts that were essentially unilateral. *See, e.g.*, Albrecht v. Herald Co., 390 U.S. 145, 149 (1968); Simpson v. Union Oil Co., 377 U.S. 13, 18 (1964). The Supreme Court is not likely to take such liberties today.

[59] The Commission's recommendation on pricing was made in the context of attempts to monopolize. The recommendation is, in theory, equally applicable to pricing strategies that may offend the monopolization prohibition.

[60] Areeda & Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975) [hereinafter cited as *Predatory Pricing*].

[61] After the Areeda and Turner article appeared in 1975, many courts began to immunize all pricing strategies as long as the actor's prices did not fall below its short-run marginal or average variable costs. *See, e.g.*, California Comp. Prod. Inc. v. IBM Corp., [1979-1] TRADE CAS. (CCH) ¶ 62,713 (9th Cir. 1979); Pacific Eng'r & Prod. Co. v. Kerr-McGee Corp., 551 F.2d 790, 799 (10th Cir.), *cert. denied*, 434 U.S. 879 (1977); Janich Bros., Inc. v. American Dist. Co., 570 F.2d 848, 857-58 (9th Cir. 1977), *cert. denied*, 439 U.S. 829 (1978); Hanson v. Shell Oil Co., 541 F.2d 1352, 1358-59 (9th Cir. 1976), *cert. denied*, 429 U.S. 1074 (1977); International Air. Indus. Inc. v. American Exel. Co., 517, F.2d 714, 724 (5th Cir. 1975), *cert. denied*, 424 U.S. 943 (1976); William Inglis & Sons Baking Co. v. ITT Continental Baking, 461 F. Supp. 410, 418-19 (N.D. Cal. 1978); Murphy Tugboat Co. v. Crowley, 454 F. Supp. 847, 853-55 (N.D. Cal. 1978); Weber v. Wynne, 431 F. Supp. 1048, 1058-60 (D.N.J. 1977). Where barriers to entry were high, however, plaintiffs were sometimes given the chance to prevail if they proved that the defendant's prices were below its short-run profit-maximizing

rule, pricing which does not fall below short-run marginal or average variable cost[62] is likely to be held legal *per se* — i.e., totally beyond the reach of the antitrust laws — even if used as part of a strategy to chill or destroy competition.[63]

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price and the barriers were so high as to prevent other entry before the defendant could reap the benefits of its market position. *See, e.g.*, ILC Peripherals Leasing Corp. v. IBM Corp., 458 F. Supp. 423, 431-33 (N.D. Cal. 1978).

Scholars have been less enthusiastic than the courts about the Areeda-Turner rule. They have noted that the Areeda-Turner rule ignores strategic and long-run effects of dominant-firm low pricing. *See generally* Williamson, *Predatory Pricing: A Strategic and Welfare Analysis*, 87 YALE L.J. 284 (1977); Williamson, *Williamson on Predatory Pricing II*, 88 YALE L.J. 1183 (1979) [hereinafter cited as *Predatory Pricing II*]; Scherer, *Predatory Pricing and the Sherman Act: A Comment*, 89 HARV. L. REV. 869 (1976); Baumol, *Quasi-Permanence of Price Reductions: A Policy for Prevention of Predatory Pricing*, 89 YALE L.J. 1 (1979); Ordover and Willig, The Economic Definition of Predation (unpublished manuscript 1980).

Scholars responding to Areeda and Turner have embraced analyses more attuned to the dynamics of competition, to the strategies of the incumbent firms, and to the long-run health of the competition process. For example, Williamson's approach is explicitly flexible enough to condemn disciplinary pricing strategies. As Williamson observes: "Successful signaling of a probably punitive response can permit a dominant firm to enjoy greater profits (or an easier life) by reducing the likelihood that its markets will be subject to encroachment." *Predatory Pricing II, supra*, at 1185.

In spite of the avalanching criticisms, and possibly because of apparent but illusory simplicity, the courts have preferred Areeda and Turner. *But see* O. Hommel Co. v. Ferro Corp., [1979-1] TRADE CAS. (CCH) ¶ 62,720, at 78,040 (W.D. Pa. 1979) (predatory pricing may be established by evidence of sales below total cost); Transamerica Comp. Co. v. IBM Corp., [1979-2] TRADE CAS. (CCH) ¶ 62,989, at 79,641 (N.D. Cal. 1979) (pricing below average total cost is a suspicious circumstance and is illegal if unreasonable). According to Judge Schnacke in *Transamerica*, a relevant inquiry is whether the monopolist is "cutting losses or cutting throats." *Id.*

[62] Marginal cost is the addition to total cost resulting from production of an additional unit of output. Variable costs are costs that vary with changes in output. Average variable costs are the average variable costs per unit of output. Variable costs plus fixed costs equal total cost. *See Predatory Pricing, supra* note 60, at 700-01. Areeda and Turner conclude that marginal cost is the appropriate measure for determining the line between acceptable and predatory behavior. However, since marginal cost is often difficult to ascertain and average variable cost is more readily ascertainable, Areeda and Turner would use average variable cost as an indicator of marginal cost. *Id.* at 716.

Marginal cost and variable costs by definition do not take into account any fixed costs. Therefore, a price at marginal or average variable cost may be very low indeed, and may be well below a level that, if persistently charged, would allow a firm to survive. *Id.* at 709. *See* B. Bock, Innovation and the Economy as an Organized Structure 4 (Feb 13, 1980) (revised paper for N.Y.S. Bar Antitrust Section Program)[hereinafter cited as Bock].

[63] *Predatory Pricing, supra* note 60, at 733.

The Areeda-Turner rule came as something of a shock to the antitrust nervous system. Antitrust had through the years been perceived and applied as an open, pluralistic, multivalued system that protected competition in markets, eased entry into markets, tended to lessen extreme disparities in bargaining power, and tended to encourage independence of traders. Sullivan, *Antitrust, Microeconomics and Politics: Reflections on Some Recent Relationships*, 68 CAL. L. REV. 1, 4 (1980). Courts, including the Supreme Court, sometimes utilized economics. "But it [the Supreme Court] used economics to determine whether competition, as the Court conceived it, continued to thrive, not as a source for determining what competition means." *Id.*

In the 1970's a shift occurred. Courts began to define competition in terms of efficiency.

As one trial court observed, the Areeda-Turner rule protects monopolies. A conclusive presumption of legality for pricing above marginal cost "would truly be a 'defendant's paradise.' "[64]

Concerned with the narrowness of the Areeda-Turner rule and its tendency to protect market power, the National Commission made a modest recommendation: "(2) the fact that a defendant's prices were not below either average variable cost or marginal cost shall not be controlling, but may properly be considered, in assessing the defendant's intent and the conduct at issue."[65] Under the Commission's proviso (2), taken together with proviso (1), pricing strategies would be judged by their probable effect on competition in the marketplace, not rigidly by the relationship of defendant's price to its marginal cost.

Background and Critique of the Areeda-Turner Rule

Prior to the seminal Areeda-Turner article, the law on predatory pricing focused principally on the intent of the alleged predator and the effect on the victim. Pricing that was intended to hurt a rival and that did so was for that reason likely to be held illegal.[66] A problem emerged. Courts were protecting competitors, not necessarily competition. These courts may have protected inefficient competitors. Consumer interests may have been threatened by depriving the public of the benefits of low prices.

Professors Areeda and Turner both took the lead in identifying the problem. They pointed out that intent to take from a rival all the business one can get is entirely consistent with desirable procompetitive behavior. Intent to beat a rival by better performance is of no negative antitrust significance.[67] Reacting to the state of the law, Professors Areeda and Turner set about to create an environment conducive to rigorous price competition. They may, however, have overreacted. The Areeda-Turner rule swings the pendulum from the protection of inefficient competitors to

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Areeda and Turner provided an economic rule of apparent simplicity, objectivity and precision, and the rule was at once embraced by the courts. *See* note 61 *supra*.

[64] Transamerica Comp. Co. v. IBM Corp., [1979-2] TRADE CAS. (CCH) ¶ 62,989 at 79,640 (N.D. Cal. 1979) (quoting *Predatory Pricing II*, *supra* note 47, at 305). *Contra*, Areeda & Turner, *Predatory Pricing: A Rejoinder*, 88 YALE L.J. 1641 (1979).

[65] COMMISSION REPORT, *supra* note 1, at 166, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 50. *See* Handler, Blake, Pitofsky & Goldschmid, *Note on Enforcement of Section 2 Since* Grinnell, in TRADE REGULATION: CASES AND MATERIALS (3d ed. Supp.), 24-31 (1979).

[66] Most of the predatory pricing cases arose under the Robinson-Patman Act, 15 U.S.C. § 13 (1976). *See, e.g.*, Utah Pie Co. v. Continental Baking Co., 386 U.S. 685, 702-03 (1967); Moore v. Mead's Fine Bread Co., 348 U.S. 115, 118 (1954). In Sherman Act cases, predatory pricing when it was found to exist, was ordinarily one piece of a complex mosaic of anticompetitive acts. *See, e.g.*, Standard Oil Co. v. United States, 221 U.S. 1, 43 (1911); United States v. American Tob. Co., 221 U.S. 106, 181-83 (1911).

[67] Turner, *The Scope of Attempt to Monopolize*, 30 ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK RECORD 487 (1975); *Predatory Pricing*, *supra* note 60, at 704. *See* Borden, Inc., [1976-79 Transfer Binder] TRADE REG. REP. (CCH) ¶ 21,490 at 21,517-19 (FTC 1978) (Commissioner Pitofsky concurring).

the protection of monopoly power.

The Areeda-Turner rule reveals the following premises. Economics alone is the appropriate guide to antitrust policy, which should seek to maximize efficeincy.[68] Static microeconomics provides the tools to measure efficiency. Only the most efficient firms should enter and remain in markets. Firms less efficient than their competitors should not survive; society is better off if their owners invest their resources elsewhere.[69]

Reflecting these values, the Areeda-Turner rule has the ostensible merit of simplicity[70] and the merit of hospitality to price competition in the short run. However, it has the following limitations. It ignores long-run welfare. Focusing narrowly on the relationship between a firm's prices and its costs, and only in the short run, it ignores strategic pricing behavior and strategic behavior of which pricing is only a part.[71] As a result, it condones conduct designed to have and having the effect of crippling effective competitors, raising barriers to entry and deterring aggressive competition, and it thereby tends to preserve and enhance the long-run dominance of the short-run price-cutter.

Approach of the Commission

A major contribution of the Commission is to highlight the limitations of the Areeda-Turner rule and to reject the rulemaking approach Areeda and Turner initiated. The National Commission does not embrace rigid rules governing price behavior. It offers a framework rather than rules. The framework allows for an open analysis in the tradition of antitrust.

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[68] *See* 3 AREEDA & TURNER, *supra* note 26, at 289-390.

[69] *Id.* at ¶ 715a at 165. *See* Transamerica Comp. Co. v. IBM Corp., [1979-2] TRADE CAS. (CCH) ¶ 62,989 at 79,639 n.68 (N.D. Cal. 1979).

[70] *See* Bock, *supra* note 62, at 6. "The essence of competition, whether in a stable or a more dynamic market, does not lie in the relation between cost and price, since what cost means depends on the observer's method of viewing different and varying costs in different time frames." *Id.*

[71] As the Supreme Court has historically recognized, pricing behavior can be used as a tool for the destruction of competition. In Schine Chain Theatres, Inc. v. United States, 334 U.S. 110 (1948), the Supreme Court said "[Price-cutting] may be the instrument of monopoly power to eliminate competitors or to bring them to their knees." *Id.* at 120. Many cases evidence pricing strategies that thus debilitate competition. For example, in FTC v. Cement Institute, 333 U.S. 683 (1948), several cement firms collectively used disciplinary pricing to cause rivalrous firms to abandon their competitive pricing and succumb to the artificial basing point system.

In more recent cases, defendants have prevailed despite disciplinary pricing strategies. In United States v. Empire Gas Corp., 537 F.2d 296 (8th Cir. 1976), *cert. denied*, 429 U.S. 1122 (1977), Empire pressured its competitors to raise their prices and to avoid soliciting its customers. When aggressive competitors defied Empire's will, Empire used selectively low, disciplinary pricing to bring them in line. In Telex v. IBM, 367 F. Supp. 258 (N.D. Okla. 1973), Telex was aggressively competing in peripheral attachments and making products superior to IBM's. IBM procured Telex's cost data and selectively cut its prices below Telex's costs. Had it done so temporarily and with the purpose and effect of warning Telex not to risk investment in the next generation of peripherals, it would have been using its pricing strategy to dampen aggressive competition in the market.

The Commission values both long-term low prices and real opportunity for entry and survival of firms that can perform at levels satisfactory to consumers. Properly applied, the Commission's principle would protect neither dominance (as does the Areeda-Turner rule) nor inefficiency (as did older case law). Instead, it would promote the long-run health, openness and dynamism of the competition process itself.

The Commission gives these examples illustrating application of its recommendation:

> [W]here a firm with a dominant market position undertakes a pattern of pricing behavior directed at excluding new entrants from a market in circumstances in which the firm could expect such efforts to be successful, liability may be found even if the prices charged were above marginal cost. Such pricing behavior directed at existing competitors by a dominant firm in a market with high entry barriers, for example, should be reachable under Section 2. Similarly, when a firm undertakes a pattern of pricing behavior intended to "police" competitors by discouraging price-cutting, liability may be found in spite of prices above marginal cost.[72]

Below average-cost pricing would be presumptively reasonable if necessary to liquidate excess, perishable, or obsolete merchandise; or if the price cut is necessary to minimize losses in a shrinking market; or if the industry is suffering from chronic excess of capacity.[73] On the other hand, if in a high-barrier market a monopoly firm with substantial brand loyalty eliminates its premium to drive out an efficient, aggressive challenger, the pricing strategy should be presumptively illegal.[74]

Examples, like the facts of particular cases, can serve only as a guide. Facts are infinitely variable. Rules cannot accomodate the dynamics of competition. The important steps are to formulate goals and to construct a framework for analysis based on those goals. The Commission took both steps.[75]

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[72] COMMISSION REPORT, *supra* note 1, at 150, 897 ANTITRUST & TRADE REG. REP. (BNA) (Special Supp.) at 44.

[73] *See* Transamerica Comp. Co. v. IBM Corp., [1979-2] TRADE CAS. (CCH) ¶ 62,989, at 79,641 (N.D. Cal. 1979) (citing scholarly works of Oliver Williamson and Richard Posner, and citing Pacific Eng'r & Prod. Co. v. Kerr-McGee Corp., 551 F.2d 790 (10th Cir.), *cert. denied*, 434 U.S. 879 (1977)).

[74] *See* Borden, Inc., [1976-79 Transfer Binder] TRADE REG. REP. (CCH) ¶ 21,490 (FTC 1978) *and* the concurring opinion of Commissioner Pitofsky. Commissioner Pitofsky asks whether pricing behavior is "unreasonably exclusionary" in light of the respondent's monopoly position. *Id.* at 21,522-24.

Even a monopoly firm should have the freedom of competitive response. The determination of what constitutes a reasonable competitive response is a question of fact. *See id.* The question of fact should be resolved in light of the twin values of long-run low prices, and of entry and survival of effective competitors, which in turn enhances the liklihood of long-run low prices.

[75] The case can be made for a simpler formulation than that offered by the Commission. For example, Congress could add to § 2 of the Sherman Act a formulation already incorpo-

Pricing and Efficiency

It may be argued that the Commission's approach is conducive to allocative inefficiency. For example, if it costs Telex one hundred dollars more per unit than it costs IBM to produce the same quality peripheral attachment and Telex diverts sales from IBM, society "wastes" the extra one hundred dollars' worth of resources used to make each Telex-produced peripheral diverted from IBM.

This is a narrow and incomplete view of efficiency. The possible "waste" reflected by the extra resource costs of the diverted sales is likely to be small when compared with the costs of an environment that deters potentially efficient firms from entry and that deters entrants from making the investments necessary for efficient performance.[76] If antitrust principles would encourage entry and survival of Telex and other competitors, the competitive pressures from rivals may cause IBM to reduce a monopoly-level price on a long-run basis. In addition, the pressures of increased competition may cause firms with market power to be generally more responsive to consumer demand. Moreover, if Telex and other challengers no longer face prohibitive risks, they may make the investments necessary to reach the low cost-levels of IBM, thereby tending to produce additional efficiency gains. On the other hand, if IBM is permitted by law to pose a constant threat to the survival of Telex (and others), and if it can with impunity shoot Telex down following any significant competitive advance by Telex, then IBM is likely either to eliminate Telex, along with its procompetitive moderating pressure, or to deter Telex from making the investment necessary to equal or outperform IBM, and to deter the entry of other firms that would face similar prospects.

By supporting an environment hospitable to new competition in monopoly and near-monopoly markets, the Commission supports both dynamic competition and long-run efficiency.

Conclusion

In theory, the federal antitrust laws are pro-competition and antimonopoly. In practice, they are being narrowly applied in ways that pro-

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rated into law abroad: "No person shall abuse a dominant position." *See* Treaty of Rome (1957), Article 86 (European Economic Community); Act Against Restraint of Competition § 22 (1957, as amended 1965, 1973) (West Germany). *See* Markert, *Developments in International Antitrust Law*, 43 FORDHAM L. REV. 697, 711 (1975) (discussion of West German antitrust policies).

Alternatively, an addendum to § 2 of the Sherman Act could read: "No person shall abuse market power."

[76] If, given an environment that encourages appropriate levels of investment, an infant entrant is likely to become as cost efficient as a monopoly-sized incumbent, the efficiency benefits of encouraging entry and survival are clear. Even if there is likely to be some permanent cost disparity between the entrant and the incumbent, society will gain economically by survival of the entrant as long as the benefits of its moderating effect are greater than the costs of the additional resources used to make products that divert sales from the incumbent.

tect monopolies and harm competition. The balance should be tilted towards a more competitive economy. The National Commission lends its voice to this effort.