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Peter C. Carstensen

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ANNUAL SURVEY OF ANTITRUST DEVELOPMENTS: 1976-1977

PETER C. CARSTENSEN*

I. Introduction: The Words and The Music

In speaking of the Supreme Court's decisions on securities law, Professor Ratner has cautioned that one should pay attention to the "music" as well as the words of the decisions.[1] Unless one has a sense of the "music" the Court is playing, one can easily misinterpret the words in the opinions.[2] This task is no less important in antitrust matters.

In both securities law and antitrust law the task of understanding is made harder because the Court is in transition to new concerns and attitudes. How far and in which directions will the new majority proceed? This is the harder to predict because its concerns are not consistent. On one hand, the Court is promoting a more rigorous adherence to the competitive ideal than it has in the past when looking at state economic regulation from a first amendment perspective,[3] but on another hand, it is cutting back on the substantive requirements of the antitrust laws in ways which suggest less faith on the part of the majority in competition as a socially useful goal than has been the case in the past.[4] In addition, even when assuming a

* Assistant Professor, University of Wisconsin Law School. LLB, MA (Economics) Yale University. In this age of consumer warnings, it is probably incumbent to disclose that the author has already published his views with respect to the merits of several of the cases discussed herein and that he regards himself as an antitrust "hawk."

[1] Professor Ratner used this description in the course of a discussion of Supreme Court securities law opinions at the ALI-ABA, Securities Law Training Seminar, June 27, 1977, Madison, Wisconsin. A similar view is presented in Lowenfels, *Recent Supreme Court Decisions Under The Federal Securities Laws: The Pendulum Swings*, 65 GEO. L. J. 891 (1977).

[2] *E.g.*, the Court in Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976), only held that scienter is required—something which is not very hard to plead—but refused to let the plaintiff try its case under the new theory. Clearly the music was about cutting down on suits, and the words had to be understood in that vein. *See* Bucklo, *The Supreme Court Attempts To Define Scienter Under Rule 10b-5; Ernst & Ernst v. Hochfelder*, 29 STAN. L. REV. 213 (1977).

[3] *See, e.g.*, Bates v. State Bar of Arizona, 97 S. Ct. 2691 (1977) and Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, 425 U.S. 748 (1976). *See* text accompanying notes 280 - 296 *infra*.

[4] *E.g.*, Continental T.V., Inc. v. GTE Sylvania, Inc., 97 S. Ct. 2549 (1977). *See* text accompanying notes 15 - 188 *infra*.

violation, the Court has been reluctant to allow victims of that violation to sue[5] and has begun to narrow the kinds of losses for which a victim allowed to sue may recover.[6]

These antitrust decisions are also part of a larger pattern of decisions involving business and commercial issues in the federal courts. These decisions tend to follow two patterns. The first is to define in very limited ways both the substantive and liability aspects of federal causes of action.[7] The second is consciously to redirect much of this litigaton into the state courts by refusing to find that a federal cause of action exists.[8] The first of these themes has a pro business aura,[9] but the second does not necessarily. The two themes are, of course, consistent with a goal of reducing the workload of the federal judiciary regardless of the consequence for the parties seeking judicial aid. But the Court's willingness to evaluate state regulation under the first amendment[10] and antitrust rules[11] opens a vast range of litigable issues, introducing much more federal judicial review of state action and denying businesses the protection of anticompetitive state regulation.

If the themes are in evidence but their harmony in doubt, the words pose all too well the traditional problems of deciphering what the Court means. Whatever direction it goes, the Court seems largely unable or unwilling to decide antitrust or other business matters on principles that can be grasped and used productively as tools of analysis and decision. The new majority, as result oriented as the Warren Court was charged with being, seems to decide cases in terms of desired results without identifying, explicating or evaluating underlying principles and without apparent reference to the implications of the decision taken.

This past term, the Court decided seven antitrust cases. Two dealt with matters of substance; another two dealt in different ways with the relationship between antitrust law and state legal systems, judicial and regulatory; a third pair dealt with the special problems of private damage actions. The seventh case, not treated in this discussion, fundamentally concerned a general criminal law issue although it also suggests the problems of achieving effective relief in antitrust cases.[12]

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[5] Illinois Brick Co. v. Illinois, 431 U.S. 720 (1977). *See* text accompanying notes 307 - 375 *infra.*

[6] Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc. 429 U.S. 477. *See* text accompanying notes 375 - 402 *infra.*

[7] *E.g.*, Piper v. Chris Craft Industries, Inc., 430 U.S. 1 (1977); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976).

[8] *E.g.*, Santa Fe Industries, Inc. v. Green, 430 U.S. 432 (1977); Cort v. Ash, 422 U.S. 66 (1975); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975).

[9] *See* Tushnet, " . . . *And Only Wealth Will Buy You Justice"—Some Notes On The Supreme Court 1972 Term,* 1974 WIS. L. REV. 176.

[10] *See* cases cited at note 3 *supra.*

[11] *E.g.*, Cantor v. Detroit Edison Co., 428 U.S. 579 (1976); Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975).

[12] United States v. Martin Linen Supply Co., 430 U.S. 564 (1977). The only issue in this, the only government antitrust case taken up by the Court this past term, was whether or not entry of a judgment of not guilty after a hung jury in a criminal contempt case was an

II. Substantive Antitrust Law: Standards for Judging Restrictive Conduct

The two substantive cases which the Court decided both involved problems of restrictive conduct and both presented the question of what standards should be used to judge cases in which a contract in restraint of trade is conceded. In United States Steel Corp. v. Fortner Enterprises, Inc.[13] the Court adhered to a traditional analysis of tying and exonerated the defendant while leaving the stated legal standard much as it was. But in Continental T.V., Inc. v. GTE Sylvania, Inc.,[14] the Court refused to interpret or distinguish the existing standard and instead replaced it with an unformulated "rule of reason" whose specifics and operation are entirely unstated. Moreover, although both cases involved the problems of the use and abuse of market power, the Court's opinion in *Fortner* demonstrates an awareness of these issues, but in *Sylvania* its opinion ignored those problems although they were clearly present.

A. *Restraints on the Conduct of Resellers:* Continental T.V., Inc. v. GTE Sylvania, Inc.

1. *Business Analysis of Resale Restraints*

Restraints ought to be analyzed functionally.[15] To do so, we need to have functionally relevant categories, and we need to know both the market conditions required for the restraint to have its desired effect and why that effect is desired and useful to the parties.

a. *Definition*

While all so-called vertical restraints arise in association with some other business dealings between the parties thereto, one differentiation among them is to compare the level of production or distribution to which the restraints specifically relate to the level of production or distribution at which the parties have their other dealings. Restraints which control how one or both parties deal with third parties, customers or suppliers, not on the same level as the parties' business dealing, are "external" to that dealing. Producer control over dealer resale practices, as in Sylvania's

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appealable order in light of the double jeopardy bar. The Court held that such a judgement was not appealable. While this may be good criminal law, it does make effective enforcement of antitrust decrees more difficult.

[13] 429 U.S. 610 (1977).

[14] 97 S. Ct. 2549 (1977).

[15] To treat restraints in a non-functional way, labeling them according to some characteristic, e.g., vertical or horizontal, price or non-price, leads to the obvious problem that restraints having dissimilar functions are labeled and treated legally as if they were the same, and, equally bad, similar restraints serving the same function are labeled and treated differently, reducing the impact of the law on restraints to a sterile formalism. *Cf.* C. KAYSEN & D. TURNER, ANTITRUST POLICY (1959); Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division,* 74 YALE L. J. 781 (1965) [hereinafter cited as Bork I].

restraints on dealer resale locations,[16] typify such external restraints. Conversely, restraints which specifically define the business relationship between the parties are "internal" to that dealing although they will nevertheless restrain the freedom of one or both parties in dealing with others in transactions similar to the parties' dealings. Tying as in *Fortner* typifies such an internal restraint. It is functionally relevant to define these categories because the character of a restraint, internal or external, implies quite different necessary relationships to market power.

b. *Necessary Market Condition for External Restraints*

Because an external restraint limits the freedom of action of a party in its dealings with third parties, it can be useful only if such control has some economic significance. The market condition under which such control can be significant occurs when the producer and/or distributor has or expects to obtain in consequence of the restraint some market power over the product.[17] External restraints, unlike internal ones,[18] will make no sense to either party in the absence of this condition because the competition of completely substitutable products and distributors (i.e., the absence of market power) will make the restraint of resale entirely valueless to either party.[19]

The quantum of market power needed to achieve and make useful an external restraint is not necessarily very great. A trademarked product which is physically identical to other similar products serving the same function may, by virtue of its trademark, have sufficient differentiation to possess power to make resale control possible. Likewise, a product only slightly different in design or quality from others functionally similar may also possess the necessary quantum of power.[20] Market power can also arise

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[16] The restraints also had a necessary but subordinate internal dimension which specified that the producer would restrict its sales to the chosen distributors. The distributors were under no similar restraint and so remainded free to stock and sell any substitute product at any location. Because the only internal dimension to these restraints is incidental to its external goals, it is proper to characterize it as an external restraint.

[17] This point is made by commentators with widely varied points of view. *E.g.*, Bowman, *The Prerequisites and Effects of Resale Price Maintenance*, 22 U. CHI. L. REV. 825 (1955); Commoner, *Vertical Territorial and Customer Restrictions: White Motors and Its Aftermath*, 81 HARV. L. REV. 1419 (1968) [hereinafter cited as Commoner]; Louis, *Vertical Distributional Restraints Under Schwinn and Sylvania: An Argument for the Continuing Use of a Partial Per Se Approach*, 75 MICH. L. REV. 275 (1975) [hereinafter cited as Louis].

[18] *See* text accompanying notes 188-189 *infra*.

[19] This argument is developed in Carstensen, *Vertical Restraints and the Schwinn Doctrine: Rules for the Creation and Dissipation of Economic Power*, 26 CASE W. RES. L. REV. 771, 777-79 (1976) [hereinafter cited as Carstensen]. Briefly, a producer of a fungible good has no power to control the resale of its product in the absence of a producer cartel because its distributors can get fungible substitutes not subject to such conditions; and, even if control were possible, it could not affect the resale market since the controlled distributors could resell other producer's goods and other distributors could enter any market area with those same substitutes thus making any control economically irrelevant.

[20] *See* E. CHAMBERLAIN, THEORY OF MONOPOLISTIC COMPETITION (8th ed., 1962)

from a producer understanding, actual or implied, to take collective control over production of a product and its distribution.[21]

c. *Reasons for External Restraint*

Given the presence of the basic condition of market power with respect to a product, there are two possible explanations of why the parties might wish to engage in external restraints. The first explanation is that of achieving efficient distribution of the product. For a variety of reasons, producers may need distributor participation in the promotion, servicing, and selling of a product be it new or already on the market.[22] In order to obtain this conduct, the producer may simply condition the sale of its good on the distributor's doing certain things by way of selling activity. In some cases the conditioning could be truly unilateral in that no understanding would exist as to what requirements other distributors are to meet.[23]

More often, each distributor must have some assurance as to the nature of the rest of competition that it will face with respect to the sale of the product. Investment in and commitment to a product is logically going to be tempered by the prospects for making a reasonable profit on its resale under the conditions imposed. In this conceptually pure case, the dealer gets the restraint on other dealers in return for performing efficiently the distribution functions required of it, and the producer employs only that degree of restraint on both dealers individually and on inter-dealer competition needed to achieve efficient distribution.[24]

The other reason for restraints is to exploit collectively the latent market power of the parties. While traditionally the label "cartel" has been narrowly used to describe a group of competitors which have gotten to-

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[hereinafter cited as E. CHAMBERLAIN]; J. ROBINSON, THE ECONOMICS OF IMPERFECT COMPETITION (2d Ed. 1969).

[21] It is also possible to imagine a case where a group of distributors select a single producer of a fungible product and use restrictive contracts with such a producer as devices to control and police a distributor cartel.

[22] The reasons are canvassed in Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division*, 75 YALE L.J. 373 (1966) [hereinafter cited as Bork II]; *see also* Louis, *supra* note 17.

[23] Thus one distributor would be required to operate a large show-room and invest heavily in promotional activity while another in the same area might only be required to dedicate some shelf space to the product.

[24] Bork II, *supra* note 22; *see also* Amicus brief for Motor Vehicle Manufacturers Association in Continental T.V. v. GTE Sylvania, 97 S. Ct. 2549 at 3-6 [hereinafter cited as MVMA Amicus Brief] (this brief was signed *inter alia* by Donald Turner).

The matter becomes more complex whenever the dealer, as is very often the case, has some market power of its own. Such power usually arises from the locational or transactional advantage of each particular dealer in dealing with some market or class of customers. In such situations, the producer's use of inter-dealer restraint must take into account the dealers' desire to have their power respected. If we assume efficiency is the only goal, then the producer will impose and enforce only restraints related to efficiency tempered by the need to respect the power of the distributors. Bork's conceptual framework causes him to ignore these issues. Bork II, *supra* note 22; *see* Carstensen, *supra* note 19, at 784-89; *see also* Bowman, *supra* note 17.

gether solely to establish collective control over price and/or production,[25] it is an appropriate label for all conduct which involves the same basic activity: collective action solely for the purpose of creating and exploiting market power.

Traditional analysis has viewed cartel arrangements as arising only at the behest and instigation of the parties which were to benefit directly from such activity.[26] What is not traditionally recognized but is equally obvious is that a producer might act as an entrepreneur and promote and organize a latent distributor cartel interest. A producer realizing that distributors would like and might profit from some form of distributor cartel offers itself and its products as the devices to make the cartel possible. There are classic antitrust cases in which individuals have acted as the coordinating and policing forces in cartels for their own profit.[27] There is no reason to think corporate entities will not also offer this kind of service if it is profitable.

There is good, albeit speculative, reason to believe that retail cartel organization is an attractive business venture. Many retailers in selling certain kinds of goods[28] have both locational advantages as to some customers and relational advantages as to others. But in order to make use of this potential power over customers, the retailer must be in a position to offer a sufficiently differentiated product in the sale of which there is little or no competition so that the risk of lost sales or customer displeasure is kept low. To the extent then that a retailer with such latent power can have access to such goods it can exploit that power. Despite the potential advantages to them, many retailers are too small and too badly organized either to create house brands, individually or collectively, or to create cartel organizations to police their own conduct. Hence the demand for a cartel exists among many retailers, but they have neither the internal capacity nor the organizational skill to achieve these desired ends in the absence of some kind of third party effort.[29]

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[25] This implicitly narrow definition is what one sees in Bork I, *supra* note 15; Posner, *Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions*, 75 COLUM. L. REV. 282 (1975) [hereinafter cited as Posner].

[26] Bork I, *supra* note 15; Posner, *supra* note 25. *Cf.* MVMA Amicus Brief *supra* note 24. Thus producers might create a cartel to seek to obtain monopoly profits, and in order to make that cartel more efficient and effective might engage in vertical restraints of their distributors. Similarly, distributors might pressure producers into engaging in vertical restraints so that a distributor cartel might be created or made to operate more efficiently and effectively.

[27] *E.g.*, United States v. American Linseed Oil, 262 U.S. 371 (1923).

[28] Items which customers buy infrequently as well as items which they find it difficult or costly (in terms of time if nothing else) to shop for will be likely candidates.

[29] Such activity will not, of course, always be in the interest of the producer. The high volume producer with a well-established product is not interested in seeing that product used as a device for retailers to reap monopoly profits. This will reduce volume and so adversely affect profit, but producers of similar, but less successful goods, may well find it attractive to differentiate their product for the distributor as well as the customer and offer it to the distributor as part of a cartel package. *See* MVMA Amicus Brief, *supra* note 24.

If there are several producers of substitute products doing this, we may have competing cartels each trying to offer the retailer a better package of competitive restraints. Moreover, since a producer will only do this to the extent that its own profits are served thereby, from the producer perspective restraints on resale serving only a cartel function may appear fully justified as a business necessity and can be claimed to be essential to retention of that producer in that business.

One of the most common but least useful distinctions made in discussions of restraints is that between vertical and horizontal restraints. In traditional terms, vertical restraints are those imposed by one level on another, while horizontal restraints are those which involve only entities at one level.[30] In some degree this distinction is parallel to that between efficiency justified restraints and cartel based ones. The traditional horizontal restraint is one whose only function is to create and allocate market power while a vertical restraint is perceived as one designed to produce efficiency in production and distribution. But as the preceding discussion has suggested, both horizontal and vertical restraints can be either efficiency or cartel based.[31]

d. *The Problem of Characterizing External Restraints*

When evaluating an external restraint, the analyst knows at the outset that it involves the use and perhaps creation of market power. The analyst can then ask whether the restraint's function or use to the parties is of an efficiency or cartel character, or both. Resolution of the characterization

[30] *Compare* United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967) *and* Continental T.V. v. GTE Sylvania, 97 S. Ct. 2549 (1977) *with* United States v. Topco Associates, Inc., 405 U.S. 596 (1972) *and* United States v. Sealy, Inc., 388 U.S. 350 (1967).

[31] "Horizontal" restraint could also mean any restraint which derives its usefulness for the participants from its mutuality among firms at the same level, and a "vertical" restraint would mean one in which the parties are indifferent as to what others on the same level do. If this were the distinction, then most external restraints are "horizontal." Central to most of them is an understanding as to what others at the same level will be expected to do or not do. There is thus a mutality of restraint among actual or potential competitors. Indeed, the best known and most convincing of rationales for efficiency based restraints rest on the need for that kind of mutual understanding between firms on the same level of distribution. Bork II, *supra* note 22; Preston, *Restrictive Distribution Arrangements: Economic Analysis and Public Policy Standards,* 30 LAW & CONTEM. PROB. 506 (1965) [hereinafter cited as Preston]; Telser, *Why Should Manufacturers Want Fair Trade?* 3 J. LAW & ECON. 86 (1960) [hereinafter cited as Telser].

A "vertical" restraint in the sense of one lacking any horizontal mutuality would be a rare case and would reflect very substantial power on the part of the party imposing such a condition if the condition was at all onerous since the party imposed on would not be given any protection in return for its required conduct. Such a vertical restraint is very likely to be for efficiency purposes, but not necessarily so since it could represent an effort to secure or protect future power or to divide or allocate existing power.

The "vertical" and "horizontal" tags even if redefined to focus on a genuine difference, therefore, do not distinguish between the two functions of a restraint and serve only to confuse and obscure the ways in which restraints actually operate. This is more clearly the case when the usual meaning of the vertical and horizontal labels is intended.

question would focus on what the restraint is supposed to make possible.

If it is an efficiency oriented restraint, one would expect that either explicitly or implicitly one could find a set of conditions that the distributor is to meet and a clear relationship between the restraints on distributors and the achievement of a compensation for those activities.[32] This also implies that the producer has itself some fairly articulated idea of how much restraint is needed in order to get certain kinds of desired conduct, when such conduct is fully compensated, and how the conditions can be manipulated in order to achieve the desired conduct with the minimum of cost to the producer. In short, one looks for the full agreement, actual or implicit, which reflects the total business understanding and expectation between the parties.

If one finds that no specific conduct is expected of the distributor, or that the expected conduct is largely or entirely unrelated to the restraints imposed, then the function of the restraint is only to allow the distributor an area free from competition. As in the case of an efficiency based restraint, each distributor gets its benefit from the restraint on others and not on itself, but the producer gains only by being a cartel manager and having its products sold and not as a result of specific conduct required of the parties.

Even restraints requiring large amounts of effort may nevertheless be ultimately cartel in character. The required activities may not in fact be required (what policing does the producer do) or else the activities may be unrelated to the restraint thus making it clear that they are mere surplusage. Alternatively, the required activity, while related and required, may be so disproportionately little with respect to the restraint involved that it is clear that the activity itself is but an incident to the restraint. Finally, in some cases, one can imagine a fairly elaborate set of required activities which upon examination turn out to implement the restraint.[33]

In a static economic world restraints can be expected to be of only one character and correctly identifiable. This is so because in a static world, economic power is already distributed and a vertical relationship will not affect that predetermined power allocation.[34] Hence the producer will have whatever power it may possess and will, if it is engaging in efficiency based

[32] This is the ancillary analysis which Taft held necessary to establish a right to a rule of reason analysis. United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

[33] Once one dimension of competition is fixed, it is quite possible, indeed probable, that firms may start to compete in other dimensions, e.g., "excessive" service or promotional activity. To avoid this and insure the participants their monopoly profits, it may become necessary to restrict this competition. Such restriction, in order to avoid the appearance of blatant illegality, may take the form of a list of required activities which appear to be affirmative obligations but which in fact are upper limits.

[34] *See* Bork, *Vertical Integration and the Sherman Act: The Legal History Of An Economic Misconception*, 22 U. CHI. L. REV. 157 (1954). This limiting character of static analysis is explored in Scherer, *Predatory Pricing and the Sherman Act: A Comment*, 89 HARV. L. REV. 869 (1976). *See also* Carstensen, *supra* note 19.

restraints, seek only to impose on the distributor the least amount of restraint necessary to achieve the desired goal. Hence any restraint which is excessive will be by that fact clearly a cartel type restraint since it would make no business sense otherwise.

The real world of commercial activity is not, however, static. It is a world in which market power is a dynamic element created and allocated by ongoing market activity.[35] In such a world, restraint may and probably will serve both efficiency and cartel interests either over time or at the same time. It will create market power by inducing the doing of things needed to differentiate and otherwise establish a product; it will allocate that power by determining how much is retained by the producer and how much by the distributor, and it may operate in a longer perspective to try to fix and determine, to the extent that the parties can, the relative power relationships among the parties for the future and in more general terms.

Hence once the dynamic character of market power is recognized, it is not possible to assume with Mr. Bork that all "vertical" restraints which have an efficiency justification are reasonable, nor is it possible to conclude that by showing a restraint to be unreasonable one can infer that the restraint is entirely of a cartel character. In fact, given a dynamic economic world, it is reasonable to suppose that many restraints may have both characteristics in some measure, and purely cartel or efficiency oriented restraints will be the exception.[37] The key point for present purposes is that there is no reason to believe a priori that an external restraint involving firms vertically related is necessarily purely efficient in character. This is true even in a static economic world but is even more likely in the real world of dynamic market power.

2. *The Legal Analysis of External Restraints: Pre-*Sylvania

a. *Resale Price Restraints*

The development of the law on this topic has received extensive treatment elsewhere[38] and need not detain us for very long. Certain salient features do however deserve mention. The initial resale price control decision, *Dr. Miles Medical Co. v. John D. Park & Sons, Inc.*,[39] from which

[35] This idea is developed in general terms in Adams, *Market Structure and Corporate Power: The Horizontalist Dominance Hypothesis Reconsidered,* 74 COLUM. L. REV. 1276 (1974), and related to market restraints in Commoner, *supra* note 17, (generally restraints are relevant to creating market power by facilitating product differentiation which in turn creates market power for such products which is then protected, augmented and entrenched by the use of restraints); *cf.* Louis, *supra* note 17.

[36] Bork II, *supra* note 22.

[37] Bork recognizes this to be the case for horizontal restraints because such restraints can, even in a static world, create market power and thus can serve both cartel and efficiency interests. Bork II, *supra* note 22.

[38] *E.g.,* Bork, *supra* notes 15 and 22; Posner, *supra* note 25; Carstensen, *supra* note 19; Telser, *supra* note 31; Preston, *supra* note 31.

[39] Dr. Miles Medical Co. v. John D. Park & Sons, Co., 220 U.S. 373 (1911).

many have derived a per se rule[40] with respect to all price fixing in vertical resale situations was a frank and confessed cartel situation.[41] The case thus fitted closely with the existing run of price fixing cases in which the defendants had sought to prove the reasonableness of the agreed price.[42] The only novel legal claim advanced to justify and distinguish this conduct was the assertion that resale price control is an attribute of the property rights of the producer.[43] This is a claim for general and absolute, hence "property," right to control subsequent resale of a producer's output. Although rarely remarked upon in commentaries, it is nevertheless significant that the ancient general rule against "restraints on alienation" was invoked only with respect to this contention.

Dr. Miles was decided contemporaneously with *Standard Oil Co. v. United States*[44] and *American Tobacco Co. v. United States*[45] and so should be read and was clearly intended to be read as an application of the rule of reason announced in those cases. As such, *Dr. Miles* condemns as unreasonable without inquiry (i.e., per se illegal) only a cartel-type vertical price control agreement, and rejects any assertion of a non-contractual, "property" right to control the conduct of resellers.

Subsequently in *United States v. Colgate & Co.*[46] the Court explicitly recognized that a producer has a legitimate interest in the conduct of the reseller of its product. The implicit rationale for the holding is that all vertical controls were not necessarily of a cartel character. In order to allow some protection for these efficiency interests,[47] the Court upheld an announcement of policy and subsequent refusal to deal rationalizing this as a circumstance lacking an agreement. The unfortunate result of this approach was that the next set of cases involved the issue of whether or not there was an agreement rather than whether or not price control protected

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[40] *E.g.*, M. Handler, H. Blake, R. Pitofsky & H. Goldschmid, Cases and Materials on Trade Regulation, 568 (1975) [hereinafter cited as M. Handler, H. Blake et. al.].

[41] This is clear from the complaint by Dr. Miles which only asserted that the favored dealers could not charge the desired prices if there was competition and did not in any way assert that the purpose of this price control was to allow dealers to do things needed to promote distribution.

[42] United States v. Joint Traffic Ass'n, 171 U.S. 505 (1898); United States v. Trans-Missouri Freight Ass'n, 166 U.S. 290 (1897); United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

The only difference was the vertical relationship between Dr. Miles and its distributors, but that, as has been argued above is not a functional difference. *See* text accompanying notes 30-37 *supra*.

[43] 220 U.S. at 385-87.

[44] 221 U.S. 1 (1911).

[45] 221 U.S. 106 (1911).

[46] 250 U.S. 300 (1919).

[47] The Court was not at all clear or explicit on this characterization issue, and indeed the allegations suggest *Colgate* was operating a modified retail cartel. Nevertheless, the appeal of the *Colgate* result is that it recognizes the obvious interest of a producer of differentiated products in the way its distributors behave and the need to have some control over that behavior including pricing policy.

a legitimate interest of the producer.[48] In these cases the defendants' argument of no agreement was in reality a variation of the property right argument rejected in *Dr. Miles.*[49] Moreover, since few if any of these cases involved anything other than cartel conduct in fact, by refining the definition of agreement to encompass the various cases in which a producer and competing distributors had reached an understanding on resale prices, the Court was only covering all the variations in which cartel conduct came.

Only in the *Albrecht v. Herald Co.*[50] case did the issue of the justification for a price fixing agreement finally surface. *Albrecht* involved the efforts of a monopoly newspaper to control the maximum resale price of its carriers each of which had an exclusive territory. Presumably exclusive territories were an efficient distribution technique,[51] but their effect was also to create significant market power in the carrier within their territories. Hence, the newspaper conditioned continuance of the assignment on the agreement to honor the price schedule. In condemning this agreement as per se illegal the Court suggested that it may have been a cartel.[52] But rightly conceding that it could not tell (and indeed the balance of probability tips the other way), it ultimately condemned the agreement as illegal without opportunity for justification even though it may have been an efficiency justified one.[53]

The Court justified its result on the ground that individual businesses must have nearly absolute freedom to decide what price to charge. Such freedom is essential to the independence of business.[54] The Court may have been suggesting that although there are social costs in terms of economic inefficiency, the gain in terms of other social values offsets these costs, or that as a matter of dynamic economic policy the better approach is to disallow certain controls efficient in the short run because of their cost to the dynamic potential for development of our economy.[55]

b. *Non-Price Controls on Reseller Conduct*

There is a paucity of case law prior to 1963 on the proper analysis of

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[48] *See, e.g.*, United States v. Parke, Davis & Co., 362 U.S. 29 (1960).

[49] The appellee was asserting a "*Colgate*" right to announce and enforce terms of resale and not defending on the grounds of efficiency considerations. *Id.* at 35-37, 45-46.

[50] 390 U.S. 145 (1968).

[51] Because of the need for quick delivery and intensive coverage of an area, the arguments are especially compelling here. *See* Preston, *supra* note 31.

[52] 390 U.S. at 150 n.6.

[53] *Id.* at 152-53.

[54] *Id.* at 152.

[55] This is the thesis of the writer's earlier analysis of these cases, Carstensen, *supra* note 19.

A third alternative rationale for *Albrecht* which, in light of *Sylvania,* may have greater significance is that the difference between a cartel justified and an efficiency justified external price restraint is so hard to determine in practice (an experience over 70 years suggests that efficiency justifications are unlikely, and in any event unlikely to justify price control as opposed to other less restrictive controls) that the public interest is best served by the blanket condemnation which includes even efficiency justifications. *See* Louis, note 17.

non-price external restraints.[56] Indeed, it was not until the early 1950's that the antitrust enforcement agencies concerned themselves with these problems in any degree.[57] A few early cases condemned non-price controls, but these involved situations where there was also a direct price control to which the territorial or customer assignments were incidental, and the entire package was clearly of a cartel character.[58]

Hence, the Supreme Court first faced the issue of a fairly pure non-price restraint in *United States v. White Motors Co.*,[59] and White Motors presented one of the more forceful arguments for the efficiency analysis of external restraints.[60] White Motors did not assert that it was necessarily not in violation of the antitrust laws but only, that it deserved to make a record on the need for restraints and the reasonableness of the restraints employed. The Court, therefore, remanded the case for a full trial leaving open the prospect that it would still adopt a "per se" rule after that trial. Such a per se rule might not have distinguished cartel and efficiency restraints, but could have condemned all equally. If the Court had emphasized that there is a problem of characterization in all restraint cases and that only those situations fitting within the cartel characterization are to be treated as per se illegal, then its use of "per se" would have been clear and consistent with its past practice. As it was, especially in light of Justice Brennan's concurrence,[61] it seems that the Court felt it could and should in light of a suitable record condemn generally even an efficiency justified restrictive practice.[62]

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[56] The only cases in the Supreme Court prior to *Schwinn* were FTC v. Curtis Publishing Co., 260 U.S. 568 (1923) (territorial assignments upheld where assigned parties were characterized as, and appeared in fact to be, true agents and not independent business entities); United States v. Bausch & Lomb Optical Co., 321 U.S. 707 (1944) (equally divided court affirmed a finding of no violation as to territorial restraints).

[57] Robinson, *Restraints on Trade and the Orderly Marketing of Goods*, 45 CORNELL L. REV. 254 (1959).

[58] E.g., United States v. Trenton Potteries Co., 273 U.S. 392 (1927); United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

[59] 372 U.S. 253 (1963).

[60] White Motors asserted that its trucks were in large part custom-made and the dealer must therefore engage in expensive design work with a prospective buyer. If the buyer, once a suitable design was developed, could then go to other dealers for the truck, the other dealers, not having the costs of doing the design work, could easily beat the price of the dealer who had to cover design expenses. Hence, it argued, some control over the dealer competition was essential, and its use of customer controls and territorial assignments was a reasonable solution to that problem.

[61] Justice Brennan sought to define when a nonprice restraint might be reasonable, and his terms of reference clearly exclude from reasonableness many potentially efficient restraints, 372 U.S. at 264-75 (Brennan, J., concurring). *See* Bork I, *supra* note 15, at 826-27; Bork II, *supra* note 22, at 470-71.

[62] Whatever the Court intended by way of fuller record in *White Motors* never occurred for White Motors settled the case largely on the terms that the government had sought. 1964 TRADE CAS. (CCH) ¶ 71, 762 (N.D. Ohio). Thus, having represented to the Court that a full defense was possible and having implicitly promised to provide it, White Motors then agreed that none of its restraints were needed.

The first fully litigated case to reach the Court was *United States v. Arnold Schwinn & Co.*[63] which arrived four years after *White Motors*. *Schwinn* has been extensively canvassed elsewhere.[64] It is customarily read as announcing a rule based on formal title,[65] but it can be read as announcing a rule base on the functional relationship of the parties.[66] The rule, however based, forbade external non-price restraints. How generally was, of course, an open question. In understanding the *Schwinn* outcome, it is important to recall that much of Schwinn's argument had the flavor of a claim that as a producer it had an absolute right to control non-price resale activity,[67] that neither Schwinn nor the government distinguished between cartel and efficiency based restraints,[68] and that Schwinn's rule of reason argument was cast solely in dynamic terms, i.e., the right of a small firm to survive, and did not separate out an explicit efficiency claim for the restraints.[69]

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[63] 388 U.S. 365 (1967).

[64] *See, e.g.*, Louis, *supra* note 16; Posner, *supra* note 25; Carstensen, *supra* note 19.

[65] Continental T.V., Inc., v. GTE Sylvania, 97 S. Ct. 2549, 2554 (1977).

[66] Where the manufacturer retains title, dominion and risk with respect to the product *and the position and function of the dealer in question are, in fact, indistinguishable from those of an agent or salesman* of the manufacturer, it is only if the impact of the confinement is "unreasonably" restrictive of competition that a violation of §1 results from such confinement, unencumbered by culpable price fixing.

United States v. Arnold, Schwinn & Co., 388 U.S. at 380 (emphasis added). The implications of this functional approach are developed in Carstensen, *supra* note 19.

[67] *See* Brief for Appellee, United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1968) 64-5, 56-7 [hereinafter cited as Schwinn Brief for Appellee]. The argument was put in terms of a right which Schwinn ought to have in its own interest as a small producer and in the interest of its retailers who were small businesses competing against giants. This right was one to which apparently not all producers, especially larger ones were entitled. *Cf.* Baker, *Vertical Restraints in Times of Change: From White to Schwinn to Where?*, 44 ANTITRUST L. J. 537 (1975) [hereinafter cited as Baker].

[68] Schwinn Brief for Appellee, *supra* note 67, did purport to assert an ancillary analysis, *id.*, at 59-60, 62-64, but in fact never related the restraints to specific conduct required of its retailers or distributors so as to complete the argument. The real argument was a populist claim that "little" Schwinn and its small dealers had a right to impose these restraints to stay in business. *Id.* at 30-31, 65-68, 90-96.

The government's Brief was similarly nonspecific about the efficiency and cartel analysis. It essentially equated any restraint which involved any horizontality with a cartel. *See* Schwinn, Brief for Appellant *supra* note 67, *excerpts reprinted in* R. POSNER, ANTITRUST CASES, ECONOMIC NOTES AND OTHER MATERIALS 266-72 (1974).

[69] The recurring theme of the Schwinn brief was that it, and more importantly, its retailers would some how be driven from the market unless these restraints were upheld. Brief for Appellee, *supra* note 67, at 90-96. Without more, this was a reverse form of the argument for protecting independent business used in *Albrecht* and *Topco* and did not imply an efficiency justification for the restraint since a cartel based one would also have served this ultimate good purpose. *See* note 80 *infra*.

Indeed, the facts in *Schwinn* suggest that its efficiency case was very weak. Schwinn already distributed most of its products via a system which employed agents to book orders which Schwinn then filled by direct shipment. Pollock, *Alternative Distribution Methods After Schwinn*, 63 Nw. U. L. REV. 595, 606-07, (1968). Even for fill-in purposes, most of the necessary supplies were stored by Schwinn at its expense in warehouses from which it authorized its retailers to draw supplies as they required and for which Schwinn then billed them.

It is nonetheless true that when Schwinn lost its case it did so in a way pointed toward general condemnation of non-price restraints regardless of the functions which those restraints served. Particularly in light of Schwinn's alternative distribution methods and White Motor's surrender,[70] the Court may well have inferred that such controls were generally unnecessary or that the same ends could be handled in other ways.

The next major development in the area of non-price restraints was *United States v. Topco Associates, Inc.*[71] Topco, a joint venture among a group of small retail grocery chains, provided for its participants a general buying agency and had its own trademarks placed on some of the products it obtained for its members.[72] Each participant could sell Topco brands only in an assigned territory, and within that territory the participant's stores were the only ones that promoted and sold the Topco brands. This made the Topco branded products the functional equivalent of large chain's house brands, which are very important to success in the retail grocery business.[73]

Topco was by its own evidence as much as ten times larger than it need have been.[74] It, therefore, produced up to ten times as much competitive foreclosure as was needed assuming rigid territorial assignments were essential.[75] Despite this obviously unreasonable character, the trial judge

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Id. at 607-08. Having thus demonstrated that it had effective alternatives to control and functionally independent distributors for the distribution of its products, Schwinn should have been hard pressed to justify its use of territorial and customer restraints as reasonably necessary for efficiency.

Schwinn might also have argued that even when the bicycles were "sold," the "buyer" was not a functionally independent business, but was in reality nothing more than an agent or employee, and the title transfer was but a tax or property law device having no functional significance. Instead, Schwinn accepted the implicit characterization of the buyers as functionally independent business even while establishing that these same entities when dealing with Schwinn under other distribution arrangements were nothing more than manufacturers representatives or agents.

[70] *See* note 62 *supra*.

[71] 405 U.S. 596 (1972). *Topco* is characterized as a horizontal case although it involved a clear vertical relationship between Topco and the participating grocery chains. The reason for the characterization is apparently that the grocery chains had created Topco. If the facts were otherwise, perhaps it would have been regarded as a vertical case.

[72] It is perhaps significant that Topco itself did little or no productive work of its own, but rather acted almost entirely as a middle man or agent for its members. *Id.* at 602-03.

[73] House brands appear to be important for several reasons. First, they have a lower cost to the store and so can either be marked up more or sold at a rate significantly below that asked for similar products sold under nationally advertised brands. Second, to the extent that house brands generate consumer loyalty, the retailer can be assured that consumers will have to return to its store because, by definition, no other retailer carries that brand. The arguments for Topco's restraints related primarily to this second reason.

[74] Topco's members combined total retail sales in 1967 were more than $2.3 billion. 405 U.S. at 600. But according to Topco's evidence for an efficient house brand program a retailer or group of retailers needed sales of $250 million or more. 405 U.S. at 614 n. 1 (Burger, C. J., dissenting).

[75] What is postulated here is that Topco could have been divided into about ten coopoeratives, and each would have been as efficient as Topco and, even assuming rigid territorial

found that Topco was reasonable. In reversing, the Supreme Court confirmed the sweeping rule of per se illegality for territorial restraints relying in part on the *Schwinn* case but including a number of other cases all of which involved cartel situations.[76] At some points in the opinion the Court refers to the Topco arrangement as a naked restraint;[77] and if the Court perceived the facts in *Topco* that way, Topco was merely a variant of the traditional cartel. On the other hand, the stated rationale is similar to that in *Albrecht* and suggests a general social policy of antitrust law to suppress all restraints on the freedom of business regardless of justification.[78]

Justice Marshall's majority opinion also asserts the desire to avoid rambling in the economic thickets,[79] but what thickets does he have in mind? On the one hand if Justice Marshall saw this as a cartel case in which the cartel seeks to defend itself on the ground that it is a good cartel,[80] then the refusal to be lured into a discussion of possible economic arguments to justify such a cartel is consistent with the long line of cases going back to the very first price fixing cases. On the other hand, if this is indeed a joint venture which requires some restraint in order to operate efficiently, and the Court is refusing to consider that argument,[81] then its position can be defended, if at all, only on the ground that the dynamic economic or social implications of such restraints, absent special facts, preclude a full consideration since the balance between the economic gain in static terms of an efficient restraint and the social or dynamic economic costs in any specific case is something impossible for a court to determine.[82]

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allocation, there could have been ten chains with a right to compete in each area where there was presently only one.

[76] 405 U.S. at 607-08.

[77] *Id.* at 608.

[78] *Id.* at 610.

[79] *Id.* at 611-12.

[80] It is a good cartel, presumably, because it protects small chains from competition *inter se* thus creating partially protected markets (protected from competition by other small chains) and preserving more competitors for some ultimate comercial Armageddon. Such partial protection may be very valuable if customers who use regional and local chains are, in any economically significant number, differentiated from those who use national chains so that competition between small chains would be more intense and more worrisome. There is some evidence of this, *see* National Tea Co. [1965-1967 Transfer Binder] TRADE REG. REP. (CCH) ¶ 17, 463 (1966), and its theoretical predicate exists. *See* E. CHAMBERLAIN, *supra* note 20; Markovits, *A Response to Professor Posner,* 28 STAN. L. REV. 919, 920-32 (1976).

[81] This is the way Chief Justice Burger saw the case in dissent, 405 U.S. at 613-24, but his failure to detect the obvious problems in even a prima facie efficiency case on these facts greatly weakens the force of his general position.

[82] And yet despite the per se label and sweeping language of the opinion, the trial court entered a decree which allowed Topco to continue to exist and to allocate territories among its members, and the Supreme Court affirmed that decree. United States v. Topco Associates, Inc., 414 U.S. 801 (1973), *per curiam aff'g* 1973-1 TRADE CAS. (CCH) ¶ 74, 485, ¶ 74, 391 (N.D. Ill. 1973) (decree).

c. *The Pre-*Sylvania *Cases on External Restraints In Context*

Overall, the Supreme Court, with one exception,[83] has consistently rejected those restraints which have no defense beyond their creation and distribution of market power and subjected them to per se condemnation. Very generally it also has subjected efficiency justified restraints to tests of reasonableness. External restraints on distribution, however, have not fitted this general pattern as the foregoing discussion has suggested.[84]

The cases involving external restraints whether involving price control or non-price control had by the time of *Schwinn* and *Albrecht* arrived at a parallel solution to the question of the legal standard. Such restraint was generally forbidden. In reaching this result, however, the Court rejected more or less consciously the distinction between the cartel restraint and the efficiency restraint as a useful distinction upon which legal standards might depend. But as the cases came to condemn more clearly efficient restraints, the apparent inconsistency between the outcomes and rational economic policy and defensible social control of business became more pronounced. At the very least, the Court was unsuccessful in communicating the true bases of its decision.[85] The opinions in *Schwinn* and *Topco* are two noteworthy examples of bad workmanship, sloppy use of terms, and a persistent failure to examine the reasons why the decision might be criticized.

It is fairly easy on the facts of *Topco* to argue that it was, in all likelihood, a traditional cartel despite its appearance and so justify the result if not the majority opinion. But in *Schwinn* and *Albrecht* and, of course, *White Motors,* the Court confronted restraints more defensible on efficiency grounds. Because it allowed for an exception for new and failing firms, the per se condemnation in these cases is qualitatively different from the traditional one found in *United States v. Socony Vacuum Oil Co.*[86] In addition, those who violate the *Topco-Schwinn* per se rule can and have obtained decrees which permitted them to continue some form of the apparently offending practices.[87] Despite these two obvious differences from traditional per se values the Court did not, in its decisions, either explicate the basis for its conclusions or acknowledge that it was expanding or altering the traditional per se category. An outside observer could reasonably conclude that the "per se" category encompassed any practice that a ma-

[83] United States v. National Ass'n of Window Glass Mfrs., 263 U.S. 403 (1923).

[84] This argument is developed in Carstensen, *supra* note 19, at 831-38. *See also* Bork I, *supra* note 15.

[85] Kauper, *The 'Warren Court' and the Antitrust Laws: of Economics, Populism and Cynicism*, 67 MICH. L. REV. 325 (1968).

[86] 310 U.S. 150 (1940).

[87] *See, e.g.,* United States v. Topco Associates, Inc., 1973-1 TRADE CAS. (CCH) ¶ 74, 391 (N.D. Ill.), *modified*, 1973-1 TRADE CAS. (CCH) ¶ 74, 485 (N.D. Ill.), *aff'd per curiam*, 414 U.S. 801 (1973); United States v. Arnold, Schwinn & Co., 1968 TRADE CAS. (CCH) ¶ 72, 327 (N.D. Ill. 1967).

jority of the Court condemned but that there was no logic to the labeling and no way to predict outcomes.[88]

3. *The* Sylvania *Case*

a. *The Facts*

Sylvania, a subsidiary of GTE a large conglomerate, is a maker of television sets. It was not in the late 1950's and early 1960's a very substantial factor in television sales and its share was declining.[89] No reason is given for this decline, and no claim was made that the dominant firms, RCA and Zenith, engaged in predatory practices or otherwise attempted to drive the smaller firms from the market, or that access to retail outlets was in any other way restricted. Hence the most likely explanation for Sylvania's relative decline is that RCA, and Zenith, and others made a better product in the opinion of most customers.

Prior to 1961 or 1962, Sylvania had sold its sets to wholesalers in various parts of the country who in turn resold the sets to retailers. In appears, inferentially, that most retailers were very small operators having a very low volume of sales and were not for that reason very attractive outlets since they did little or nothing to promote the product and were expensive to serve.[90] In 1962 Sylvania decided to bring in new management for its television set division, and the new managers decided to alter the distribution system. They terminated most of the wholesalers and introduced in most areas a direct factory sales system.[91] Second, they decided to franchise dealers and to limit those franchises to a small group of dealers (compared to their previous selling group). The chosen dealers were to be in the larger volume category.[92] As part of this plan Sylvania would only franchise specific selling locations and a chosen dealer could sell only at its franchised location. The stated purpose of this requirement was to provide "elbow room" for each dealer.[93] The promotional materials are quite explicit that the function of the policy is to create market power in the franchised dealer with respect to Sylvania set sales so that each dealer can maintain its desired price level.[94]

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[88] *See* Posner, *supra* note 25.

[89] Although exact shares are not given, Sylvania had about 3-5 percent prior to 1960 but had declined to about 1 percent by 1961 or 1962.

[90] Joint Appendix to Briefs for Petitioner and Respondent, 23-24 [hereinafter cited as Joint Appendix].

[91] This resulted in some cost savings since sets were now shipped direct from the factory to the retailer and no separate inventory was maintained in different localities.

[92] *Id.* at 23.

[93] *Id.* at 25. Sylvania's promotional material explained that, "the franchise contains a good profitable selling climate by creating 'elbow room' in a sensible territory based on market and dealer potential."

[94] S.L.D. [Straight Line Distribution] also eliminates 'same brand competition.' Sylvania wants fewer dealers and—quality rather than quantity. By not over franchising, Straight Line Distribution eliminates vicious price cutting and estab-

Continental TV was a specialized retailer operating in the San Francisco Bay area selling primarily to customers in their own hcmes at prices at least as high as those listed by Sylvania.[95] Continental did also operate several retail stores, and its business flourished so that it was also among Sylvania's largest customers.[96]

In 1965, Continental decided to enter the Sacramento area, and Sylvania's sales personnel understood that it planned to use Philco and Motorola products.[97] Sylvania at that time had as its only outlet in Sacramento one of the two leading television set dealers in the community[98] which had produced substantial sales for Sylvania.[99] The dealer was also affiliated with a wholesaler who distributed Sylvania products in some rural areas to which the elbow room and direct selling programs had not yet been extended.[100] Sylvania's managers did not want to create any additional competition for this firm.[101] Further complicating the relationship between Sylvania and Continental was Sylvania's decision to grant another franchise in San Francisco located near Continental's show room to a seller Conginental regarded as a likely price cutter on Sylvania products.[102]

During the summer of 1965, Continental first placed a large order for Sylvania products, then, having learned that the competitor to which it objected was to be allowed to enter San Francisco, cancelled its order and indicated that it was going to use Philco products primarily.[103] However, a few weeks later it requested permission to have a Sylvania franchise for its new Sacramento location which had previously been announced as a major new Philco outlet.[104] Sylvania refused permission; Continental nevertheless moved sets to which it had title from its other franchised locations to Sacramento. Sylvania responded not merely by cancelling its franchise agreements and stopping sales to Continental but by causing all Sylvania sets still in Continental's possession to be repossessed and even having Continental's doors chained shut.[105]

> lishes suggested 'go' prices that enable each dealer to make a fair profit. . . .'Elbow room' gives every Sylvania dealer a geographic area in which to sell our Sylvania products. S.L.D. does not promiscuously franchise dealers without first studying their size, location, and effect on the market (as well as other Sylvania dealers in the area). By franchising dealers by territory—Sylvania becomes an important profit factor to its dealers.

Id. at 27.

[95] *Id.* at 113-15 (testimony of L. French, Sylvania sales Manager).

[96] Continental was handling 50% of all Sylvania sets sold in the area. *Id.* at 58.

[97] *Id.* at 66.

[98] *Id.* at 127-29.

[99] *Id.* at 171.

[100] *Id.* at 161.

[101] *Id.* at 168.

[102] *Id.* at 340.

[103] *Id.* at 66.

[104] *Id.* at 64-80.

[105] *Id.* at 104. Continental survived this onslaught but was forced to close some of its stores including its Sacramento operation.

In response to the efforts to repossess its inventory, Continental counterclaimed for an antitrust violation. The antitrust issues were separated and tried to a jury with retired Justice Clark sitting as the trial judge. In evaluating the antitrust issue it is essential to make a business analysis of the record to see what it tells about the business reason for this restraint.

b. *A Business Analysis*

The initial but fundamentally unanswered question in this case is why did Sylvania do what it did? Why did it seek to restrict distribution to a limited number of dealers in an area? What function or purpose was this to serve? The testimony of the top managers of Sylvania was that restricted distribution was seen as a way to increase the profits of the television business and expand volume.[106] How? That issue is rarely addressed and not answered except in the very general terms of creating an exclusive or quality image for Sylvania, i.e., to differentiate the product. There was certainly no claim of special investment or risk taking by dealers who handled these sets. Similarly, the field representatives charged with implementing this plan were told to emphasize the fact that the participating dealer would face less competition in selling Sylvania products,[107] but they offered no coherent explanation of what Sylvania expected in return or how the elimination of competition with respect to a product which held at the time only a one or two percent share of the total television market would be of the slightest interest to the dealers with whom they were talking, the larger volume dealers.

The testimony was also very unspecific as to the basis for initial dealer sanction and for addition of dealers in areas.[108] There was a kind of a bottom line criteria based on a desired share for Sylvania of total sales of television sets in an area.[109] But how control over the number and addition

[106] Morgan, president of Sylvania's TV business testified that the management, "felt that Sylvania could fulfill a need and the need was to provide a line of merchandise to dealers that they would be proud to sell and we would be proud to sell and everybody could make a living at it, make the kind of profit they would make on it." *Id.* at 132. While Steiner, the national sales manager, explained that Sylvania "needed something, a sales pitch that the sales company could use in order for us to get a foot hold in the market. . . . [If] we were in a 'me too' approach . . . there was no reason for the dealers to handle our line because they would handle other lines." *Id.* at 365. Moreover, the list prices were adjusted so that a dealer would receive a generous return on his investment. *Id.* at 371. Similarly, the present head of Sylvania's TV business stressed profits: ". . . with this elbow room . . . [the customer] has less area to shop in and we think resultingly area dealiers gross a better profit from our line." *Id.* at 390.

[107] *See id.* at 39, 183, 359 (testimony which suggests that profits were the primary selling point).

[108] The testimony stressed that dealers were selected in terms of total sales in an area and the sales volume desired by Sylvania in that area. *Id.* at 39, 52, 91, 124, 148-49, 171, 189, 206-07, 391-92. Replacement dealers were expected to take over the duties of their predecessors, but those duties were never explicitly stated. *Id.* at 180, 52.

[109] *See, e.g., id.* at 149. Sylvania expected each district to generate sales at least equal to one percent of total television set sales in that area.

of franchises was to serve the functional goal of adding to sales was never explored.[110]

The selling documents that are quoted in part similarly reflect only a final conclusion: sales and profits for both retailer and producer will be better from the use of this system.[111] But why? The franchise agreement itself is likewise not very informative. It makes no explicit, unusual requirements of a dealer in terms of service, promotion or other activity;[112] but there are several very elastic clauses that could be the basis for an assertion that the implicit understanding was that the dealer was to do certain things in return for a partially protected market, and that this would vary from market to market.[113]

Looked at in terms of the alternative ways in which restraints can be explained, either as promoting efficiency in production and distribution or as serving only the interest of facilitating some exploitation of market power, there are bits of evidence that go both ways.[114] On the side of efficiency there is a suggestion from time to time that dealers were expected to engage in promotional activity,[115] provide a reasonable amount of display area so that the entire line of sets could be shown,[116] and that in other ways dealers were expected to undertake costs and assume risks with respect to the promotion, sale and service of Sylvania sets that could be recompensed only if they were substantially assured that the market demand which they would have participated in creating would not be suddenly flooded with sets being sold by dealers who did not have to bear these costs.[117]

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[110] *See, e.g., id.* at 39, 24. The goal of sales people for Sylvania was put in terms of coverage or penetration, ultimate measures of sales volume, which the restraint somehow made possible, and not in terms of specific conduct obtained or retained as a result of the restraint.

[111] *See* notes 93 & 94 *supra.*

[112] The franchise agreement is set forth at Joint Appendix, *supra* note 90, at 18-22.

[113] *Id.* at 19. The franchise agreement provided: "3. Dealer agrees to maintain an *adequate* stock and *representative* display . . . and to promote *vigorously and effectively* the . . . merchandise." (Emphasis added). *See also* sections "4" and "5" of the agreement which require "proper installation and service" and adherence to "advertising and promotional policies from time to time established."

[114] The attitude of Sylvania's managers may be one of indifference to this distinction. They are interested in total sales; and whether those sales come from increased efficiency in distribution or from providing a method of exploiting market power, absent external legal requirement, is of no concern to Sylvania. Similarly, at the field representative level, it is not unimaginable that, since either a cartel or an efficient system of restricted distribution can achieve the same final result in terms of total sales, the actual use of the restraints may have varied from location to location.

[115] In addition to the franchise agreement requirement, *see* note 110 *supra*, several witnesses mentioned this as a duty of the retailer, *see, e.g.*, Joint Appendix, *supra* note 90, at 376, 390. There was, however, no evidence which indicated that this conduct included special or unusual efforts.

[116] The display of a full line was referred to as a dealer duty. Joint Appendix, *supra* note 90, at 39, 367, 390. *See also* the agreement, note 113 *supra.*

[117] *See, e.g.*, Joint Appendix, *supra* note 90, at 180.

On the other side, the emphasis on retaining profit levels and having a product over which the retailer had power together with an independent effort to imbue Sylvania sets with an aura of exclusivity and high status are all consistent with a plan to create a product image and a set of restraints suitable for dealers who wished to exploit latent power over some classes of customers. The larger volume dealer generally may well attract different types of customers and will want to have a range of products available, a range not in a technological sense, but in a selling sense. It will want to have RCA and/or Zenith sets available for which prices will be set by competition and which will be sold to price sensitive customers. It will also desire a product line which has or can be given a high quality image and which is only available in the market in a way which insures little or no price competition. The customer who is responsive to quality claims can then be sold that higher price, "quality" set. Crucial to the success of this selling is that such sets not be conspicuously available elsewhere in the market at a clearly lower price because then competition in selling "quality" goods would break out leaving the dealer without an opportunity to exploit the customer. In essence then, the dealer in order to exploit its latent power needs not only a quality good but also, and quite inependent of the quality image, restriction on the degree of competition in the selling of those sets. The strongest evidence that this was a primary function of Sylvania's restrictive distribution program is ironically the attitude of Continental toward its new competitor in San Francisco in light of the way Continental sold and priced its Sylvania sets.[118]

The failure to produce more and better evidence with respect to the characterization issue is explicable in part by the fact that the plaintiff was indiffirent with respect to the issue believing that *Schwinn* commanded the conclusion of illegality in any event, while the defendant apparently was of the view that if it established that the ultimate effect of the restraint was to permit Sylvania to stay in the business of making and selling television sets regardless of how the restraint achieved this result, it had established its rule of reason case.[119]

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[118] Similarly, the evidence on the Sacramento situation provides a hint or two that Sylvania's motive was to protect its dealer's capacity to exploit that market without any reference to what the dealer did to promote Sylvania sales.

[119] Sylvania's belief is most clearly seen in the examination of the defendant's expert Professor Preston. *Id.* at 409; *see* Preston, *supra* note 31. Preston took the position that any means by which a marginal firm remained in business was economically desirable. Joint Appendix, *supra* note 90, at 413. The expert himself did not distinguish between the methods a firm might use to stay in business nor was he pressed to do so by either side. Explicitly asserting the self righting quality of the market, Preston maintained that even if a restraint exists for the wrong reasons the market will work it out since competing substitutes will limit and eventually eliminate the power of the wrongful actor. *Id.* at 414-15, 424-25. *See also Dr. Miles*, 220 U.S. at 409-13 (Holmes, J., dissenting).

c. *The Decisions Below*

Justice Clark, sitting by designation, instructed the jury that if it found an understanding between the producer and distributors to use location franchises, it should find a violation. He gave, in short, a per se instruction based on his reading of *Schwinn* which he felt outlawed such restraints. There is also a hint, but, alas only a hint, that he was not persuaded on the merits that the defendant had presented a case on the issue of reasonableness that entitled them to get to the jury.[120]

On appeal, a panel of the Ninth Circit upheld this result in a 2 to 1 vote;[121] the majority concluded that *Schwinn* did apply. This decision induced a spate of comments, largely unfavorable;[122] meanwhile the opinion was withdrawn and the case set for rehearing en banc. The en banc decision resulted in a reversal of the district court by a 7 to 4 vote.[123] The en banc majority argued that locational clauses did not fall under the *Schwinn* rule since *Schwinn* involved absolute limits on the customers to whom a dealer could sell while locational clauses did not.[124] The majority drew support from the decrees in *Schwinn* and *Topco* both of which allowed some form of locational assignment, from the continued judicial acceptance of exclusive distributorship and other franchise arrangements, and from general policy arguments about the purpose and goal of the Sherman Act.[125] The majority assumed that having found *Schwinn* inapplicable, a rule of reason inquiry was in order.[126]

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[120] "It is apparent that the territorial restrictions here involved were the result of a contract, combination or conspiracy *with willing dealers* to serve the interests of both Sylvania and the dealers, rather than the *unilateral imposition* upon unwilling distributors by the manufacturer to serve his own interests." Pet. for Writ of Cert., Continental TV, Inc. v. GTE Sylvania, Inc. 97 S. Ct. 2549 (1977), Appendix B at 128 (emphasis added), *citing, White Motors,* 372 U.S. at 267 (Brennan, J., concurring). One can read this finding as saying this was a cartel restraint and so illegal under *White Motors* if one sees the test of a "unilateral imposition" as really testing for efficiency (purely manufacturer) rather than cartel (dealer included) interests.

[121] GTE Sylvania, Inc. v. Continental TV, Inc., 1974 TRADE CAS. (CCH) ¶ 75, 072·(9th Cir. 1974), *opinion withdrawn.*

[122] Negative comments on this decision include: Baker, *supra* note 66; Posner, *supra* note 25; Robinson, *Recent Antitrust Developments—1974,* 75 COLUM. L. REV. 243, 275-81 (1975). Note, *Antitrust Laws—Sherman Act—Vertical Restraints: Enforcement* of *Resale Location Clauses Is A Per Se Violation of Section 1 of the Sherman Act,* 88 HARV. L. REV. 636, 641-42, 468 (1975); Note, *Antitrust Law-Vertical Restraints-Per Se Mandate of Schwinn Extended to Location Clause to Franchise Agreement,* 26 MERCER L. REV. 629, 637 (1975); Note, *Antitrust Law—Enforcement of Dealer Location Clauses Declared Per Se Illegal,* 53 N. CAR. L. REV. 775, 784-85 (1975); Comment, Schwinn *Recycled-Enforced Restriction On Location of Franchised Retail Outlets Held a Per Se Violation of Section 1 of the Sherman Act,* 49 N.Y.U. L. REV. 947, 969 (1975); Note, *Antitrust-Vertical Restraints*—Schwinn *"Per Se" Doctrine Extended To Location Clauses,* 53 TEX. L. REV. 127, 134-37 (1974).

[123] Continental T.V., Inc. v. GTE Sylvania, Inc., 537 F.2d 980 (9th Cir., 1976) (en banc).

[124] *Id.* at 988-92.

[125] *Id.* at 991, 997-1003.

[126] The opinion defined the rule of reason broadly and concluded that the testimony that asserted that the restraints made possible Sylvania's survival established a jury question. The

The dissenters argued that *Schwinn* applied because it expressed a rule of general condemnation for restraints on where and to whom a reseller might sell and so made no sense if it applied to only some restrictions.[127] They also argued that the exclusive dealing cases were not inconsistent with this reading.[128]

The key failure of all judges involved was neglecting to identify or analyze the real question presented. Thus it appears that the majority assumed that the purpose of the restraint was to promote efficient distribution, while the dissenters assumed that it operated as a cartel device.[129] Neither side separated the problem of characterization of the conduct from that of determining the proper legal standard to judge such conduct. As a result the majority incorrectly equated vertical restraint with efficiency and so with almost per se reasonableness while the dissent, correctly seeing the restraint as a use of market power, incorrectly equated it to a cartel situation and so concluded that such restraint ought to be per se illegal.

d. *The Supreme Court Decision*

1) *The Arguments*

Continental sought and got a writ of certiorari from the Supreme Court. Its position was straight-forward and limited to stare decisis.[130] The rule of *Schwinn* governed this case; the majority in the Court of Appeals had twisted and distorted *Schwinn* in order to avoid applying it and should be reversed. There was no extensive justification of the *Schwinn* rule or reasoned explication of it.[131] The brief did argue that since vertical price fixing and other vertical resale restraints are functionally identical, the condemnation of one on a per se basis should apply to the other as well.[132] Without more this is merely an argument for symmetry lacking any policy basis. Continental also argued that less restrictive conditions could have protected any proper interests Sylvania had in control of resale;[133] but because

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opinion did not define further the general rule or what factual findings were necessary to support a favorable outcome. *Id.* at 1001-02.

[127] *Id.* at 1008 (Kilkenny, J., dissenting).

[128] *Id.* at 1013-14.

[129] The majority premise is implicit in its factual statement which emphasizes efficiency type notions. *Id.* at 982-83. The minority view that this is a use of market power not related to efficiency is evident in Browning's opinion, *id.* at 1018-21, but is very much intermixed with notions of the right of retailers to be free to do so as they wish without reference to efficiency considerations.

[130] Petition for Writ of Certiorari, Continental T.V. v. G.T.E. Sylvania, 97 S. Ct. 2549 (1977).

[131] Brief for Petitioner, Continental T.V., Inc. v. GTE Sylvania, Inc. 97 S. Ct. 2549 (1977) at 37-39 (presents as desirable the stated goals of the *Schwinn* opinion, especially retailer freedom, but does not treat the efficiency considerations explicitly despite testimony from one Sylvania official that Continental's entry into Sacramento was unlikely to have a disruptive effect). Joint Appendix, *supra* note 90, at 171-72.

[132] Brief for Petitioner, *supra* note 90, at 50-52.

[133] *Id.* at 48-49, 55. While the argument purports to deal with the free rider problem and other efficiency issues, *id.* at 56-60, it ignores or understates the complexity of the problems

the record did not show what interests existed or how the restraint served them, the argument was entirely an abstraction. Interestingly, Continental's briefs did not directly address the formulation of the rule of reason and seek to obtain a more exact or limited definition thereof.[134]

Sylvania sought to defend the circuit court position that *Schwinn* did not apply,[135] but also made a direct challenge to *Schwinn.*[136] The argument was that a rule based on title-passing made no sense in a functionally oriented antitrust analysis. The argument focused on the impracticality and irrationality of such rule of illegality.

Sylvania did not stress how the rule of reason would operate as a legal standard except to assert that a manufacturer's restraints ought to be regarded as "presumptively" legal which amounts to a return to the argument rejected in *Dr. Miles.*[137] In addition, Sylvania relied on one recent rejection of the less restrictive alternative doctrine[138] by way of rebuttal to the plaintiff's argument that such alternatives existed.[139]

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and so is unconvincing especially in light of the amicus briefs that were subsequently filed in this case. Moreover, the argument failed to distinguish the facts in the Sylvania situation from those where real efficiency issues might arise although on the record as made this would seem to have been possible. Such an effort would have been relevant here to create a basis to affirm the trial court, *see* note 120 *supra,* even while rejecting *Schwinn's* per se rule.

[134] Neither did Continental argue that a proper rule of reason analysis dictated that defendant, having already been allowed to put in its case on the issue, could not prevail and so the judgment of the trial court was proper.

[135] Brief for Respondent at 31-51. Their argument strongly emphasized possible efficiency reasons for locational restraints without any reference to the record to show that the evidence supported a conclusion that Sylvania had such reasons, e.g., *id.* at 45.

[136] *Id.* at 51.

[137] *Id.* at 64-65.

[138] American Motor Inns, Inc. v. Holiday Inns, Inc., 521 F.2d 1230 (3rd Cir. 1975).

[139] Supporting the defendant were several amicii: Associated Equipment Distributors (retailers of heavy construction equipment who have substantial investment sales and service facilities as well as inventory); International Franchise Association (generally concerned with the need of franchisors to restrict competition in order to achieve specific efficiency in such business arrangements, but the argument did not develop the implicit ancillary analysis in a clear or specific way instead relying on the general *Chicago Board of Trade* formulation); Motor Vehicle Manufacturers Association (representing the major car makers, this brief argued that efficiency considerations always and fully explained producer imposed restraints and argued that the size or share of a producer should not affect this right so that, implicitly, GM may continue to use locational clauses despite its near monopoly position). Each amicus brief outlined specific fact situations in which it was assertedly necessary in order to achieve or maintain efficient distribution to have some restraint over the way in which distributors competed inter se. Although none of these briefs sought to compare its facts to those in Sylvania to show that even if Sylvania was perhaps unjustified in its conduct, such restraint might be justified in other cases, a rule of reason standard to cover the amicii would not need to encompass some general right to restrain resale independent of specific justification nor would it require protection of cartel arrangements.

Although reportedly the Solicitor General authorized the Antitrust Division to prepare an amicus breif, no such brief was filed. 791 ANTITRUST TRADE REG. REV. A-23 (Nov. 30, 1976).

2. *The Opinions*

Justice Powell, writing for a five-member majority, first rejected the effort of the court of appeals to distinguish *Schwinn* saying that there was no principled way to achieve that result, and then concluded that the *Schwinn* rule was too mechanical a way to treat antitrust issues. It followed that if the *Schwinn* rule had to go, the rule of reason applied.

The opinion begins its consideration of the proper legal standard for judging vertical restraints with the assertion that the rule of reason is the "prevailing standard of analysis [for all antitrust situations]. . . . Under this rule, the fact finder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition."[140] Conversely, a per se standard is "appropriate only when . . . conduct . . . is manifestly anticompetitive."[141] In order to determine when conduct is "manifestly anticompetitive," the Court refers to a "test" laid down in *Northern Pacific:* "Practices which [have a] . . . pernicious effect on competition and lack . . . any redeeming virtue" are those which should be held per se illegal.[142] The opinion then characterizes *Schwinn's* per se rule as turning on the "pivotal factor . . . [of] passage of title."[143] This distinction is then criticized as lacking "analytic support."

The next logical step, although not the next step as the opinion is written, is to demonstrate that there are "redeeming virtues" to at least some vertical restraints. Support for this proposition is "implicit in every decision sustaining vertical restraints," although no cases are cited.[144] Moreover, economic analysis has "identified a number of ways in which manufacturers can use such restrictions to compete more effectively. . . ."[145] There is then a list of examples of what Justice Powell presumably means by permissible or reasonable restrictions. The examples all involve efficiency type restraints,[146] and point toward specific producer

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[140] Continental T.V. v. GTE Sylvania, Inc., 97 S. Ct. 2549, 2557 (1977).

[141] *Id.* at 2558.

[142] *Id., citing* Northern Pacific Ry. v. United States, 356 U.S. 1, 5 (1958).

[143] 97 S. Ct. at 2559.

[144] *Id.* at 2560.

[145] *Id.*

[146] For example, new manufacturers and manufacturers entering new markets can use the restrictions in order to induce competent and agressive retailers to make the kind of investment of capital and labor that is often required in the distribution of products unknown to the consumer. Established manufacturers can use them to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products. Service and repair are vital for many products, such as automobiles and major household appliances. The availability and quality of such services affect a manufacturer's good will and the competitiveness of his product. Because of market imperfections such as the so-called "free rider" effect, these services might not be provided by retailers in a purely competitve situation, despite the fact that each retailer's benefit would be greater if all provided the services than if none did.

Id. at 2560-61. A footnote purports to qualify this by asserting that "marketing efficiency is interests in the efficient operation of production and distribution. None involve cartels in which the outcome is deemed desirable and so the restraint reasonable.

Having demonstrated that some vertical restraints will have redeeming virtues, the opinion reverts to the question of whether the passage of title has any relationship to the presence or absence of "virtue."[147] Finding none, the opinion concludes first that a per se rule must apply regardless of title if at all, but, secondly, having found "substantial scholarly and judicial authority," wide use "in our free market economy," and "no showing in this case" of a pernicious effect, the per se rule "must be overruled," and the law returned "to the rule of reason that governed . . . prior to *Schwinn.*"[148]

Interspersed in this discourse is an economic analysis of vertical restraints. The opinion asserts that "competition among manufacturers of the same generic product . . . is the primary concern of antitrust law."[149] And since substantial interbrand competition exists among television set makers, "it provides a significant check on the exploitation of intrabrand market power. . . ."[150] At another point, having acknowledged that the purpose of vertical restraint is to "reduce . . . competition," the Court asserts that "the ability to exploit the resulting market may be limited both by the ability of consumers to travel . . . and . . . to purchase the competing products of other manufacturers. . . ."[151] Justice Powell also suggests that efforts at product differentiation "convey socially desirable information" thus indicating acceptance of a world of monopolistic competition.[152] Finally, Justice Powell cites several lawyers, mislabelled "economists," for the proposition that "manufacturers have an economic interest in maintaining as much intrabrand competition as is consistent with the efficient distribution of their products."[153]

The Court's premise in examining vertical restraints is that a sufficient number of producers of generically identical products insures that market power will not exist. But if that is so, what sense can vertical restraints make to the parties? Why would a producer ask or distributors agree to any of the burdensome tasks which Justice Powell associates with

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not the only legitimate reason for a manufacturer's desire to exert control. . . ," and cites a case involving a producer who employed customer resale restrictions in order to reduce product liability risks. *Id.* at 2560-61 n.23, *citing,* Tripoli Co. v. Wella Corp., 425 F.2d 932 (3rd Cir. 1970) (en banc). The qualification, however, is not inconsistent with the general proposition that all the examples involve problems of economic efficiency. Thus, the restraint justified by product liability concerns is an example of reducing costs of production by handling risks in an efficient way.

[147] 97 S. Ct. at 2561-62.

[148] *Id.* at 2562-63.

[149] *Id.* at 2559 n.19.

[150] *Id.*

[151] *Id.* at 2560.

[152] *Id.* at 2561 n.25.

[153] *Id.* at 2561, *citing,* as "economists", Posner, *supra* note 25, and Bork II, *supra* note 22.

"efficiencies in distribution" unless control over the branded product will produce sufficient power over price to compensate for the costs involved? But if that is so, and it must be if vertical restraint is to make any sense, we have also described a situation in which market power exists or can exist and so can be misused. The fact that substitutes may limit this power does not change the fact that the limits are loose enough to permit some power to be exercised. The television set industry is a case in point. Sylvania's activities indicate that it did not view sets as fungible goods.[154] Thus, despite an apparent small share, Sylvania still had a product which had some market power. Justice Powell's factual premise thus does not explain Sylvania's conduct.

The Court also may accept the Bork/Posner view that producers want to maximize intrabrand competition[155] but that argument is limited to cases of efficiency oriented restraints and not cartel ones. By not stating that limitation explicitly, Justice Powell omits the factual issue of characterization. This in turn makes his economic argument less realistic.

A second problem with the opinion is the treatment of the "pivotal" issue of title passage. The absurdity of the denial that title properly defined is relevant emerges when one considers the rule of per se illegality for vertical price fixing which Justice Powell explicitly states is still good law.[156] Such a rule does not apply to master and servant, employer and employee, or to dealings with true agents or contractors. It is absurd to say that sending a package c.o.d. means the delivery person must set a price. To suggest that an employer may not tell employees what prices to charge is similarly absurd. What Justice Powell refuses to acknowledge is that title confers legal rights of control and that one with legal and equitable title has a legal, property right to control subject to whatever limits the law imposes. One with a legal right to control ought not to be held to be a wrongdoer on the mere showing that he did what he had a legal right to do. Something more is needed: the legal right may be a sham, or may result in creation of unreasonable market power, or may unnecessarily affect other interests. Conversely, one without an inherent legal right can control only if a lawful contract grants that right. The antitrust laws, among others, define when such control can be transferred. This is not to argue that a per se line should be drawn at the point where inherently lawful control ends, it is only to say that Justice Powell should not have treated title as irrelevant, because such a position ignores legal and economic realities. The real issue in this case was what contractual control is a manufacturer to be allowed over functionally independent businesses reselling its products where, absent such control, the buyer would have absolute freedom of action.

Justice White concurred in the conclusion that a rule of reason should govern this case but argued that it was not necessary to reverse *Schwinn*

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[154] *See, e.g.*, Joint Appendix, *supra* note 90, at 365, 390, 400-01.

[155] *See* note 153 *supra*.

[156] 97 S. Ct. at 2558-59 n.18.

to reach that result.[157] Justice White also suggested that *Schwinn's* per se rule ought not apply because Sylvania was either seeking to enter a market or expand therein and so fits into an exception hinted in *Schwinn*[158] This view of per se rules as only sometimes applying suggests that Justice White has in mind a rule very different from that which makes cartels illegal per se.

Justice White, the author of the *Albrecht* opinion, also sought to restate the policy underlying the *Schwinn, Topco* and *Albrecht* holdings. Justice White's argument is that *Schwinn* addressed the problem of how much control a producer ought to have over a functionally independent distributor. Independence is crucial for business, and the antitrust laws have as a goal protection of that freedom and that is at the heart of the *Schwinn* rule.[159] Justice White is obviously concerned with the way the majority has stigmatized the *Schwinn* opinion and by implication the non-economic values which it sought to protect. White's opinion does note several times that the evolution of the law in this area has not been satisfactory or clear,[160] but he urges his colleagues to proceed "deliberately" in seeking "to improve it."[161]

e. *The Remand: What is the* Rule of Reason

The case is to be remanded for a new trial under the "rule of reason." But what is the rule of reason and what does the plaintiff or defendant in a rule of reason case have to demonstrate? Justices Powell and White seem to assume that the rule of reason is a clear, well-defined standard or set of standards whose application is self-evident. There are, however, very few cases which expound or analyze the rule of reason; and those cases do so in quite contradictory terms.

The ambiguity of the standard is evident in Justice Powell's handling thereof. He defines it initially as a standard requiring that "the fact finder weighs all of the circumstances of a case . . ." and in a footnote quotes the passage in *Chicago Board of Trade* in which Justice Brandeis asserted that:

> The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competi-

[157] *Id.* at 2563 (White, J., concurring). Justice White asserts that the distinctions between the restraints in *Schwinn* and those in *Sylvania* are in fact significant and since Sylvania's restraints were not absolute, they ought not be regarded as per se illegal. Justice White secondly argues that "Sylvania clearly had no economic power in the generic market." *Id.* at 2565. This conclusion like Justice Powell's is inherently suspect because it makes the restraint illogical.

[158] *Id.* at 2566.

[159] *Id.* at 2566-68.

[160] *Id.* at 2568, 2569.

[161] *Id.* at 2569. It seems evident that Justice White is not satisfied either with the past articulation of the law in this area or with the sweeping remodeling that the majority is engaged in. At the same time, he is not prepared to offer a broad alternative view.

> tion or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulations or the reverse; but because knowledge or intent may help the court to interpret facts and to predict consequences.[162]

Justice Powell does not refer to the cases which limited and circumscribed the formulation of the rule of reason so that restraints of a purely cartel character were denied a "reasonableness" evaluation, but he does assert that per se rules are "appropriate" for "conduct that is manifestly anticompetitive." Any restraint is anticompetitive, and it is intentionally and so "manifestly" so. Cartel restraints are, however, not merely "manifestly" anticompetitive, they are solely and exclusively so. To be sure, one can argue that there is social value in a pure restraint, but it has been common ground that the policy of antitrust was to promote competition even where it was painful and that it was for Congress to alter that result if it deemed it in the public interest.[163]

If we assume then that Justice Powell's examples illustrate the class of cases in which some restraint would be permissible, they all point to efficiency considerations either in marketing or in fulfilling other duties of the producer or distributor. This would be consistent with a view of all cartel restraints as "manifestly anticompetitive" because they do not make possible specific efficient activity on the part of any party whatever ultimate good effect they might be said to have.

However, Justice Powell does not make this connection or even suggest it. Indeed, one can infer an exactly opposite conclusion given the facts of the case, Justice Powell's description thereof and the argument of the defendant's economic expert. The facts as discussed earlier certainly do not reveal a strong case for any of the efficiency arguments that Justice Powell lists as examples of the redeeming virtues of vertical restraints. Moreover, Justice Powell himself is content to describe the facts in terms of decreased competition "thought necessary to the improvement of the company's market position" without explanation except that "aggressive and competent retailers" were to be attracted thereby.[164] Such a description is consistent with a producer promoted cartel arrangement which offers "aggressive and competent retailers" a chance to eliminate competition inter se and exploit the resulting market power. The conclusion that

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[162] Chicago Board of Trade v. United States, 246 U.S. 238 (1918), *quoted in,* Continental T.V., Inc. v. GTE Sylvania, Inc. 97 S. Ct. at 2557-58 n.15.

[163] Hence, the antitrust exemptions for labor, insurance and certain activities of regulated industries.

[164] 97 S. Ct. at 2552.

the "strategy appears to have been successful" because Sylvania's share of television set sales rose suggests both something of a *post hoc ergo propter hoc* analysis and a focus on some final outcome as the proper measure of reasonableness,[165] and not the way this outcome was achieved. Such an approach could suggest almost per se lawfulness for such restraints unless the evidence showed monopolization or some other independent evil. In fact, some defendants and journalists have so read the case.[166]

Sylvania through its economic expert and brief argued for a very broad reading of the rule of reason. The expert took the position that any means by which a marginal competitor can stay in business and offer competition to large producers of substitute goods is reasonable.[167] He explicitly assumed that no economic power could arise for such a marginal competitor because of this restraint.[168] The expert did not identify anything that the retailers were required to do in return for the benefit of the restraint and did not seem concerned about the failure to find this kind of efficiency justification. While not fully explicit, the expert's position appeared to be that restraint serving the function of either cartel or efficiency goals is acceptable because of its desirable dynamic effect on the structure of a generic product market. Sylvania's legal argument followed the expert's position and advanced almost a structuralist agreement of reasonableness: small firms can use restraints for any reason.

There is a danger, however, in reading these items as demonstrating conclusively that a broad rule of reason exists. Neither at trial nor on appeal did Continental develop or argue the issue of the definition of the rule of reason or its application to the facts of the case.[169]

The Court further obscures the standard by its failure to suggest what factors might be relevant to the determination of reasonableness in this case. There is no discussion of the evidence and no guidance to the trial court as to what constitutes a reasonable restraint.

The possible versions of the rule from the opinion thus run the gamut from a rule that makes such restraints generally lawful as an inherent right of the producer, to a rule that allows such restraints for marginal or nondominant firms for any reason but would deny them to large or leading

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[165] This is partially confirmed by a subsequent footnote which asserts that courts can indeed balance intrabrand competitive loss against interbrand gain. *Id.* at n.27.

[166] *See* 39 NAT'L J. 1241 (1977) (report on *Sylvania* substantially misreporting the decision concludes that the opinion makes the conduct lawful). *See also* FTC WATCH, (Aug. 26, 1977) 15-16 (report on briefs in bottlers case which also apparently assert per se lawfulness).

[167] *See* note 115 *supra, quoted at,* Continental T.V., Inc. v. GTE Sylvania, Inc., 537 F.2d 1001 n.36 (9th Cir. 1976). *See also* Preston, *supra* note 31. It should be noted again that Professor Preston reaches this result largely because of his abiding faith in the self righting character of the market.

[168] *See* Joint Appendix, *supra* note 90, at 410-11, 414-15, 421-25. Elsewhere he did acknowledge that some power over some customers might be involved, *e.g., id.* at 440-41.

[169] No effort was made to explore how the expert's judgment could be stated in general rules that would exclude cartels nor did Continental point to the evidence of a lack of efficiency reasons for the restraint and ask that the Court consider the problem associated with allowing such restraints to be held reasonable.

firms, to a rule that permits only those restraints which serve some specific interest related to the efficient production and distribution of goods and which do so without unreasonable restraint. It is clear from the opinion that vertical restraints should not be condemned out of hand and in fact should be permission that the opinion is deficient.

Considered as a matter of policy what rule of reason ought a trial court use? A rule of reason implies reasonableness, but reasonableness in this as in most other contexts is a relative and not absolute term: restraint can be reasonable only in relationship to some objective and then in a comparative sense.

One approach would be to treat the result in this case as declaring that there is an inherent right in a producer to control non-price resale conditions thus limiting the *Dr. Miles* result. If a producer has a general legal right to use controls after it has sold its product, then any exercise of that right is by definition reasonable unless it is objectionable as part of some other wrongful conduct. Such a rule of reason would make controls presumptively lawful in the sales context as they are in the true consignment, agency and employment areas where the nature of the legal relationship mandates such control.

Such an approach would draw support from the analysis in *Schwinn* which upheld as reasonable the controls over the customers and territories in and to which Schwinn's distributors sold under the various agency plans. In the context of the opinion it was fundamental that the actions of the distributors were "indistinguishable in function from agents or salesmen."[170] Moreoever, the overall system of agency and consignment distribution was a legitimate one not involving monopolization so the normal legal rights of such relationships would allow control. Because *Sylvania* held that the passage of title is not "sufficient" to justify a per se rule, it does not follow that all legal rights which exist over agents and employees are necessarily now included in the rights of producers who sell their goods to others. To extend the analysis from situations in which the legal relationship necessarily contemplates control in the principal to contexts where it does not is to alter radically the bundle of rights which the law confers upon a producer. The awarding of such rights raises grave risks of clogging the lines of distribution, thereby erecting barriers to entry and to effective competition, and, of course, increasing costs to consumers for no reason. There seems to be no gain to be had by such a sweeping redefinition of producer rights, and the reasons for objecting to *Schwinn* do not require or even suggest that restraint is a matter of right on its own; it is a right only when needed and only to the extent of that need.

A second approach would ask whether or not Sylvania would, more probably than not, have survived as a viable entity but for this restraint. This assumes implicitly that so long as Sylvania survives, we have achieved a socially desirable goal.[171] But that is not reasonable. One can

[170] United States v. Arnold, Schwinn & Co., 388 U.S. 365, 380 (1967).

[171] This seems to be the test which Sylvania was arguing and which the court of appeals

posit cases where survival is no defense,[172] e.g., Sylvania, to survive, engages in a price fixing conspiracy or customer allocation conspiracy with its competitors. Similarly, if, in order to survive, Sylvania makes dangerous and defective products, refuses to honor its debts, engages in credit manipulation or deception of its customers, its failing condition is no defense. Hence, even this broad rule of reason must concern itself not merely with whether Sylvania survives, but how it does it. One test would be whether the means chosen were or were not "reasonable" (assuming they are shown to be needed, necessary and sufficient) in the sense of whether the level of restriction chosen is socially acceptable. Such a "test" is entirely open ended and logically implies no consistently applicable limitation on conduct. It could uphold the creation of a cartel provided the monopoly profits are reasonable in amount for survival.[173] Under this approach, therefore, either the judge or jury has unbounded discretion to say that something is or is not reasonable conduct.[174] This will be a case-by-case decision and will introduce a very high level of uncertainty into business planning most especially if it is up to the jury to say that the restraint is unreasonable.

A rule of reason so open as to include some, but apparently not all, forms of cartels as well as efficiency justified restraints is too unwieldy to work. Similar cases will be treated differently and vice versa. In practice, the litigation may become largely a matter of seeing how many economists will say a practice in a context is good or bad. A second objection is that any effort to adhere to it will invite mind boggling record making designed to leave no "circumstance of the case" undocumented. A final objection is that the primary implication of this approach is that a restraint need not be justified in efficiency terms. While one could argue that this is acceptable because even if inefficient the restraint has a dynamically useful effect of preserving a competitor, the better view is that all business should be

was prepared to accept.

[172] This defense has been rejected in Socony Vacuum, Inc. v. United States, 310 U.S. 150, 217-18, (1940); Trenton Potteries, Inc. v. United States, 273 U.S. 392, 397 (1927); United States v. Topco Associates, Inc., 405 U.S. 596, 611 (1972). *But see* Appalachian Coals, Inc. v. United States 288 U.S. 344 (1933); National Ass'n Window Glass Mfrs. v. United States, 263 U.S. 403 (1923).

[173] Proof of inefficiency, i.e., that the producer was a high cost, low quality operator which stayed in business only by virtue of its use of restraints which served the cartel interests of its distributors, would not mandate a finding of unreasonableness since an economic expert might say this allowed a marginal competitor to stay in business and it is desirable to have more rather than less producers.

[174] This approach would rely for its legal validity on the formulation of the rule of reason in the *Chicago Board of Trade* case and the restatement therefore in *Sylvania.* It would also require ignoring the line of cases which have limited and qualified this open-ended mandate. *See* Socony-Vacuum, Inc. v. United States, 310 U.S. 150 (1940); Trenton Potteries, Inc. v. United States, 273 U.S. 392 (1927). Justice Brandeis, at least, might have agreed that this is exactly the kind of situation in which a restraint could be upheld on the basis of its ultimate social value. *See* American Column Co. v. United States, 257 U.S. 377, 418 (1921) (Brandeis, J., dissenting) (suggests that even if the facts prove restraint it is "reasonable" because the firms involved are small). However, the size of Sylvania's conglomerate parent might have lead him to an unfavorable outcome.

subjected to the test of the market in free and open competition. A restraint whose only function is to allow exploitation of market power while it may keep a "desirable" producer in the market may equally keep alive a firm which ought to have failed to make room either for expansion by more efficient producers of substitute products or for entry by new producers of such products. To allow producers to survive by use of cartel restraints is to retard greatly the market place test of their actual merit. For these reasons, this approach ought to be rejected.[175]

Finally, an approach could focus on how the restraint operates and require that 1) the restraint have an efficiency explanation and not a cartel one and that 2) it be no more restrictive than reasonably necessary for that efficiency purpose.[176] Courts could protect efficiency justified restraints on the ground that efficiency is itself a primary antitrust goal and reject categorically restraints whose only justification is that they generate enough market power to make possible the survival of the perpetrators. This formula still involves complex factual analysis and a series of subjective judgments, but by starting with the problem of characterization which identifies broad classes of favored and disfavored restraints and then setting a general mechanism for assessing the reasonableness of those which are favored, it creates a viable analytic framework.

This approach is the better policy choice because it minimizes the amount of interferences in the economy that will be allowed. Only when a restraint serves a valid interest of one of the parties and is the efficient way to serve that interest is it reasonable. This would seem an approach most consistent with a general policy of promoting economic competition while still recognizing a public interest in efficiency. Its great virtue is that it provides a way to balance these considerations which also defines what

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[175] The recent ABA monograph on vertical restraints demonstrates, apparently unintentionally, the problems with this broad formulation. The authors, while using the formulation, offered next, as a basic guide, seek to find and define what else *Chicago Board of Trade* permits. The resulting verbal and underlying intellectual swamp reveals the pitfalls and dangers of trying in a legal context to expand the coverage of the rule of reason beyond the *Addyston Pipe* formulation. ABA ANTITRUST SECTION, MONOGRAPH No. 2, VERTICAL RESTRICTIONS LIMITING INTRA-BRAND COMPETITION 53-70 (1977).

[176] This approach which has common law roots has its original Sherman Act articulation in the *Addyston Pipe* case in which Chief Justice Taft distinguished naked (cartel) and ancillary (efficiency) restraints and argued that it was impossible to make consistent judgements about the merits of restraint whose only function was to restrain. United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1898), *aff'd,* 175 U.S. 211 (1899). Bork has argued that this is the understanding that Chief Justice White had arrived at by the time he wrote the *Standard Oil* and *American Tobacco* opinions. Bork I, *supra* note 15. Certainly Hughes' opinion in *Dr. Miles* is consistent with this approach. Moreover, the facts in *Chicago Board of Trade* are also consistent with this approach for the restraint could be regarded as ancillary to the operation of the commodity exchange. Indeed, when defendants charged with naked restraints sought to raise reasonableness issues after *Chicago Board of Trade* the Court distinguished the case on those grounds and reiterated its objection to trying to assess naked restraints or cartels for their reasonableness. *E.g.,* Socony Vacuum, Inc. v. United States, 310 U.S. 150 (1940); Trenton Potteries, Inc. v. United States, 273 U.S. 392 (1927).

circumstances are relevant and how they should be evaluated.[177] As a matter of sound policy then, *Sylvania* ought to be read to mandate this substantive approach to the rule of reason, but it is manifest that nothing in the opinion compels this conclusion and some aspects of it clearly point in other directions.

Closely related to the substantive definition of the rule of reason is the procedural problem of which side has what burden of proof. This includes the burden of final persuasion, the burden of pleading an issue, and the burden of offering some proof on the point. A plaintiff to survive at all in antitrust litigation must plead, offer evidence of and ultimately persuade the court of existence of the restraint. The issue of reasonableness can be an affirmative defense or an element in the plaintiff's case.

The matter need not be so absolute. In assigning procedural obligations courts should regard the problem pragmatically bearing in mind that as a party is forced to bear more of the burdens, its chances of winning in a close case are reduced. In assigning these burdens the courts ought to be concerned with finding a proper balance between the social interests in competition and in those restraints which the courts are to judge under the rule of reason. Courts also ought to be very concerned with the potential for open ended discovery and litigation that a rule of reason might call for and so, in the interest of judicial economy, try to structure the inquiry to avoid non-specific proceedings. Finally, proof of a negative, in the abstract, e.g. unreasonableness without reference to a claim of why conduct is reasonable, is well nigh impossible.

One way to strike the balance is to require the party defending a restraint to plead any asserted basis for reasonableness with sufficient specificity that the factual basis for and legal theory of reasonableness are explicitly set forth.[178] The defender should also be required to go forward with the evidence in support of its theory of reasonableness. Only if its prima facie case is adequate in law and fact should the inquiry proceed. If the

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[177] This approach does not mandate that all efficiency justified restraints be accepted. Chief Justice Taft himself indicated that the risk of monopoly would justify rejecting even an apparently efficient restraint. United States v. Addyston Pipe & Steel Co. 85 F. at 291. BORK I, *supra* note 15, would presumably disagree. Any such rejection does raise risks of ad hoc decision-making of the same kind as that found in the second approach to the rule of reason. But where the courts define a general class of restraint to be rejected without regard to its efficiency justification, they have fashioned a rule to its efficiency justification, they have fashioned a rule which avoids the ad hoc quality even if it has an arbitrary effect. The so-called "per se" rules in *Topco, Schwinn, Albrecht* and the tying cases discussed later are of this character. This analysis is developed in Carstensen, *supra* note 19, at 831-38. Such per se rules have explicit exceptions and as *Sylvania* shows can be repealed in part without necessarily requiring rejection of other similar rules. This is forcefully indicated by the explicit reaffirmance in *Sylvania,* 97 S. Ct. at 2558 n.18, of the general ban on resale price fixing which has similar redeeming qualities to other resale controls. *Id.* at 2566-68 (White, J., concurring).

[178] Such pleading could possibly be done while also denying the existence of a restraint. It is likely that a defender would be forced to elect its theory because a reasonableness claim implies some explicit specification of the how and why of the restraint.

first approach to the rule of reason is adopted, the defender will prevail in most cases despite any pleading burden while if the second approach is employed the defender will also have a fairly easy time, but at least some ad hoc guidance will be present as to what circumstances will make restraints permissible. If the third approach is followed, defenders will have a more difficult, more rigorously defined task and more cases should be resolvable at this stage.

Once a prima facie case is made out, the challenger has the option of disputing either the characterization of the restraint as efficiency related or, conceding the general character, the reasonableness of the specific restraint given its purported function. Once again some obligation of explicitness at the pleading and motion stage as to what the nature of the challenger's case will facilitate the avoidance of excessive litigation and focus the inquiry on fewer factual issues.

Nevertheless, the probability is that there will be substantial uncertainty in many cases about the general characterization or the specific reasonableness of practices or both, and so the allocation of the ultimate burden of persuasion may well be significant both in cutting off access to the jury and in guiding the jury's decision. The effect of placing persuasion upon the defender of a restraint is that such a party, if counseled in advance, may be likely to be very cautious in employing any restraint. This may be undesirable because, given the risks, restraint will be likely to be employed in suboptimal ways thus denying the public the advantages of reasonable restraints. At trial if close questions can be resolved against the party defending a prima facie reasonable restraint, it is likely that a number of reasonable restraints will be held unlawful. Conversely if the challenger has the persuasion burden, any challenge to arguably reasonable restraints is discouraged since the prospects of success will be reduced. A possible result is that many unjustified restraints would escape challenge and the totality of restraint on economic activity could exceed the level intended by the rule of reason. This problem is greater under the second and third approaches to the rule of reason both of which involve a weighing of competing considerations. It is clearly greatest under the second because of the lack of any explicit way to weigh or relate the competing values.

No easy solution suggests itself, but if the defender has a significant burden both in pleading and in producing evidence of a prima facie case, the courts can fairly conclude that the restraint in issue is within the ballpark of arguable reasonableness so that it is probably the better course to insist that the attacker carry the burden of persuasion.

As applied to the record in *Sylvania*, it is not at all clear that if the court imposes any requirements of pleading or proof on Sylvania that it can meet them unless the first approach is used. Its legal theory of reasonableness is very sweeping and does not provide a definition of reasonable and unreasonable restraints, or otherwise identify a reasonableness criterion in the rule of reason except perhaps in terms of a right of the producer. Moreover, there is no articulated theory connecting the restraint with the outcome. By addressing this causal issue, which is relevant to either the second or third approaches, in terms more logical than *post hoc ergo propter hoc* Sylvania would have to identify the connection it believed existed between restraint and survival and so by implication state something about the functions which a permissible restraint could serve. Since it is not clear that Sylvania's managers or expert knew how the restraint might have functioned to save the company, this may be the end of the case. More likely, Sylvania would focus on the efficiency arguments and thus create factual issues of characterization and reasonableness, both of which are highly ambiguous on this record.[179]

4. *The Rule of Reason Reconsidered*

The Court has embraced the rule of reason as the appropriate standard for judging the validity of non-price vertical restraints. This has already resulted in the reversal of other decisions[180] and the opening up of many cases to potentially prolonged litigation. Given the functional similarity between price and non-price, vertical and horizontal restraints, and the unsatisfying nature of the Court's distinctions among them, the present limitation to vertical, non-price restraints may be only temporary. But if the trend of the past four decades towards relatively absolute rules in antitrust is to be reversed and some more open inquiry substituted in most cases, the Court has the obligation of clarifying and explicating what this new standard is. The majority conspicuously failed to do this in *Sylvania* where it had a record before it from which it might have formulated some factual and legal guidelines for the lower courts.

The history of the rule of reason in the Supreme Court is one of a tension between the open-ended Brandeis version which may connote a willingness to weigh any restraint against any possible benefit, and the Taft version which would limit the application of the rule to cases in which it is claimed that the restraint is ancillarly to some other specific, efficiency producing activity. As a historical matter, the Taft formulation has been dominant, albeit implicitly, in the actual application of the rule of reason, especially in conduct type cases, even while the Brandeis formulation is more frequently quoted. Moreover there has been little or no development or informative applications of the rule. Thus for Justice Powell to act as if all knew exactly what was meant by the rule of reason, is a kind of practical joke on the judiciary which is likely to backfire in most unfunny ways on the Supreme Court itself.

Two other problems with the rule of reason merit noting. The first is

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[179] Sylvania may also have to justify its specific conduct both excluding Continental from Sacramento, since the evidence was that no adverse effect was likely even if they did enter, and in causing the closing, temporarily, of Continental's entire group of stores which might seem a more drastic response than was reasonable in the context. A rigorous analysis ought to include a concern with the reasonableness of specific applications of a restraint as well as for its overall justification.

[180] McClatchy Newspapers v. Noble, 97 S. Ct. 2966 (1977) (per curiam); Adoplh Coors & Co. v. A & S Wholesalers, Inc. 1977-2 TRADE CAS. (CCH) ¶ 61, 565 (10th Cir. 1977).

the role of less restrictive alternative doctrine. Both the second and third approaches to the rule of reason have within them by implication a least restrictive alternative requirement.[181] Whether we are inquiring as to the connection between the restraint and the survival of the restraining firm or between the restraint and some efficient conduct it has made possible, the evidence must show that the restraint is needed, necessary and sufficient. If another, lesser restraint could reasonably be expected to have done the same job, then the restraint, while needed and sufficient, was not necessary and so not reasonable if we assume, as the Sherman Act would seem to require, that competition is a value which Congress wishes to have maximized.[182]

Although the Supreme Court has never explicitly held that a least restrictive alternative is all that is allowed in a conduct case, it has so held in a related context. In the bank merger field it is a defense to a merger otherwise illegal that it is needed to serve some convenience and need of the community. If service to such a convenience and need exists, then it must be balanced against the competitive effect. To date no case has required that weighing because the Court has held that there was no benefit to convenience and needs unless the least restrictive approach was taken.[183] So, unless the parties demonstrated that methods other than merger would not suffice to achieve this beneficial goal, they could not assert that the merger was convenient and necessary. The justification for this conclusion was that the Court did not want to sacrifice competition needlessly—even in banking.[184] This holding would suggest that to be consistent with a national policy in favor of competition, any formulation of the rule of reason must concern itself with the problem of compelling parties to minimize their restraints on competition.

The counter argument[185] is that lawfulness ought not to turn entirely on the imagination of subsequent litigators in coming up with less restrictive alternatives. Such a situation will be likely to discourage the use of restraints which are socially desirable. It is therefore suggested that any reasonably necessary restraint should be upheld.

The distinction may be largely a semantic one.[186] To be justified as

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[181] The first (property right) approach would not necessarily require a least restrictive alternative test because it has already assumed that this is a right that ought to be the producer's and one can define that right in whatever terms are consistent with the scope of rights conferred.

[182] To the contrary is American Motor Inns, Inc. v. Holiday Inns, Inc., 521 F.2d 1230, 1249 (3rd Cir. 1975). Some slight support for this view is given in *Sylvania* where the restraints were characterized as "neither the least nor most restrictive provision," 97 S. Ct. at 2562 n.29. In context, the discussion was addressing the usefulness of a per se rule for such a type of restraint.

[183] United States v. Third Nat'l Bank, 390 U.S. 171 (1968).

[184] *Id.* at 189-92.

[185] E.g., Handler, *Twenty-Five Years of Antitrust (25th Annual Antitrust Review)*, 73 COLUM. L. REV. 415 (1973).

[186] Any test of less restrictive alternative must contemplate an examination of the facts at a particular point in time and ask for no more than what a reasonable business person in

"reasonably necessary," assuming that it is agreed that restraint beyond the minimum required is affirmatively undesirable, a restraint must be demonstrated to be no more than needed to serve whatever permitted goal it has, i.e., that it was the least restrictive option available at the time. Whether one puts test in terms of "least restrictive" or no more than "reasonably necessary" so long as there is agreement on the relative relation of restraint and competition, the same fundamental proposition is stated.[187]

Finally there is a damage issue: when a party establishes only that a restraint was unnecessarily restrictive, ought that party then be entitled to damages ipso facto or must it also demonstrate that its damages would not have occurred under the alternative, reasonable restraint which it has proven.[188] This is a manifestation of broader problems of causation and proximate causation which are now arising in private damage cases. The general issues will be discussed subsequently. For present purposes it may suffice to note that the choice of a damage rule will greatly affect incentives to challenge provably unreasonable restraints. Thus while the choices are clear, which is the better one is not obvious.

B. *Tying:* Fortner II *and the Proof of Market Power*

1. *A Business Analysis of Tying*

Tying, the conditioning of the sale of one product on the buyer agreeing to buy some other product is an example of an internal restraint.[189] It operates to define the relationship between the parties and by doing so also circumscribes the freedom of action of at least one of the parties with respect to its dealings with competitors of the other party.

Unlike external restraints where usefulness necessarily requires that the product or service involved possess some market power, no comparable condition is necessary for tying to occur. It can make business sense for a seller to offer something extra to the buyer to make a sale. Such situations may be thought of as package deals. Such combinations are especially

the position of the parties would regard as the least restrictive alternative consistent with the achievement of the permitted goal.

[187] As a matter of procedure if a challenger wishes to challenge a restraint on this ground, it seems clear that, assigning to such a challenger, the burdens of pleading, proving, and persuading that such an alternative exists will also serve to redress the balance and insure that mere imagination in pleading will not suffice to invalidate retroactively an otherwise not unreasonable restraint.

[188] This is illustrated by the informed consent cases. *Compare* Cantebury v. Spence, 464 F.2d 277, 290-91 (D.C. Cir), *cert. denied,* 409 U.S. 1009 (1972) (lack of informed consent to operation gives rise to no liability if a reasonable person in plaintiff's position would have consented) *with* Reyes v. Wyeth Laboratories, 498 F.2d 1264, 1281 (5th Cir.), *cert. denied,* 419 U.S. 1096 (1974) (failure to give warning presumed to have causal connection to injury and proof that warning would not have affected decision held irrelevant).

[189] Reciprocity, requirements contracts, exclusive dealing, and full line forcing agreements are other examples. *See* Comment, *Franchises, Requirements Contracts and Tie-Ins: One Test for a Tangled Two,* 74 YALE L. J. 691 (1965).

useful when a seller confronts buyers with special needs. By assembling a package for the buyer whether it is flour and sugar or houses and financing, the seller may be giving more value than the equivalent price cut on the primary object of sale. Indeed package deals are a variant on the traditional price cut and represent alternative ways in which an equivalent discount can be offered. In such situations the tied product is the significant object from the seller's perspective and the tying product is relevant only in its role as the equivalent of a price cut. While such a seller would be willing to sell the tied product by itself, it would probably not be willing to part with the tying product alone except for at least its full market value.

Without further information to show why or how a package sale is likely to have an adverse effect on some market,[190] no one is likely to believe that such conduct is unreasonable or anticompetitive. By hypothesis all other sellers could offer the same package at the same price, and other sellers can also offer the products separately; hence the buyer has had full freedom of choice and made a choice in this context on the basis that the package gives more value than a cash discount.[191]

Tying can also, probably with greater frequency, represent an exercise of market power. For a variety of reasons, the seller of a relatively unique good or service may wish to employ its power over that good by requiring buyers to take some other product or service. A business analysis of these requirements suggests that they can function to serve a range of goals from direct profit maximization by achieving price discrimination, to protection of quality or good will, to transference of economic power from one product line to another.[192] The tying seller, using market power will, like a package seller, not sell the tying product alone, except at a very high price, although it will probably sell the tied product separately.

There is a substantial basis to object to tying based on market power. Such tying is generally said to cause two kinds of injury. First it is an abuse of the market power of the seller which unfairly exploits the buyers need for the tying product.[193] Second, it is unfair to competitors in the sale of

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[190] This analysis may seem to conflict with the relatively absolute ban on tying contained in § 3 of Clayton Act. However, that ban can be invoked— only when the conduct at issue "may substantially tend to lessen competition." This condition will always occur in some degree when tying involves use of market power. The use of a "quantitative substantially" test with low thresholds for liability may make some sense then, but it will not in the context of fungible products where no market power is being exploited although generally such conduct, too, may tend to "lessen competition." *Compare* United States v. Standard Oil Co., 337 U.S. 293, 302-14 (1949) *with* Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 320, 329-35 (1961). *See also* Bok, *The Tampa Electric Case and the Problem of Exclusive Arrangements Under the Clayton Act,* 1961 SUP. CT. REV. 267.

[191] *See* Areeda, *Antitrust Violations Without Damage Recoveries,* 89 HARV. L. REV. 1127 (1976) [hereinafter cited as Areeda].

[192] F. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE 506-07 (1970).

[193] United States v. Loew's Inc., 371 U.S. 38, 44-45 (1962); Northern Pacific Ry. v. United States, 356 U.S. 1, 6 (1968); IBM Corp. v. United States, 298 U.S. 131, 135 (1936); *see also* Times—Picayune Pub. Co. v. United States, 345 U.S. 594, 605 (1953).

the tied product since some portion of the market is foreclosed to them not because of the superior virtue of the successful seller but because of the power of that seller with respect to some other product or service.[194] It is thus clear that the objection to tying rests on an assumption of market power, and so proof of the validity of that assumption in a particular case is a very central issue in any tying litigation. It is especially critical that the threshold of what will be regarded as power be defined so that it is clear when a seller has crossed that line. This is not an easy task to perform. The observable characteristics of the tie and the conduct of the parties will not provide unambiguous evidence. One needs to know something of the market characteristics in which the tying good is sold. As the evidence points toward uniqueness either of the product itself or cost advantages in its production one can be relatively confident that the producer has some power in its sale. This power is not necessarily large nor is it necessarily equally applicable to all buyers.

Although traditionally characterized as "unfair," many uses of tying, even where market power is present, are easily explicable in terms of the same kind of efficiency arguments used to justify external (vertical) restraints earlier. In one class of tying arrangements, the tie is explicable in terms of its utility in protecting some aspect of the tying product either its productivity or its good will. Examples include cases in which the tie is arguably necessary in order to assure that proper inputs (the tied product) are used in a machine (the tying product),[195] or that the equipment purchased (the tying product) is properly installed (the tied service)[196] or that the producer's good will not be jeopardized by use of improper or nonconforming parts or attachments.[197]

The profit maximizing goal is also consistent with efficiency if we assume that a seller has a right not only to discriminate among buyers but also to use functionally equivalent methods which are more efficient to achieve the same result. If one with market power has a right to the maximum "monopoly" profit that this power will yield through any means, then a tie can be but an efficient way of exercising that right.[198] The

[194] United States v. Loew's Inc., 371 U.S. 38 (1962); Northern Pac. Ry. v. United States, 356 U.S. 1, 6 (1968); International Salt Co. v. United States, 332 U.S. 392, 396 (1947).

[195] *See, e.g.,* International Salt v. United States, 332 U.S. 392 (1947); IBM Corp. v. United States, 298 U.S. 131 (1936); Siegel v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971), *cert. denied,* 405 U.S. 955 (1972).

[196] *See, e.g.,* United States v. Jerrold Electronics Corp., 187 F. Supp. 545 (E.D. Pa. 1960), *aff'd per curiam,* 365 U.S. 567 (1961).

[197] *See, e.g.,* Dehydrating Process Co. v. A.O. Smith Corp., 292 F.2d 653 (1st Cir.), *cert. denied,* 368 U.S. 931 (1961); Pick Mfg. Co. v. General Motors Corp., 80 F.2d 641 (7th Cir. 1935), *aff'd,* 299 U.S. 3 (1936).

[198] This is probably the better explanation for the ties found in the cases cited in note 194. *See also* United States v. Loew's Inc. 371 U.S. 38, 49 (1962) and Northern Pacific Ry. v. United States 356 U.S. 1, 8 (1958) (by discounting the price of land sold to buyers agreeing to ship on defendant's railroad, the railroad secured added business not otherwise available).

The basic theory behind this analysis is that by using a tied product whose volume of purchase or price can be varied with the buyers demand or need for the tying product, buyers determination of whether there ought to be a right to maximize monopoly profits, assuming the monopoly is itself otherwise lawful, represents a policy judgment not only of economic[199] but of social and political character[200] as well.

Other uses of tying are more clearly like those which fall under the cartel analysis with respect to external restraints. The classic case is where a producer uses its power in one area to foreclose competition in another only for the sake of that end. This is purely anticompetitive in the usual case. It involves a refusal to compete on terms that can be met directly by others in that market.[201]

At the very least then some uses of tying based on market power are arguably ancillary to achieving efficiency, but depending on the definition of rights of a seller with market power, more or less of the uses of tying are analogous to a cartel-like exploitation of power for its own sake. There is thus a strong parallelism between the logical analysis of external restraints and tying based on market power.

2. *The Legal Analysis of Tying Prior to* Fortner II

The judicial treatment of tying prior to *Fortner II* has been a consistent and vigorous condemnation. The courts have refused to accept any argument that producers have a right to maximize profit by the use of a tie-

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will pay varied prices for the tying product and the seller will run no risk of cross sales (a low price buyer reselling to one with a high price) and the prices paid will reflect relative demand.

[199] The economic argument would focus on the benefits. Will a seller produce more if it can exercise this right? If it will, then the right is socially productive from an economic view point.

The conclusion turns out to be more ambiguous than might seem to be the case. Depending on the amount demanded at various degrees of need we may find more or the same production under discrimination as under uniform price. *See* Bowman, *Tying Arrangements and the Leverage Problem,* 67 YALE L. J. 19 (1957) [hereinafter cited as Bowman]; Stigler, *United States v. Loew's Inc.: A Note on Block-Booking,* 1963 SUP. CT. REV. 152.

It is worth passing notice that the economist would differentiate this case from that of a cartel on the basis that here there is a single integrated producer which will produce more or less depending on its total profit whereas the cartel will produce less than its participants would otherwise because they have created collectively market power and employed it to suppress production. So long as the power of the tying product is assumed to be "natural" or "inherent" the cases look and are dissimilar. But if the legal system consciously chooses to allow product differentiations, then one may wish to question the propriety of the underlying market power that gives rise to the capacity to tie. Demsetz, *Two Systems of Belief about Monopoly,* in INDUSTRIAL CONCENTRATION, THE NEW LEARNING 164, 200 (GOLDSCHMID, MANN & WESTON eds. 1974).

[200] The social and political arguments are cast largely in terms of fairness. Is it right or proper to allow either unequal treatment of buyers taking similar goods or foreclosure of selling opportunities to competitors in the tied product especially where the foreclosure is something which is unrelated to the merits of the product sold? The argument seems to imply a sort of cost benefit analysis which would weigh the loss to a sense of fairness against the economic costs which a "fair" rule was likely to generate. *See* Northern Pacific Ry. v. United States, 356 U.S. 1, 6, 11-12 (1958).

[201] It may not always be objectionable because in some cases it may be an entry device useful for a small firm seeking to gain entry into a market where the structure is very oligopolistic. *See* Pearsall Butter Co. v. ETC, 292 F. 720, 722-23 (7th Cir. 1923).

in[202] and have explicitly rejected the argument that efficiency considerations will in general justify tie-ins.[203] The oft expressed view is that almost any need a tie-in might serve can be served as well by some other requirement which does not involve trespassing on the rights of other producers of the tied product.[204] Although the Court has sometimes put its views in terms of the predatory implications of the usurpation of the market for the tied product, it is farily evident that the real basis for condemnation is the conclusion, reinforced by the Clayton Act and the Robinson Patman Act, that it is unfair to both customers and competitors to allow market power to be exploited in this way.[205] A crucial factor premise underlying this outcome is the belief that in most cases the seller has alternatives which are not substantially less efficient to achieve any legitimate ends that may exists.[206]

The resulting condemnation is a "per se" rule with exceptions. The exceptions relate either to the character of the tying firm,[207] (if it is a new or failing firm, it may use tying in reasonable ways to protect its efficiency interests) or to impelling circumstances which make a tie not only efficient but the only practical method of protecting some legitimate interest of the seller.[208] This kind of a per se rule is exactly parallel to that found in *Topco, Schwinn* and *Albrecht* and quite different from the per se rule found in *Socony-Vacuum* and similar cartel cases. Moreover its justification is the protection of independent businesses which is the rationale for the "per se" prohibitions announced in the first line of cases.

There are four elements that a plaintiff must demonstrate in a Sherman Act tying case:

1. That two distinct products are involved.
2. That the sale of one is tied to the purchase of the other.
3. That the tying product has some market power.
4. That not an insubstantial amount of commerce is affected.

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[202] *See* cases cited in notes 199 & 195 *supra.*

[203] *See* cases cited in note 195 *supra.*

[204] *See* Northern Pac. Ry. v. United States, 356 U.S. at 6 n.5.

[205] There is no reason to think the Court is willfully refusing to see the economic argument. It has instead, to date, found the potential marginal gain in efficiency not to be worth the probable social cost in terms of reduced fairness to buyers and competitors. *Compare* Turner, *The Validity of Tying Arrangements Under the Antitrust Laws,* 72 HARV. L. REV. 50 (1958) *with* Bowman, *supra* note 199; Markovits, *Tie-Ins, Reciprocity and the Leverage Theory,* 76 YALE L. J. 1397 (1967); and 80 YALE L. J. 195 (1970).

[206] Thus the franchisor in Siegal v. Chicken Delight, Inc., 498 F.2d 43 (9th Cir. 1971), can take a percent of the revenue of the franchisee. The IBM company can lease computers based on usage, *but see* United States v. United Shoe Machinery Corp., 110 F. Supp. 295, 352 (D. Mass. 1953), *aff'd per curiam,* 347 U.S. 521 (1954).

[207] Pearsall Butter Co. v. F.T.C., 292 F. 720 (7th Cir. 1923). *See also* Siegal v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971); United States v. Jerrold Electronics Corp., 187 F. Supp. 545 (E.D. Pa. 1960), *aff'd per curiam,* 365 U.S. 567 (1961).

[208] Dehydrating Process Co. v. A.O. Smith Corp., 292 F.2d 653 (1st Cir.), *cert. denied,* 368 U.S. 931 (1961); Pick Mfg. Co. v. General Motors Corp., 80 F.2d 641 (7th Cir. 1935), *aff'd,* 299 U.S. 3 (1936).

The proof of these four elements makes out a case to which no general rule of reason defense is possible although a defendant may still offer selective defenses as discussed previously.

The first and last requirements are relatively clear. The two product requirement is essential to the entire theory of a tying case because without two products there can be no tie. The problems produced in application of this standard are matters of factual characterization which, while difficult in some cases, raise few serious problems of factual or legal conceptualization.[209] Similarly while some tying may be so de minimus as not to merit judicial action, exactly what that minimal amount is, is not yet clear.[210]

The second element would seem similarly obvious: The sale of one product must be conditioned on the buyer taking the other product. Despite the apparent clarity of the idea, recent decisions in the lower courts reflect a confusion between conditioning of sales and some vague notion of "coercion".[211] Antitrust law regularly gets into trouble when its practitioners use colorful terms whose meanings are not clear. Since tying involves economic relationships, no coercion in a "godfather" sense[212] is likely to occur. A business will not spend more for the bundle of tied goods or services that they are worth in total; as a result, it is simply not accurate to describe the business as being "coerced" if what is meant is conduct that is economically irrational.[213] If by coercion the courts merely mean an action which the actor would not have taken but for the insistence of another party, then the mere fact of charging a price for goods is an act of coercion and the concept again has become meaningless.

What the coercion misnomer reflects is a muddling of the question of when a combination sale is in fact conditioned with the question of whether a tied sale involves the use of market power (hence coercion in some sense) or not.[214] The issues ought to be kept separate.[215]

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[209] A good discussion of the issues is found in Ross, *The Single Product Issue in Antitrust Tying: A Functional Approach,* 23 EMORY L. REV. 963 (1974).

[210] In *Fortner I,* the Court was quite explicit about the low threshold required to get over the de minimis level. Fortner Enterprises Inc. v. United States Steel Corp., 394 U.S. 495, 501-02 (1969).

[211] Ungar v. Dunkin Donuts of America, Inc., 531 F.2d 1211 (3rd Cir.), *cert denied,* 429 U.S. 823 (1976); this requirement was interpreted as merely calling for proof of a tie-in requirement in Bogosian v. Gulf Oil Corp. 1977-2 TRADE CAS. (CCH) ¶61, 568 at 72, 299 (3rd Cir. 1977) and in that later opinion the other circuit court opinions were read as being in accord with this view: Response of Carolina, Inc. v. Leasco Response, Inc., 537 F.2d 1307 (5th Cir. 1976); Davis v. Marathon Oil Co. 528 F.2d 395 (5th Cir.), *cert. denied,* 429 U.S. 823 (1976); Belliston v. Texaco, Inc. 455 F.2d 175 (10th Cir.), *cert. denied,* 408 U.S. 928 (1972); American Mfrs. Mutual Ins. Co. v. American Broadcasting-Paramount Theatres, Inc. 446 F.2d 1131 (2nd Cir. 1971), *cert. denied,* 404 U.S. 1063 (1972).

[212] "I made him an offer he couldn't refuse." *The Godfather,* Part I.

[213] Professor Areeda has demonstrated that a clever and quite logical argument can be made that no damages ever accrue to the victim of a tie-in since, ex hypothesis, he got a value that he was satisfied with because he agreed to the tie. Areeda, *supra* note 191.

[214] Varner's defense of the coercion requirement more than adequately illustrates this confusion. Varner, Voluntary Ties and the Sherman Act, 50 S. CAL. L. REV. 271 (1977).

The greatest source of difficulty is the definition and test of market power. Since the basic objective of the per se prohibition is to deal with the unfairness of tying, the prohibition need only apply when it is a game that one and not many can play. Hence the package sale not accompanied by market power does not involve the kind of competitive unfairness that the per se prohibition has as its concern. The key question is what power will trigger the rule.[216] There is a clear line of development of the market power analysis in tying which culminated in *Fortner I*.[217] The trend was to reject consistently any requirement of proof of the kind of power such that its possessor might risk a monopolization charge;[218] but even *Fortner I* did not dispense with a requirement of proof of some market power[219] although it did hint that the showing of extensive sales under tying conditions might satisfy the requirement. Moreover the Court has always adhered to the idea that the power must be general in some degree and not limited to a single relational context.[220] Relational power arises in any contractual context in which one party has the legal right to insist on some future conduct or performance. If the entry into such a contract did not involve the exercise of market power, then subsequent insistence on adherence to the contract, while an exercise of relational power, would not involve an exercise of market power.[221]

The return of the *Fortner* case provided the new majority with an

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[215] The first question is whether the sale of one good was in fact made dependent on the buyer taking some other good. In cases where the tying good was ostensibly offered separately, the relevant tests are whether that is true and whether the tied purchase was significantly better than any other transaction possible. If there was no separate sale or such sale was economically irrational conduct for a buyer, there is a tie-in sale; but, of course, if the reason for a lower combination price is some economy of joint production or sale, then the tie-in will not reflect the use of market power and so will not be objectionable but on other grounds. Ungar v. Dunkin Donuts, Inc. 531 F.2d 1211 (3rd Cir.), *cert. denied,* 429 U.S. 823 (1976) for example turned on the issue of whether sales of products were in fact tied to the sale of the franchise and would have been far easier to understand if the opinion had focused on that issue explicitly instead of rambling on about coercion.

[216] Sufficient power can come from a patent, e.g., International Salt Co. v. United States, 332 U.S. 392 (1947); a popular product, e.g., IBM Corp. v. United States, 298 U.S. 131 (1936); land ownership, e.g., Northern Pacific Ry. v. United States, 356 U.S. 1 (1958); or copyright, e.g., United States v. Loew's Inc., 371 U.S. 38 (1962).

[217] Fortner Enterprises v. United States Steel Corp., 394 U.S. 495 (1969).

[218] The line starts with some oblique language in *International Salt,* 332 U.S. at 396, which seems to call for substantial market power absent a patent or other presumptive source of power, *see also* Times-Picayune Publishing Co. v. United States, 345 U.S. 594, 608-09 (1953), moves to a weaker standard in *Northern Pacific,* 356 U.S. at 5-7, and culminates in *Loew's,* 371 U.S. at 45, and *Fortner I's,* 394 U.S. at 499, 506, requirement of a sufficient uniqueness to a good or service that it is able to attract buyers.

[219] The opinion in *Fortner I* called for a showing that "the seller has the power to raise prices, or impose other burdensome terms . . . ," 394 U.S. at 504.

[220] *See,* Bohling, *Franchise Terminations Under the Sherman Act: Populism and Relational Power,* 53 TEX. L. REV. 1180 (1975).

[221] The "coercion" element may also address this issue by trying to insist that the proper focus is the time of agreeing and the state of the parties' power then and not in the post agreement period.

opportunity to reconsider the law on tying. Most particularly the case presented the issue of what evidence could be said to prove objectionable market power.

3. Fortner II

In the late 1950's, Fortner was a builder and developer of single family homes in the Louisville area with a farily thin financial position. He held an option on some land which he wished to develop with relatively low cost housing. At this time U.S. Steel's not very successful prefabricated homes business was looking for additional outlets for its product. After some negotiation, Fortner and U.S. Steel agreed that U.S. Steel Credit Corporation, a subsidiary of U.S. Steel engaged in financing U.S. Steel sales and related activity, would loan Fortner all the funds necessary to finance the entire project;[222] in return Fortner agreed to buy U.S. Steel prefabricated homes.[223] The contract explicitly conditioned the loan on the buying of the houses. After assembling some of these houses and finding that they were not satisfactory, Fortner sought to be released from that requirement; U.S. Steel refused; and subsequently the Credit Corporation started a foreclosure action on the project. Fortner counter-claimed charging an attemt to monopolize, unreasonable restraint of trade and tying.

Initially, the district court dismissed Fortner's tying claims before trial finding that no substantial amount of commerce was involved and that there was no evidence of market power.[224] The Supreme Court reversed.[225] It found that substantial commerce was indeed involved. The more important aspect of the opinion dealt with whether or not there was sufficient evidence of market power to defeat a motion to dismiss before trial. The Court found, primarily in the affidavit of one mortgage banker and in the tie itself, sufficient evidence of the probability of market power that a factual issue was created such that trial was warranted.[226] The case finally came to trial before the judge sitting without jury. The judge made findings of fact which concluded that U.S. Steel had market power as a matter of fact with respect to financing, and this made the conceded tie unlawful.[227] The Court of Appeals affirmed.[228] It bears noting here that the trial

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[222] In addition to financing the cost of the houses themselves, this project needed financing to cover the cost of land acquisition and development (i.e., sewers and water lines, sidewalks, streets, etc.).

[223] The homes themselves amounted to about one third of the total financing.

[224] Fornter Enterprises, Inc. v. U.S. Steel Corp. 293 F. Supp. 762, 768-69 (W. D. Ky. 1966), *aff'd per curiam,* 404 F.2d 936 (6th Cir. 1968), *rev'd,* 394 U.S. 495 (1969).

[225] Fortner Enterprises, Inc. v. U.S. Steel Corp. 394 U.S. 495 (1969).

[226] *Id.* at 504-05. Although the opinion is fairly explicit on this point, the district court judge nevertheless concluded that Fortner was entitled to summary judgment, but the circuit court rejected this conclusion. Fortner Enterprises, Inc. v. U.S. Steel Corp., 452 F.2d 1095 (6th Cir. 1971), *cert. denied,* 406 U.S. 919 (1972).

[227] This decision was not reported.

[228] Fortner Enterprises, Inc. v. United States Steel Corp., 523 F.2d 961 (6th Cir. 1975), *rev'd,* 429 U.S. 610 (1977).

judge and court of appeals were clearly responding to the "music" of the original *Fortner* judgement and not just its words. This music was in the tradition of bigness is badness, and any apparently wrongful conduct by a big firm is probably illegal. As a more technical legal matter the courts sought to use the fact of a tying agreement together with its substantial use[229] as some evidence of market power. The high cost of U.S. Steel's houses, was also said to indicate something about market power. However, while emphasizing that U.S. Steel's loan was in fact unique and was not imitated by other lenders at that time, the Court of Appeals, at least, concluded that there was no evidence that other lenders could not have made similar loans or that U.S. Steel had a cost advantage over such other potential competitors in making such loans.[230]

The problem of what evidentiary implications to draw from the fact of a tie-in is one that several circuits have considered. The most informative discussion is that of Judge Sobeloff in the *SCM* case.[231] He suggests that the market power requirement of *Fortner I* can be satisfied by proof of a tie *not otherwise explained* involving any significant number of buyers. This only shifts the burden of going forward with the evidence to the defendant in a tying case once the plaintiff has shown that a tie exists. The question remains whether the plaintiff can rely on that inference once the defendant offers another explanation. That is to say, does the defendant have the persuasion burden as well? This is the basic legal issue that the *Fortner* case presented to the Supreme Court, but in resolving that issue the Court could have elected to reconsider much of tying law.

U.S. Steel argued that it had taken a low price on its money, below what it could have gotten on a comparable loan, in order to obtain the sale of the houses, and that it had no market power in the money market.

In addition to pointing to the number of ties that U.S. Steel employed, Fortner argued that because U.S. Steel charged a low price for its money, it must have had power with respect to money. Fortner sought to buttress this argument by a showing that banks and savings and loan associations were legally barred from making comparable loans. This might tend to establish that other mortgage and construction lenders could not meet this kind of competition regardless of price but only if the significance of these specific types of lenders is established.[232]

A primary element in Fortner's position was the populist theme of big, bad U.S. Steel using its large resources to destroy competition. The fundamental objection to this approach is not that it is a necessarily bad theory

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[229] 523 F.2d at 966-67. The court also alluded to the high cost of U.S. Steel homes.

[230] *Id.* at 966.

[231] Advance Business Systems & Supply Co. v. SCM Corp., 415 F.2d 55 (4th Cir. 1969), *cert. denied*, 397 U.S. 920 (1970).

[232] There appears, however, to have been no analysis of mortgage lending or construction financing in the Louisville area so that there is no structural information about numbers or types of lenders, types of loans made, relative costs of funds to lenders, or the barriers to entry into the market by out-of-area lenders. Without more of this structural information there is no implication of the limits on bank and savings association lending.

but that it is not a theory to be developed in a per se case. It requires a record showing how this kind of competition affects and is likely to affect the business of selling homes as well, perhaps, as the business of financing the construction and development of such homes. Only with such a record can a plaintiff prevail on this kind of theory.[233]

Given, then, that Fortner restricted itself to proving a per se case the issue became whether the record supported the finding of market power, and the burden was on the plaintiff to persuade that the tie represented an exercise of market power. Fortner's own expert and the Court of Appeals both recognized that the rate on the loan to Fortner was substantially below what one would have expected given the facts about the business and the risks involved. It was therefore understandable that he would take the loan and agree to buy the houses. In fact this deal avoided the problems of finding independent financing and so was probably more attractive than a comparable price cut on the houses themselves since that would not have solved the financing problem. The facts are therefore consistent with a pure package deal:[234] U.S. Steel gave Fortner more value by providing cheap financing rather than cheaper houses, and so the financing was the equivalent of a price cut. Moreoever, this deal makes business sense whether or not U.S. Steel has market power with respect to finance.

Fortner's counter arguments failed to rebut this. Although banks and savings and loan associations were legally precluded from offering the same kind of loans, it was clear that at least some other lenders, e.g. mortgage bankers, were not so precluded and it was not established that the legally barred lenders were significant. If, nevertheless, it had been shown that U.S. Steel was in a more favorable position in terms of cost of money than other making construction loans, a different result might have been possible because then U.S. Steel's position with respect to a class of borrower (construction loan borrowers) would have continued economic uniqueness.[235]

Fortner could still point to three other items, the first two of which the circuit court had also relied upon: the large number of tied sales, the low cost of the loan, and the uniqueness of the loan. The first two facts are not

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[233] Some recent cases show a continuation of the great traditions of predation. *See, e.g.,* Otter Tail Power Co. v. United States, 417 U.S. 901 (1974), *aff'g* 360 F. Supp. 451 (D. Minn. 1973); Mt. Hood Stages, Inc. v. Greyhound Corp. 1977-1 TRADE CAS. (CCH) ¶61, 465 (9th Cir. 1977). It is therefore not implausible that a plaintiff might make a reasonably creditable record which would justify the conclusion that package selling in this context by a large firm even without market power is unreasonable conduct. Fortner did not do this despite an explicit invitation in *Fortner I.* Significantly, the Court in *Fortner II* indicates that the issue was not addressed and so was not considered in deciding the appeal. 429 U.S. at 612 n.1.

[234] Dam, *Fortner Enterprises v. United States Steel: "Neither A Borrower, nor a Lender Be."* 1969 SUP. CT. REV. 1. Areeda, *supra* note 191. *See also* L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST, 470 (1977).

[235] A third obvious argument is that once Fortner signed the contract, U.S. Steel had power in relation to him which the facts easily demonstrated; but such purely relational power is not the equivalent of general market power and is not probative of it.

dispositive ones.[236] Footner's strongest argument was that U.S. Steel's loan was unique. This meant that at the time of the loan Fortner had no then available, complete substitute. It would seem undeniable that this would give the offeror of such a product some power, however transient. If a buyer needs this product now, it has to deal with one supplier and in this sense Fortner did establish some transient power in U.S. Steel. Yet even *Fortner* I suggests that such power is not impermissible power unless others are legally or economically unable to make an offer of similar products or services,[237] and *Fortner* II, by holding that indeed such power is not legal sufficient to create an illegal tie-in, resolves this issue correctly. One of the most likely sources of innovation is, of course, those who need to solve a problem to serve their own related interests. U.S. Steel thus pioneered 100% financing not because it was primarily a finance company, but because it believed this would attract or perhaps even create certain classes of buyers.[238] It was seeking to sell houses. So long as its competitors in financing can copy its innovation freely, thus insuring that no lasting or substantial power will accrue, the transitory power that may exist is an essential and unavoidable concomitant of the process of innovation. Hence the Court's conclusion that uniqueness alone was not sufficient evidence to establish power makes very good sense as a policy judgment delimiting the kind of power which is subject to the tying rule.

The Court's opinion essentially presents an analysis of Fortner's evidence to show that none of it is probative of the kind of non-transitory market power that is essential for a tying case. The opinion embraces the Sobeloff formula as a useful starting place,[239] but it makes clear that once the alternative explanation is tendered a plaintiff cannot continue to rely on some general inference of market power.

The opinion for a unanimous court does not admit to any doubt as to the correctness of the nearly total ban on tying when market power is employed. It thus keeps the case focused on the single issue of defining market power. As to that issue, it is fully in accord with the position of *Fortner* I.[240]

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[236] To the extent that U.S. Steel overpriced its houses we would expect discounts of some sort would occur to drop the price. To find large scale tying is suggestive that the discounts are taking the form of some other good or service rather than a direct price cut and to find that the particular good or service being "thrown in" is priced below its general market price would then seem to clinch the argument. These facts do not at all negate the possibility that U.S. Steel had market power. They simply do not resolve the issue. Hence, depending on the initial presumption one would or would not find power.

[237] 397 U.S. at 504-05.

[238] U.S. Steel argued in the circuit court that Fortner would never have been able to buy any homes but for the 100% financing, and so competing sellers of homes had not lost a customer. The evidence was very thin on this point. 523 F.2d at 967. But it is certainly a plausible factual claim and an explanation for innovation.

[239] 429 U.S. at 618 n.10.

[240] The District Court had also found an attempt to monopolize based on the tying conduct. The Court in a footnote reversed this conclusion, 429 U.S. at 612 n.1, on the basis that because U.S. Steel's conduct had been shown to be "nonpredatory competitive conduct,"

4. Fortner II *and the Status of Tying Law*

Fortner II is not a departure from the main line of tying cases. It does treat the outer limits of the market power problem and demonstrates that the present Court, not surprisingly, is disinclined to infer market power in the absence of proof. This will reduce the potential for summary judgments for plaintiffs in tying cases, but ought not seriously affect the main line of litigation in this area.

Unlike *Sylvania,* the *Fortner* II opinion reflects an adherence to existing doctrine, thus suggesting that the law at least as to tying is not going to change. By way of footnote, for example, Justice Stevens demonstrated that he is quite aware of the economic and legal arguments for a more open view of tying and these are inferentially rejected.[241] The vice of tying we are told is that it is "an abuse of market power"[242] and the Court will not tolerate such abuse regardless of its justification.

C. *The Tension Between* Fortner II *and* Sylvania

In *Fortner* II, Justice Stevens announces that the Court has long believed that market power ought not to be misused and that tying based on such power is an example of misuse. However, although one can characterize the *Sylvania* facts to make them fit a tying pattern,[243] Justice Powell largely ignored the fact that market power was an essential element in the operation of any external restraint and so did not address the question of why this use of market power is permissible in spite of the *Fortner* II declaration. Thus, while the outcomes are not necessarily inconsistent, there is an inconsistency in their recognition of market power and a more basic risk of inconsistency in their differing treatment of the use of such power. Why is one use an abuse on its face without regard to justification while the other is not an abuse unless it is "unreasonable"? It is not adequate to invoke stare decisis in one case, but reject it in the other. In some way the Court needs to recognize more directly than it has, the market characteristics that underlie the situations with which it is dealing. Further, the Court should consider the alternative ways power can be used and decide in general whether and what kind of efficiency or cartel interests it will allow to be presented to justify restraints. Only by considering

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no inference of wrongful intent could be drawn. This treatment, which would suggest that intent and conduct can create a violation regardless of probability of success, would imply that any unlawful tie-in was also an attempt to monopolize, but earlier in the same note the court indicates that the lack of evidence of a "large market share or dominant market position" is also dispositive. If that is the case, then the power needed to make a tie unlawful may not be and, under the analysis of the tying cases, ought not be sufficient on its own to show either an attempt to monopolize or actual monopolization in violation of § 2.

[241] 429 U.S. at 617 n.7, *citing* Bowman, *supra* note 199, at 618 n.8.

[242] 429 U.S. at 620.

[243] Sylvania "tied" the sale of its products to the buyer's accepting territorial limitations (the buyers buying those limits). The object here is only to demonstrate that external restraints and tying based on market power involve similar market analysis.

these questions can the Court avoid the kind of ad hoc decision making that has heretofore characterized its treatment of market power. The fundamental ambiguity over the meaning of the rule of reason reflects the ad hoc quality of present decisions. If the decisions are to avoid the creation of meaningless, formalistic categories whose effect is either to trap the unwary or to allow courts to condemn restraints at random some more explicit analysis of why and when firms may legally use their market power is essential.

The revival of an ad hoc rule of reason analysis for restraints also suggests that some long dormant cases might be revived. *Appalachian Coals*[244] and *National Window Glass*[245] prior to *Socony Vacuum* could be said to have allowed failing firms or industries to defend traditional cartel type price fixing and market allocating activity. The Court has never overruled these cases. They could provide, along with *Chicago Board of Trade,* useful precedent for courts willing to tolerate more cartel activity if it were apparently reasonable.[246]

III. The Relationship of Antitrust Law to State Courts and Law

Two cases decided in the past year dealt with the problems of the interrelationship between antitrust law and state law and courts. Although the cases are non-substantive in form, attitudes toward antitrust law and its significance as national policy clearly underlie the resolutions reached.

A. *Vendo and the Relationship Between Federal and State Courts*

1. *Background*

In 1959, Harry B. Stoner caused a corporation he controlled to sell its candy vending machine manufacturing business to Vendo, one of the largest makers of vending machines in the country. As part of that transaction, Stoner also entered into a five year "employment" contract with Vendo

[244] Applachian Coals, Inc. v. United States, 288 U.S. 344 (1933).

[245] National Ass'n of Window Glass Mfr. v. United States, 263 U.S. 403 (1923).

[246] This issue arises most immediately in the context of the increased penalty for violation of the Sherman Act. One district court has indicated that it will allow defendants great latitude to demonstrate that their agreement to restrict and eliminate competition was in some sense reasonable and thus not a felony under the revised law. United States v. Nu-Phonics, 433 F. Supp. 1006 (E.D. Mich. 1977). The judge declared that while the defendants may not try to prove that a chosen price was reasonable, they may try to prove the eliminating price competition among themselves by agreement was a public service since it reduced deception of customers. In other words if a cartel agreement serves some public interest or value beyond the preservation of the parties, it may not be a criminal violation of the Sherman Act; and if it is a defense to a criminal case, why not in a civil case? *Cf.* United States v. United States Gypsum Co., 550 F.2d 115 (3rd Cir.), *cert. granted,* 98 S. Ct. 52 (1977) (court recognized a defense that allows conspirators to confer on prices provided they do so to check specific bids because of the Robinson-Patman Act; the defense implies a pre-existing agreement to keep prices above the competitive level to which they would otherwise fall because the price exchange makes sense only as a means of policing that antecedent agreement; the court is thus creating a legally protected right to maintain a cartel aggreement).

which did not require him to do any work.[247] The sales agreement bound the corporation and the employment agreement bound Stoner not to compete with Vendo in the manufacture or sale of vending machines of any kind in any territory in which Vendo was then selling or might in the future sell for a period of ten years.[248] The product line and the territory thus encompassed were both greatly in excess of products and sales territory of the business which was acquired.[249] The length of the restraint would also appear to go beyond any conceivably justifiable period with respect to that acquired business,[250] and, in fact, Vendo's management viewed the restraint as a potential competitor of Vendo in any of Vendo's activities.[251] This purpose is functionally unrelated to the business acquired from Stoner or his "employment" with Vendo.

Shortly after Stoner sold his business, a former employee developed and patented a new vending machine which was a significant technological advance and a commercial success. Stoner, who had aided financially in the development of this machine kept that fact concealed from Vendo, but did disclose his own interest in investing in the production of the machine. Vendo refused to let him and then asked him to try to buy it for them. Vendo was apparently unwilling to pay the price asked and did not follow up on the initial negotiations. Stoner then invested in the company established to produce the machine.

Upon discovering the investment, Vendo sued Stoner for breach of the convenant not to compete. This suit was in the Illinois courts.[252] The only

[247] "The . . . contract provided that Stoner '[s]hould regulate his own hours of employment and shall determine the amount of time and effort he shall devote' . . . to Vendo." Lektro-Vend Corp. v. Vendo Co., 545 F.2d 1050, 1053 (7th Cir. 1976).

[248] The Agreements are set out in some detail in the Illinois appellate court opinion, Vendo Co. v. Stoner, 105 Ill. App. 2d 261, 267, 268, 245 N.E. 2d 263, 266-67 (1969).

[249] Stoner's company made only candy vending machines which were sold entirely within the United States while Vendo had until that time, made beverage and ice cream vending machines which it sold internationally. Lektro-Vend Corp. v. Vendo Co., 403 F. Supp. 527, 530 (N.D. Ill. 1975).

[250] The function of a covenant not to compete in the sale of a business is not to work a perpetual foreclosure, but only to allow the new buyer time to have fair chance to compete for and attract the sellers' customers. Ten years would seem grossly excessive to achieve this goal in the vending machine business.

[251] "[O]ne of the major advantages was . . . it guaranteed that your [Stoner's] design genius and experience would never be coupled with our money to put a new and most formidable competitor into the business against Vendo." 58 Ill. 2d 289, 298, 321 N.E.2d 1, 6 (1974). This letter also indicates that Vendo's management did not regard Stoner as an employee. Even if he were so regarded, the restraints bear no relationship to the actual work he did for, or knowledge he acquired of, Vendo as a result of his "employment." Since he did nothing for and knew nothing unique about Vendo, Vendo had no valid interest in restricting his future employment. *See* Sullivan, *Revisiting the Neglected Stepchild: Antitrust Treatment of Post Employment Restraints of Trade* 1977 U. ILL. L. F. 621; *cf.* Purchasing Associates, Inc. v. Weitz, 13 N.Y. 2d 267, 196 N.E.2d 245, 246 N.Y.S.2d 600 (1963) (covenant not to compete enforced only to the extent necessary to protect trade secrets, processes, and formulae).

[252] Vendo Co. v. Stoner, 105 Ill. App. 2d 261, 245 N.E.2d 263 (1969), 13 Ill. App. 3rd 241,

explicit consideration of the lawfulness of the restraint as a matter of common law took the form of a highly mechanical analysis.[253] That analysis accepted the formal characterization of Stoner's contract with Vendo as one of employment and asked only whether the restraints were too broad because they covered more than allowed by the state of Illinois. The court relied on an exception in Illinois case law to uphold the restraints.[254]

The Supreme Court of Illinois sought to avoid the issue of validity of the restraint and ostensibly put its decision on a different, independent ground, but that ground, breach of a fiduciary duty, necessarily assumed the validity of the characterization of the agreement as one of employment and the validity of Vendo's rejection of Stoner's request to quit. The fiduciary duty and corporate opportunity analysis in the Illinois Supreme Court is also open to very serious question given the facts in the case.[255]

Having thus lost in the state courts, Stoner revived a pending federal antitrust case and asked for a preliminary injunction against the enforcement of the state court judgement. The trial judge concluded that the restraints were clearly illegal at common law outside Illinois, and, more importantly, violated the Sherman Act in their own right and were but part of a more general scheme to monopolize the vending machine business.[256] The court of appeals accepted explicitly these conclusions as did at least four of the justices of the Supreme Court.[257] In addition, the district court held that the effort to enforce unlawful restraints in a state court was itself a violation of the Sherman Act if there was knowledge of the illegality of the restraints under the federal laws.[258] Given the facts reported in the various decisions, a conclusion of illegality under the Sherman Act for the restraint seems unavoidable. Vendo's efforts to enforce such a patently unlawful restraint would also seem highly objectionable although it may be questionable whether such a suit should be made a separate offense if the underlying, substantive restraint is readily condemnable.

300 N.E.2d 632 (1973), *rev'd*, 58 Ill. 2d 289, 321 N.E.2d 1 (1974), *cert. denied*, 420 U.S. 975 (1975).

[253] 105 Ill. App. 2d at 281-87, 245 N.E.2d at 271-76.

[254] The exception excluded from a general ban on statewide restraints contracts covering the entire state or any larger area enforced "in-term"; to make this an "in-term" restraint the court had to treat it as an employment contract. *Id.* at 284-86, 245 N.E.2d at 273-75. As to the accuracy of that description, see note 251 *supra*.

[255] 58 Ill. 2d 289, 321 N.E.2d 1 (1975). The court asserted that Stoner had breached a fiduciary duty to Vendo when he invested in the project since otherwise Vendo might have done so. For a critical comment on this aspect, see Carstensen, *Antitrust*, 53 CHI.-KENT L. REV. 167, 183-84 [hereinafter cited as Carstensen II]. It may also be worth noting that Vendo was a Missouri corporation and not an Illinois corporation, 403 F. Supp. at 527, so that the application of the Illinois standard to it seems doubly dubious.

[256] Lektro-Vend Corp. v. Vendo Co., 403 F. Supp. 527 (N.D. Ill. 1975) (the trial judge was Richard McLaren, sometime head of the antitrust division, and an acknowledged expert on antitrust law).

[257] 545 F.2d 1050 (7th Cir. 1976), *rev'd*, 97 S. Ct. 2881, 2894-2902 (1977) (Stevens, J. dissenting); neither did the two majority opinions express disagreement with the conclusion of illegality.

[258] 403 F. Supp. at 535.

The case thus reveals a serious and continuing problem of federalism. The Illinois courts had failed to make an analysis of the facts and law that was consistent with the national policy of free and open competition as embodied in the Sherman Act.[259] Although arguably the damage remedy would remain following enforcement of the state judgement, the competitive harm would be done unless the federal court were allowed to intervene in the state proceeding to vindicate the national interest.[260]

At the same time, the case illustrates a pattern that the Supreme Court has in other ways sought to encourage: use of the state rather than the federal forum.[261] Thus, most of the factual issues were resolved by findings in state court having at least some collateral estoppel effect.[262] Thus the task of the federal court was greatly eased and focused on the federal issue: had the state court resolution interferred with the federal policy of competition. However, the federal court also faced the problem of balancing the explicit federalist interest of Congress in preserving freedom of action for state courts.

Under the anti-injunction act,[263] federal courts are generally forbidden from enjoining state court actions. Exceptions exist if a federal statute specifically permits such an action or it such an action is needed in protection of the jurisdiction of the court. Judge McLaren found that Section 16 of the Clayton Act was a specific exception by implication to the anti-injunction act,[264] and that an injunction was essential in order to protect the court's jurisdiction.[265] Having also found that the conduct at issue was very probably a violation of the antitrust laws which would have irrevocable effect on competition he issued a preliminary injunction. The court of appeals affirmed based on the first ground only.[266]

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[259] The substantive failure of the state court analysis and the correctness of the federal court analysis is the focus of this writer's earlier commentary on this case, Carstensen II, note 255 *supra*, at 178-85.

[260] It was contended that ownership of Lektro-Vend Corp. would pass to Vendo, and so the former would be eliminated as an effective competitor of the latter.

[261] *See, e.g.*, Santa Fe Industries v. Green, 430 U.S. 432 (1977); Blue Chip Stamps v. Manor Drug Stores, Inc. 421 U.S. 723(1976).

[262] Judge McLaren interpreted the facts differently from the earlier courts, but he did not suggest that the basic facts were or could be different in this case.

[263] 28 U.S.C. §2283 (1970).

[264] 403 F. Supp. at 536-37.

[265] *Id.* at 537-38.

[266] 545 F.2d at 1056-58. The general standard in the case law for finding an exception to the anti-injunction rule is whether "an Act of Congress, clearly creating a federal right or remedy enforceable in a federal court of equity could be given its intended scope only by the stay of a state court proceeding." Mitchum v. Foster, 407 U.S. 225, 238 (1972). Thus the standard for intervention turns on an evaluation of what is needed to give "intended scope" to a specific congressionally declared policy and ultimately requires a judge to weigh or balance interests even if only implicitly.

2. *The Opinions*

The Supreme Court reversed.[267] Even though six Justices held that Section 16 does allow for injunction of state court actions, two of the six would limit that right so that it would not cover this case. The remaining three Justices held that Section 16 conferred no right to enjoin state courts. Thus the majority was split three to two on the basis for its decision. The opinions are significant because they reflect a three way division of the Court in fundamental attitude toward competition and the policies thereon embodied in the antitrust laws.

To Justices Rehnquist, Powell and Stewart intervention was not necessary. Justice Rehnquist's opinion on their behalf talks of federalism,[268] but it addresses also the relative significance of the antitrust laws as matters of national policy.[269] It is clear that state courts can and will, as in *Vendo,* frustrate the federal policy either if they fail to take it into account or if they hold contrary views about the importance of competition as a value. Congress was clear about the function of the antitrust laws and the goal they were to achieve. If Congress did not address the issue of intervention in state court proceedings explicitly, it is not at all clear why that should lead to an inference that Congress had affirmatively decided that the states should be given freedom to reverse this national policy at will, the effect of the plurality position.[270] In other contexts subsequent to the adoption of Section 16, Congress has been very careful to define what rights it was delegating to the states by way of control over competition and in fact has subsequently withdrawn that delegation.[271] Similarly the Court had previously read narrowly such delegation.[272] This subsequent development can be said to show a judicial and congressional recognition of the need to restrict state freedom of action, both legislative and judicial. Indeed these developments tell more of the reality of the federal relationship than one is likely to find in the original legislative history. Justice Rehnquist's position, nevertheless, is not objectionable if one accepts the policy premise that the interest in federalism overrides all other national interests lacking very substantial merit and the policy conclusion that the antitrust laws lack such merit.

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[267] 97 S. Ct. 2881 (1977).

[268] *Id.* at 2886.

[269] According to this opinion there was a clear Congressional concern reflected in the statute construed in Mitchum v. Foster, 407 U.S. 23 (1972) that state courts could and would adversely affect the federal rights. 97 S. Ct. at 2888-89. This was in part what the *Vendo* case showed state courts could and would do in antitrust matters as well. If the policy of the antitrust law is important, then the facts demonstrate it can "be given its intended scope only by the stay of" these state proceedings and others like them.

[270] Justice Rehnquist's argument that: " . . . Congress in no way focused upon a scheme using litigation in the state courts," 97 S. Ct. at 2888, is a rhetoric device largely designed to justify a conclusion arrived at on other grounds.

[271] *See, e.g.,* Miller-Tydings Fair Trade Act and McGuire Act, 15 U.S.C. §45(a) (2) (5) (1970), *repealed,* 89 Stat. 801 (1975).

[272] Schwegman Bros. v. Calvert Distillers Corp., 341 U.S. 384 (1951).

If a strong federalist policy is the goal, it is still arguable that the plurality position in fact may tend to push in exactly the opposite direction. One needs to consider what the practical lesson of *Vendo* is. That lesson, a little late for Mr. Stoner and his counsel, but clear to all future parties, is to rush to the federal court house and seek initial relief there, as well as an early trial of all issues.[273] The strict construction achieves the avoidance of friction between state and federal courts by allocating a greater burden to the federal courts and making the state courts higher risk forums for dealing with matters that involve national policy issues together with state issues.

Justice Blackmun and Chief Justice Burger, concurring in the result, held that while Section 16 does permit injunctions of state actions, it only permits them when there has been a continued abuse of state court proceedings: "no injunction may issue . . . unless those proceedings are themselves part of a 'pattern of baseless, repetitive claims' that are being used as an anticompetitive device."[274] Since this litigation involved only one state court suit, it did not fit under that standard. Thus, the two justices concurred in the result of the plurality in this case.

Justice Blackmun's three paragraph opinion strongly reflects a minimal intervention approach. It does not appear to consider fully the relevance of state court actions to the achievement or frustration of the federal policy in the antitrust laws. As the dissent pointed out there are many situations in which a single suit will do as much damage to the federal values as will a large number. Justice Blackmun's response is to rely on *California Trucking* as dispositive of the issue.[275] This response demonstrates that Justice Blackmun views the issue in terms of an abuse of legal process as a separate kind of antitrust problem. Only when such abuse of process is present would Justice Blackmun allow intervention. He thus ignores the substance of Vendo's conduct which was, based on the record and decisions so far, clearly illegal and contrary to the federal antitrust laws.

Vendo proved it had a legal right under Illinois law to achieve highly anticompetitive and illegal restraint. Vendo's substantive wrong was in seeking and obtaining the restraint on Stoner. The Illinois courts facilitated the wrong doing because they did not or could not consider the national interest in competition. Justice Blackmun's position would preclude barring state court assistance to wrongdoers so long as the state court found the claims to have a proper basis. This is consistent with Justice

[273] The plurality opinion suggests that Stoner should have raised his federal issue as an affirmative defense, 97 S. Ct. at 2889 n.6, and he could then have had a review in the Supreme Court if that Court was willing to grant certiorari. Fairly obviously, someone relying on a federal law which the state courts are likely to ignore takes a great risk in assuming that the Supreme Court will rush to the rescue. The more cautious course is to pursue federal rights in the federal courts. Thus, the plurality position is disingenuous at the very least.

[274] 97 S. Ct. at 2893-94, 2902-05.

[275] California Motor Transport Co. v. Trucking Unlimited, 404 U.S. 508, 513 (1972).

Blackmun's expressed reservations about the abstract merits of competition.[276]

The *Vendo* case requires balancing the interest in protecting a state forum for business litigation against the risks created to the effective maintenance of national policy favoring competition between unregulated businesses operating in or affecting interstate commerce. The result in *Vendo* is one which, as part of achieving the first interest, gives great deference to the state court judgments on the latter issues. Neither the plurality nor the concurring opinion sees this as a problem although it would be a serious one if the competitive policy of the antitrust laws were held to be central and fundamental guides for the conduct of interstate commerce. These two opinions then suggest that at present five of the justices have serious and substantial reservations about the validity or usefulness of the policy of the antitrust laws.

Justice Stevens' dissent focuses on the merits of the underlying competitive issues and is far more enthusiastic about competition as a central national policy. As a result, the dissenters would emphasize the broader reading of the cases on the anti-injunction act, would down play an abstract emphasis on federalism, and so would have sustained intervention in this case.[277] The dissent would read post-civil war federalism as requiring the states generally to adhere to federal policies embodied in the set of statutes which authorize injunctions.

Justice Stevens' view of federalism may be a more functional and useful one for the last quarter of the Twentieth Century than that of either the plurality or the concurring opinion. It would make it possible for federal courts to defer more to state courts as the forum for major litigation involving both state and federal issues. The federal courts need then only review resolution of the matter as it affects the federal issues after there is full litigation. Unless some such method exists for considering closely the federal issues in state court litigation, the temptation to move to federal court for all purposes will remain quite strong and may prove impossible to deny.

While the outcome in *Vendo* is undesirable both as a matter of judicial efficiency and antitrust policy, it may point toward a closer integration of state and federal courts in handling competitive issues. The question of when federal courts may intervene will arise again[278] since it is clear that at least some intervention is proper.[279]

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[276] United States v. National Association of Securities Dealers, 422 U.S. 694, 729-30 (1974) (opinion by Justice Blackmun).

[277] 97 S. Ct. 2894-2902 (1977).

[278] *See, e.g.*, 827 ANTITRUST & TRADE REG. REP. (RNA) A-2 (1977). (Deputy Assistant Attorney General Sims warned that the Antitrust Division might use a *Vendo* right to block disbarment proceedings if used to police overly restrictive advertising rules).

[279] The problems will be most acute in the "state action" cases. *See, e.g.*, Cantor v. Detroit Edison Co., 428 U.S. 579 (1976); United States v. Texas State Board of Public Accountancy (No. A-76-CA-219, filed Nov. 18, 1976, M.D. Texas), *see also* TRADE REG. REP. (CCH) ¶45, 076 (1976). In those cases, the state or a private party may seek to enforce rights under state law which are the object of a federal litigation.

Even if the concurring opinion in *Vendo* does not accept the competitive policies themselves as substantial enough to warrant intervention, perhaps a concern to achieve effective federalism which means, among other things, that the choice of a state forum should not expose a party to excessive risks of losing federal rights and the effort to find effective ways to reduce the federal court work load will lead its author to accept a more sweeping right to invervene as a functionally more productive way to handle the real problems involved in this class of case.

B. Bates *and The Problem of State Regulation and the Antitrust Laws.*

Following up on several recent cases dealing with state economic regulation, the Court held in *Bates v. Arizona Bar Association* that it is a violation of the First Amendment for the State of Arizona to forbid lawyers to advertise their services and to advertise prices for certain kinds of routine services.[280] The Arizona Supreme Court had adopted as part of its regulation of the bar a requirement that lawyers not advertise. The challengers proceeded on an antitrust theory as well as the First Amendment argument. The antitrust theory raised again the problem addressed in *Cantor v. Detroit Edison Co.*[281] and *Goldfarb v. Virginia State Bar*[282] of when conduct apparently contrary to the antitrust laws can escape an antitrust review because a state legislative scheme mandates it recognizing the conduct as "state action." Attacks on such restraints proceed on the theory that the state was a willing or unwilling agent of a conspiracy and should not be allowed to achieve the result of the removing manifestly anticompetitive conduct from the purview of the antitrust laws.

The *Bates* opinion, joined by all justices on this point, concludes that the anticompetitive requirements were part of the state's regulatory scheme and so cannot violate the antitrust laws. Bates had argued that the recent decisions in *Goldfarb* and *Cantor* required a different result. *Goldfarb* was easily distinguishable because of the explicit conclusion in that case that neither the statutory mandate nor the state supreme court's implementation thereof required the anticompetitive action of the state or local bar associations. In *Bates* the regulatory agency had overtly promulgated the anticompetitive rule pursuant to explicit statutes and state constitutional authority to regulate the bar.

However, in *Cantor* only a year earlier the Court had held that a utility's tariff, approved by the state regulatory agency, to which the utility was legally obligated to adhere until and unless that same agency allowed a change, did not immunize the conduct from antitrust review. One stated reason for this result was that the utility had in the first instance proposed the anticompetitive practice.[283] The challengers in *Bates* argued that since

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280 Bates v. Arizona Bar Association, 97 S. Ct. 2691 (1977).

281 428 U.S. 579 (1976); *see* Dorman, *State Action Immunity: A Problem Under Cantor v. Detroit Edison*, 27 CASE W. RES. L. REV. 503 (1977).

282 421 U.S. 773 (1975).

283 Cantor v. Detroit Edison Co., 428 U.S. at 594.

the organized bar had clearly promoted the adoption of this anticompetitive rule, the rule was not in reality a state mandate but rather, as in *Cantor*, state acquiescence in a private restraint.[284]

In addition the challengers argued that the federal interest in competition must be weighed against the state interest in regulating the bar and ought to prevail especially because the anti-competitive requirement is more intrusive than reasonably necessary[285] to protect any valid state interest. This argument, also found in *Cantor*, invokes the doctrine first expressed in *Silver v. New York Stock Exchange* that the use of a less restrictive alternative test can and should determine jurisdiction as well as outcome.[286] Professor Verkuil has argued convincingly that such an approach would be unnecessarily and excessively intrusive into state affairs.[287] Scope for state experimentation and variation would be severely limited. While this is not necessarily undesirable, a basic commitment to federalism includes a willingness to accept and, indeed, a positive attitude toward, legal variation which in turn may have apparent costs in excess of some other options. Moreover, a less restrictive alternative test would be a very awkward tool for determining outcomes because such a test is not sensitive to the varied degrees of state interest in various regulatory activities or methods. To combine jurisdiction and liability therefore either would lead courts to find many highly restrictive but justified state regulations to be "least restrictive" thus making a hash out of that concept or else create a degree of federal intervention and treble damage liability that would be unacceptable even to those who want the federal courts to strike down many state regulations.

The Court rejected the plaintiff's *Cantor* analogy and advanced three reasons for its position. First, it pointed out that in *Cantor* private parties were being sued and not a public agency while Bates was challenging the state agency. Ths distinction is not a notably useful one since in *Cantor* if the practice was unlawful under the Sherman Act, the utility presumably could have gotten an injunction forbidding the state from requiring it to engage in unlawful conduct. So too in *Bates*, where the theory is that the bar has conspired to violate the law and that the state agency is a tool of the conspiracy. Bates advanced its antitrust theory against the state agency only to keep that agency from carrying out the violation of private parties and not to impose liability on the state for wrongdoing.[288] The only

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[284] 97 S. Ct. at 2700.

[285] 97 S. Ct. at 2707-08.

[286] Silver v. New York Stock Exchange, 373 U.S. 341 (1963). The Court suggests in the case that a private entity enforcing delegated federal governmental power must use due process and otherwise interfere no more than reasonably necessary to carry out its duties if it is to avoid antitrust liability.

[287] Verkuil, *State Action, Due Process and Antitrust: Reflections on Parker v. Brown*, 75 COLUM. L. REV. 328 (1975); *see also* Posner, *The Proper Relationship Between State Regulation and the Federal Antitrust Law*, 49 N.Y.U.L. REV. 693 (1974); Slater, *Antitrust and Government Action: A Formula for Narrowing Parker v. Brown*, 49 N.Y.U.L. REV. 71 (1974).

[288] 97 S. Ct. at 2696-98.

reasonable conclusion, then, is that this argument is a make-weight in *Bates* which has, one hopes, no significance except as it reflects a more fundamental analysis of interests at stake.

The second reason for distinguishing *Cantor* was that *Cantor* had found that there was no state interest in the particular type of regulation involved whereas it was clear to the *Bates* Court especially in light of *Goldfarb* that there was a strong state interest in the regulating of legal practice including the way it was marketed. This analysis of state interest is in all probability the better explanation for the *Bates* Court's first ground for distinguishing *Cantor.* The Court proposes to recognize certain areas as being the proper subject of state regulation and within those areas a valid regulatory scheme will not be ousted by the Sherman Act. This separates an initial jurisdictional issue from the substantive outcome as to the conduct at issue. Implicit in this approach is a revival of one aspect of the "substantive due process" problem that underlies so much of this area.[289] The Court has yet to define criteria to decide whether or not the states ought to regulate certain kinds of economic activity. The dimensions of this issue are but barely discernable as of yet, but clearly the outcome in *Cantor* as explained in *Bates* betokens a more rigorous analysis than has heretofore been employed. Presumably, the Court will respond differently to a formal state legislative decision to regulate with its implicit declaration of a substantial state concern and to a state regulatory agency decision to expand its jurisdiction. But what exactly will determine the scope of state powers is not clear.

The third reason for distinguishing *Cantor* was that in *Cantor* the Court was convinced that the state had merely acquiesced in the restraint whereas the record in *Bates* indicated an explicit state policy "clearly and affirmatively expressed" subject to "active supervision".[290] This criterion seems designed to exclude from state action cases in which a state interest in some regulation is clear, but in which the state has not explicitly articulated and considered what policy it will adopt. This serves to limit the jurisdictional immunity to those cases in which there is reasonable certainty that genuine state interests are at stake in the specific regulatory scheme and not just a general interest which would justify some regulation. Thus the state interest in regulating the bar does not justify allowing *Goldfarb* type private action loosely linked to a state interest in formal regulation.

The second and third reasons suggest a two step test for state action that requires both a legitimate state interest and a real policy even if that policy largely but not entirely reflects the interests and desires of the regulated parties. Conduct pursuant to regulation meeting these two tests

[289] Substantive due process seems to involve first the question of whether any state regulation is lawful, *see e.g.*, Williams v. Standard Oil Co., 278 U.S. 235 (1929) and second whether the specific regulation adopted is reasonable, *see, e.g.*, Nebbia v. New York, 291 U.S. 502 (1934); Mann v. Illinois, 94 U.S. 113 (1877).

[290] 97 S. Ct. at 2698.

will be deemed state action and immunized from the antitrust laws.

This would appear to be a reasonable resolution of the federalist concerns. It would permit a more critical review of apparent state regulatory actions than if the Court strictly adhered to legal formalism. But it would also recognize a substantial zone in which the antitrust laws would not have jurisdiction and in which anticompetitive and potentially undesirable controls would hold sway. Moreover by defining the concern with the non-public origin of regulations in terms of its reflection of conscious state choice, the Court puts itself in position to tolerate regulatory schemes largely or entirely promoted by and for the regulated so long as there is a real acceptance and adoption of this outcome by state legislative and administrative bodies.

Clearly a most important limitation for the exemption can come from the development of guidelines for what interests or goals a state may seek to advance or protect via regulation. Such guidelines will be much more significant if they focus not only on the general topic or business subject to regulation but also on the specific regulation and how it may or may not relate to the interests that a state may have in regulation. By introducing more rigorous standards for interest identification and requiring a clearer or more substantial relationship between regulation and specific interest even without any substantial limit on the interests which states may elect to protect, the courts are likely to pare down greatly the amount of anticompetitive regulation immunized as "state action" because much of it cannot withstand public exposure of the interest being protected or explicit analysis of the relation between the interest protected and method of regulation.

The ultimate outcome of the attack on the restrictive regulation in *Bates* illustrates the jurisdictional character of the state action consideration, and demonstrates that choice of jurisdiction need not be outcome determinative.[291] States do not regulate free from national policy, and so while a finding of state action terminates some legal rights, e.g., treble damages, it does not necessarily have to lead to a different substantive outcome with respect to the conduct. In *Bates,* therefore, despite the state action determination, the Court struck down the regulation. It did so on economic free speech grounds,[292] but those grounds make little sense unless the Court has some faith in the competitive market as a relevant and useful device for achieving desirable price and output decisions. It is, therefore, not surprising that it was the justices least enthusiastic about competition who saw least merit in the outcome. Thus Justices Powell, Stewart and Rehnquist, the hard liners in *Vendo,* all dissented in *Bates,* this time joined by Chief Justice Burger. Justice Blackmun wrote for the majority and was joined by the Justices White, Stevens, Brennan and

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[291] This is usually ignored by commentators. *See* Handler, *Competition v. Regulation,* 44 U. CIN. L. REV. 191 (1975). *But see* Stokes, *A Few Irreverent Comments about Antitrust, Agency Regulation and Primary Jurisdiction,* 33 GEO. WASH. L. REV. 529 (1964).

[292] 97 S. Ct. 2698-2700.

Marshall (the latter being the four dissenters in *Vendo*).

Since *Bates* was resolved on the merits in terms of constitutional requirements, this aspect of the decision falls slightly outside the scope of this article. Nevertheless, the holding of the case merits two further notes in terms of the significance of antitrust and competitive policy. First, in rejecting the Sherman Act claim, Justice Blackmun, in a footnote, quotes the *Virginia Pharmacy* case to the effect that "Virginia is free to require whatever professional standards it wishes. . . .; it may subsidize . . . or protect from competition in other ways."[293] This statement is very much at odds with the apparent enthusiasm for competition that underlies the outcome in both *Virginia Pharmacy* and *Bates.* Although the point may simply be that other explicit regulation to serve specific goals may be permissible and that the Court is not saying that the goals sought are impermissible, it may well be that this passage reflects ambivalence about competition especially in Justice Blackmun's mind.[294] In that case the free speech problem is indeed crucial and achieving the same anticompetitive result on the same dubious claims of public interest which were rejected in both *Bates* and *Virginia Pharmacy* would be acceptable if the regulatory devices were different. Such an approach would be defensible in terms of a judgment that some methods of control are less permissible than others but that the Court ought not to interfere in the final judgment once a regulatory object is found to be within the state's purview. It would be ironic indeed from a competitive policy perspective to find that more explicitly economic control such as a general price control plan for the state would be protected from objection even though it had only the remotest connection to the ethical interests that the state was ostensibly promoting. Such an approach, if it is in reality what is motivating the majority, ought to have manifested itself in a more absolutist attitude on the free speech issue. That is, if protecting speech is the real and primary goal, then the very relativistic language of the opinion which suggests weighing gain against loss would seem very inappropriate since other regulatory tools could, at perhaps much greater costs, solve the same problems without any interference with speech.

Moreover *Bates, Goldfarb, Virginia Pharmacy,* and *Cantor* all speak about competition as a substantively desirable national policy relevant to state action. Hence, while ambivalence about competition certainly exists on the Court, these cases should be read in terms of an implementation of our national policy favoring competition. It is not sensible for that substantive concern to be manifest only in a review of some forms of regulation where a constitutional speech issue also exists especially when the issue arises only because of a prior commitment to competition. Moreover, to hide competitive policy issues under a First Amendment label is to obscure the process of inquiry and direct it in a tangential course.

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[293] 97 S. Ct. at 2698 n.16, 97 S. Ct. at 2698 n.16, *quoting* Virginia Pharmacy Bd. v. Virginia Consumer Council, 425 U.S. 748, 770 (1976).

[294] *See* note 276 *supra.*

The second observation that the *Bates* opinion suggests is that the Court will soon have to articulate a general view on the least restrictive alternatives doctrine. The Court's analysis of the values protected by the advertising ban and how they might justify some ban even if not an absolute one, suggests that here, as in some other constitutional areas,[295] the Court is following a least restrictive alternative approach and so will ultimately find some regulation constitutional where no lesser restraint will reasonably protect the interest at stake. So far none of the cases presented have required a detailed evaluation of alternatives and their relationship to permitted or intended goals. Still, a test of reasonableness that uses the *United States v. Third National Bank* analysis[296] would seem suited not only to the reconciliation of the First Amendment and other interests but also to the more general task of balancing the national policy of competition, against state efforts to promote their legitimate interests by restricting such competition. What is suggested is that under a due process or commerce analysis, state regulation can be evaluated in terms of the interests served and whether less restrictive (anticompetitive) alternatives would serve those same interests equally well. If regulation was too restrictive, it would then be objectionable on constitutional and not antitrust grounds. Such a solution needs to be explored and considered at greater length than is here possible because it raises difficult problems for federalism and may involve a return to a level of federal judicial intervention in state matters not seen for some decades and perhaps not to be desired either as a matter of judicial or substantive policy.

IV. The Private Damage Action: The Emergence of the "Proximate Causation" Issue

When Congress initially adopted the Sherman Act it included in it a private cause of action for damages.[297] Some at the time thought this a useless inclusion,[298] and indeed it remained a less than overwhelming problem for wrongdoers for some substantial time. Nevertheless the Clayton Act restated the private cause of action and expanded it to include the right to injunctive as well as damage relief.[299] Despite much lavish praise of the "private" attorney general as a force for achieving antitrust compliance,[300] it is only in the past two or three decades, expecially after the electrical conspiracy cases, that private actions have achieved a great role

[295] Gunther, *The Supreme Court 1971 Term, Foreword: In Search of Evolving Doctrine on a Changing Court: A Model for a Newer Equal Protection,* 86 HARV. L. REV. 1 (1972).

[296] 390 U.S. 171, 189-92; *see* text accompanying notes 183 & 184 *supra.*

[297] 26 Stat. 210 (1890), The Sherman Act, ch. 647, §5.

[298] Pollock, *The "Injury" and "Causation" Elements of a Treble-Damage Antitrust Action,* 57 NW. U.L. REV. 691 (1963) [hereinafter cited as Pollock I] (discussing debates on the Sherman Act).

[299] 15 U.S.C. §26 (1970) (injunction); 15 U.S.C. §15 (1970) (damages).

[300] *E.g.,* Loevinger, *Private Action—The Strongest Pillar of Antitrust,* 3 ANTITRUST BULL. 169 (1958).

in shaping the substance of antitrust law and in creating a new and unique set of problems.[301]

Damage liability under the antitrust laws, a form of tort action, is no different from any common law tort except as there may be specific legislative limitations or expansions. The basic antitrust statute authorizing private damage actions contains most general and inclusive language: ". . . any person who shall be injured in his business or property . . . may sue . . . without respect to the amount . . . and shall recover threefold the damages by him sustained . . .".[302] As a result, judicial interpretation and development of the damage action has only the most remote root in specific statutory language and proceeds instead primarily as a common law matter of judicial legislation.

Because a wrongful act may have a great variety of harmful consequences, not all of which are ones the wrongdoers should be responsible for and because the consequences of a wrongful act can carry forward through time and spread out and affect a great number of remote individuals or firms in one way or another at sometime, there must be limits on the scope of liability for any wrongful act. These limits include the substantive definition of wrongful conduct as well as the limitations of the parties to whom a legal duty is owed and the types and kinds of losses which will be treated as legal injuries. This is as true for antitrust or securities law as for medical malpractice or automobile negligence.

Until recently such general tort issues, while obviously present in antitrust damage actions, have been submerged, surfacing only fitfully and then not receiving substantial or sustained attention from the courts or commentators.[303] The past year, however, produced two decisions from the Court which address the problem of the limitations on private actions. Consistent with the Court's limiting views on the substance of the law, both decisions adopted quite limited rules on the scope of liability. In *Illinois Brick Co. v. Illinois,* the Court defined "injury to business and property" so as to limit greatly the class of litigants who might sue a wrongdoer.[304] In *Brunswick Corp. v. Pueblo Bowl-O-Mat,* the Court defined narrowly the kinds of losses for which a wrongdoer might be held responsible.[305] In both cases the Court apparently assumed that the conduct in issue was wrongful as a matter of substantive antitrust law, and that the

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[301] *See,* M. HANDLER, H. BLAKE, et. al, *supra* note 40, at 160 (Chart III).

[302] 15 U.S.C. §15 (1970).

[303] Justice Brennan, in dissent, saw this issue in Illinois Brick Co. v. Illinois, 431 U.S. at 760 ("standing" in antitrust is "not unlike . . . proximate cause . . ."). Several commentators have also made this observation; Pollock, *supra* note 298; and Pollock, *Standing to Sue, Remoteness of Injury, and the Passing on Doctrine,* 32 ANTITRUST L. J. 5 (1966) [hereinafter cited as Pollock II]. *See also* Handler, *The Shift from Substantive to Procedural Innovations in Antitrust Suits: The Twenty-Third Annual Antitrust Review,* 71 COLUM. L. REV. 1, 24-31 (1971); McGuire, *The Passing-On Defense and the Right of Remote Purchasers to Recover Treble Damages Under Hanover Shoe,* 33 U. PITT. L. REV. 177 (1971).

[304] 431 U.S. 720 (1977).

[305] 429 U.S. 477 (1977).

wrongful conduct in fact caused the losses of which the plaintiff complained.[306] A traditional tort classification for the issues thus framed is proximate causation or legal duty, and it is in terms of that notion, in part, that we will examine these cases.

A. *Extent of Duty:* Illinois Brick

For those who enjoy the more cosmic of legal jokes, it is at least mildly amusing that the "citadel" of privity[307] finally overthrown in products liability and other common law torts may have arisen again this time to plague antitrust. Alternatively, and probably equally amusing, the Court may be trying to revive the distinction between "direct" and "indirect" injury, made famous by the great pleading forms, Trespass and Case, as distinctions of significance in antitrust matters, in spite of their disreputable legal history and despite the Court's rejection of ancient legal distinctions in *Sylvania.*

1. *Background*

The vehicle for all of this hilarity was a treble damage suit against a group of concrete block makers. The concrete block makers engaged in a price fixing conspiracy[308] among whose primary, and allegedly intended victims, were the state of Illinois and the local government and special government units in that state that had built large numbers of buildings using these materials. The government units had in most cases bought completed buildings from general contractors that had subcontracted the masonry work, and it was those masonry subcontractors that bought the allegedly price fixed materials from the conspirators. The governmental units alleged, however, that the intervening transactions between themselves and the contractors and between the contractors and subcontractors only passed on the unlawfully high price of the concrete blocks. Essentially the argument was that the governmental units, having specified the exact materials for building specific buildings, had determined the exact amount of input so that, with respect to each construction contract, this element was entirely inelastic and each intervening level of competition amounted to no more than a cost plus addition.

The defendants moved to dismiss and argued that they were not liable for the damage done since these plaintiffs had not purchased directly from defendants.[309] The trial judge dismissed the complaint on the ground that

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[306] Actually both cases, like so many other tort matters resolved ostensibly on proximate cause grounds, involve serious substantive or causal questions which while not formally addressed may account for the result. *See* text accompanying notes 401-02 *infra.*

[307] Prosser, *The Fall of the Citadel (Strict Liability to the Consumer),* 50 MINN. L. REV. 791 (1966); Prosser, *The Assault Upon the Citadel (Strict Liability to the Consumer),* 69 YALE L. J. 1099 (1960).

[308] United States v. Illinois Brick Co., [1974] TRADE CAS. (CCH) ¶ 75, 060 (D. Ill. 1974) (consent decree).

[309] The defendants had already settled with both the contractors and the subcontractors

the plaintiffs lacked standing.[310] The Court of Appeals reversed.[311] The Court of Appeals rejected the "standing" label and instead treated the case as involving two issues: causation in fact and proximate causation. With respect to causation in fact it concluded that the plaintiffs' allegations would, if proven, solve the causation problem that existed in many comparable cases.[312] The court then considered whether despite the assumed causal connection, the rights of buyers not in privity with the wrongdoer should be so limited as to preclude them as a matter of law from recovering the losses which it was now assumed the wrongdoers had caused. The court concluded that the intended as well as reasonably foreseeable victim of an illegal act under the antitrust laws ought to have a chance to collect any loss suffered as a result of such wrongful conduct.[313]

2. *The Decision*

By a six to three vote the Supreme Court reversed this decision and held in an opinion by Justice White that "the overcharged direct purchaser, and not others in the chain of manufacture or distribution is the party 'injured in his business or property' within the meaning of the section".[314] The opinion followed Justice White's prior opinion in *Hanover Shoe Inc. v. United States Machinery Corp.*[315] which had rejected a similar passing-on argument when asserted by a defendant trying to reduce its obligation to a direct purchaser. Justice White purported to reconsider that earlier decision and reaffirmed it. The opinion in this case involves a classic confusion between causation in fact and proximate causation as well as a highly ambiguous ultimate standard for deciding the latter issue when applied to cases involving issues other the price fixing.

A crucial but not fully resolved question is what issue or issues the Supreme Court believed this case presented. If the problem is one of pleading and causation in fact, then the issue turns on factual analysis of specific situations and kinds of burdens to be imposed on a party. If the problem is one of deciding whether a class of businesses or consumers which has in fact suffered economic loss as a result of wrongful conduct

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in agreements which explicitly stated that these settlements were not to affect the defendants liability to the ultimate consumers.

[310] 67 F.R.D. 461 (N.D. Ill. 1975).

[311] 536 F.2d 1163 (7th Cir. 1976). For a favorable view of this decision see Carstensen II, *supra* note 255, at 175-78 (1977).

[312] 536 F.2d at 1166. The court treated Hanover Shoe, Inc. v. United Shoe Machinery Corp., 392 U.S. 481 (1968) and Mangone v. American Radiator & Standard Sanitary Corp., 438 F. 2d 1187 (3d Cir. 1971), as cases on causation. The court also treated its own earlier decision in Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co., 315 F.2d 564 (7th Cir. 1963) as involving this issue although that characterization is a dubious one for a case which really decided that utilities were more appropriate parties to recover an overcharge than their customers.

[313] 536 F.2d at 1165.

[314] 431 U.S. 720, 729 (1977).

[315] 392 U.S. 481 (1968).

shall be allowed to sue for compensation, then the issue is one of legislative policy addressing the broad functions of private antitrust actions and their place in the judicial scheme of things. Causal proof problems are not irrevelevant to proximate cause issues, but they are not central either because, as a generalization, the issue of proximate causation ought not arise unless cause in fact is established.

At the outset of the *Illinois Brick* opinion, Justice White, through a footnote, makes clear that there is substantial doubt on his part that "passing-on" could in fact have been demonstrated in this case. The note reports that only 7% of the 700 plaintiffs could state the cost of the block used in the buildings they purchased.[316] Moreover, in the only example cited to the Court the block involved cost less than one-half of the one percent of the entire project.[317] The inability of the buyer to calculate the costs involved and the very small portion of the whole represented by the cost of concrete blocks are indeed facts making it unlikely that plaintiffs could have shown a causal connection between the final building costs and the existence of a conspiracy to fix concrete block prices to a degree of certainty necessary to prevail in a civil action. It would be perfectly plausible to have handled "remote" buyer claims by insisting they they meet an initial causation test which establishes not merely a possibility of effect, but provides a clear factual record that allows a court to see that the effect probably was present and substantial. To the extent that Justice White has fairly characterized the facts, it seems dubious that damage could in fact be shown and so the case ought to have ended.[318] The Court even characterized the court of appeals opinion in causal terms. It then appended a footnote which said that the district court was wrong to put this case on the issue of standing and that the court of appeals was correct to suggest that "the questions of which persons have been injured . . . for purposes of section 4 is analytically distinct from the question of which persons have sustained injuries too remote to give them standing to sue. . . ."[319]

Justice White does not explain what that distinction is, but he cites a passage in an article by Handler and Blechman which asserts that the basis for the *Hanover Shoe* rule is that it is generally impossible to show the causal connection between a wrong at one level of production and prices at any other level than that of the direct buyer.[320] This suggests that

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[316] 431 U.S. at 727 n. 6.

[317] *Id.*

[318] Such a result would have been quite consistent with the causal problems identified in the ealier cases denying "standing" and would have distinguished them from the cases in which the causal connections seem to have been much clearer. *See, e.g.*, In re Western Liquid Asphalt Cases, 487 F.2d 191 (9th Cir. 1973), *cert. denied*, 415 U.S. 191 (1974). The *Illinois Brick* Court conceded that the issue varies with the case in its degree of difficulty, 431 U.S. at 743.

[319] 431 U.S. at 728 n. 7.

[320] Handler & Blackman, *Antitrust and the Consumer Interest: the Fallacy of Parens Patriae and A Suggested New Approach*, 85 YALE L. J. 626, 644-45 (1976), *cited*, 431 U.S. at

Justice White saw the distinction in terms of the difference between causation ("persons . . . injured" in fact) and proximate causation ("persons . . . too remote" to have standing despite a causal injury). However, it subsequently appears the Justice White proposes to define "persons . . . injured" not by a factual inquiry as to actual injury but by definition of what "injured" means as a legal concept. It is still possible to imagine "persons . . . too remote" as a matter of legal policy even if they belong to the limited class of those who are legally "persons . . . injured". In light of the result of the case, Justice White is using both tests to define narrowly the class of permitted litigants, and he is doing so not on causal grounds but on grounds of legal policy.

Although preserving a few narrow exceptions to the general rule, e.g., those for whom purchases are made on a cost plus basis can claim damages, which might also suggest that this is a factual problem, since the Court, without a factual analysis of the instant case, rejected the right of these plaintiffs and all others similarly situated to seek to prove the fact of loss, it is clear that however much the lack of causal evidence influenced the Court in this case, its result will be applicable regardless of the facts of causation in other cases. This holding makes "indirect" parties "too remote" from the wrong to be allowed to bring a suit because they have suffered no legal "injury"; and, therefore, they lack standing. It is clear that the Court ultimately developed a proximate cause or legal duty test which delimits the class of possible plaintiffs, and that we must address that as the law for better or worse. It is not clear, given the ambiguity of the opinion, that the Court either understood the alternatives before it, or appreciated that if its view of the facts was correct, it could have resolved this and similar cases on a more limited analysis of causation.

Because the task the Court set for itself was that of legislating a meaning for the category of "person . . . injured", its conclusion cannot be criticized as right or wrong, but it can be evaluated in terms of its consistency with the stated basis of decision, its applicability to other situations, and the persuasiveness of the final result. In getting to the final rule Justice White first considered whether the *Hanover Shoe* rule could remain for defendants but allow plaintiffs to prove passing-on. He rejected this unequal application on two grounds.

First, such a rule could create serious problems of multiple recovery since the first purchaser would presumably be entitled to recover the entire overcharge while subsequent purchasers would be entitled to re-claim that portion actually passed on to and absorbed by them. A crucial premise here is that the amount of the overcharge is a proper measure of damages in these cases. Another premise is that multiple recovery is unacceptable. Given the trebling requirement already in the damage standard, an argument could be made that any additional charges on a wrongdoer were also

728 n.7 [hereinafter cited as Handler & Blackman]. For a *contra* view see Berger & Bernstein, *An Analytical Framework for Antitrust Standing*, 86 YALE L.J. 538 (1977) [hereinafter cited as Berger & Bernstein].

inconsistent with congressional policy but, basic notions of fairness as well as some conformity to the statutory scheme doesn't require that defendants generally not be held to more than three times the damages they have caused.

The lower courts which had not followed *Hanover Shoe* when dealing with plaintiffs have pointed out a range of devices that can minimize the risk of recovery exceeding the statutory norm.[321] Cases can be consolidated,[322] some damages can be escrowed for the period of the statute of limitations, statutory interpleader and joinder can be used.[323] Despite these devices, there is some risk that claims in excess of the statutory norm will be paid. There is, of course, no evidence that wrongdoers who have settled with multiple classes of buyers have in fact paid more than three times the damage they have caused.[324] Nevertheless the Court finds there is a risk and does ". . . not find this risk acceptable"[325] The fact the Court cannot and does not even try to quantify this risk or compare it to other risks of inappropriate damage liability for the defendants[326] sugggests that the argument is a make weight and not central to the result. It is, of course, also possible that the majority simply assumed that the risk existed in sufficient degree because of the obvious concern of defense lawyers with the problem.[327] While such a technique for deducing economic facts is highly suspect, it is not unknown in other legislative contexts.[328]

The second, more significant, reason[329] for rejecting the unequal treatment approach is that the basis for the *Hanover Shoe* decision and, therefore, for the bar to consideration of passing-on was the burden and difficulty of deciding the issue. There are the great "uncertainties and difficulties in analyzing price and output decisions . . . "[330] and these uncertainties and difficulties would impose great costs on the judicial system and "efficient enforcement of the antitrust laws" if they had to be resolved in

[321] *See, e.g.*, In Re Western Liquid Asphalt Cases, 487 F.2d 191 (9th Cir. 1973), *cert. denied*, 415 U.S. 919 (1974).

[322] *See* Multi-District Litigation Act, 28 U.S.C. §1407 (1970).

[323] 28 U.S.C. §1335 (1970); FED. R. CIV. P. 22 (1) & 19.

[324] In the antibiotic litigation, the settlements with all various classes do not seem to have deprived the putative wrongdoers of more than their actual gain. *See*, Wolfrom, *The Antibiotics Class Actions*, 1 A.B. FOUND. RESEARCH J. 253 (1976).

[325] 431 U.S. at 731 n. 11.

[326] The basic and very minimal standards for proof of damages, Bigelow v. RKO Radio Pictures, 327 U.S. 251 (1946); Story Parchment Co. v. Paterson Parchment Paper Co., 282 U.S. 555 (1931) create risks that defendants who in fact, caused no damage or slight damage will be held, by a jury which is given great latitude to speculate on damages, to have caused substantial damage with resulting magnification from the trebling requirement, but these risks have never botherd a majority of the court.

[327] *See, e.g.*, Handler & Blackman, *supra* note 320, Pollack I & II, *supra* notes 298 and 303. Plaintiffs lawyers have, of course, depricated any problems here. *See, e.g.*, Berger & Bernstein, *supra* note 320.

[328] Recent "crisis" in medical malpractice and products liability insurance apparently are examples of this process.

[329] 431 U.S. at 730-32, 732 n. 12.

[330] *Id.*

the court room. If this is the primary rationale for the *Hanover Shoe* decison, it would follow that it ought to be applied both ways. This is also an explicitly factual rationale. It implies exceptions for cases in which a theory of damage and the related prima facie evidence would demonstrate that the uncertainty and difficulty would not be present. That is to say, this is an argument based on causation in fact and would imply a set of rules on presumptions and burdens of pleading and offering initial evidence so that trial courts can separate out the few valid cases from the scores of invalid ones. But just as in an analogous area of securities law, the Court here is using the causation argument to justify a total closure of access to the courts for a class of litigants.[331] Had the Court approached the issue in terms of its own stated primary concern it would have seen that a plaintiff's use of the passing-on theory, since it is an affirmative proof, may be tested more easily than a defendant's negative use of passing-on as a defense. The plaintiff must plead and offer proof that would show a court with some certainty that the "uncertainties and difficulties in analyzing price and output decisions" normally to be expected can be overcome. If in *Illinois Brick* the consumer was buying a bulding which it had designed, including a detailed specification of materials, it would appear that the consumer would have estimated the probable cost of any significant item and would expect the contractor and sub-contractors to pass along that cost since it would be a common and substantial factor in the bids of all competitors.[332] Defendants trying to rebut a damage theory are not generally in a comparable situation since they have no particular interest in proving who else was in fact damaged. It may make very good practical sense to take an even tougher line with defendants who seek to escape liability by trying to show that a particular plaintiff passed on to some unknown, non-party the costs of the violation than to a plaintiff who offers a convincing proof of how the damage came to rest on it.

There are, however, two values which Justice White lists which explain, perhaps, why this factual problem can be used to justify the line drawn.

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[331] In Blue Chip Stamps v. Manor Drug Stores, Inc. 421 U.S. 723 (1975) the Court converted the *Birnbaum* rule from one of causation which had exceptions when a non-buyer could show the requisite causal connection into an absolute bar to suits by non-purchasers or sellers. The opinion, having stressed the general causal problems to which the instant case was an exception, nevertheless refused to allow the suit to proceed. As in *Illinois Brick* then, the Court was actually adopting a rule of limitation not justified by its causal concerns, but rather by other interests not fully articulated.

[332] That this may not have been the fact in the *Illinois Brick* case is the burden of the suggestion in one footnote, 431 U.S. 727 n.6. It does seem to have been the case in the electric generator and turbine conspiracy damage cases. It would seem factually absurd to say that the ultimate buyer as well as all intermediate contractors were not expecting the full cost of that equipment to be passed on. In such cases, who the "buyer" is in the first instance seems a most irrelevant inquiry in a functionally oriented analysis. *E.g.* Washington v. General Electric Co., 246 F. Supp. 960 (W.D. Wash. 1965). *See* Missouri v. Stuapp Bridge & Iron Co., 248 F. Supp. 169 (W.D. Mo. 1965). *See also* Comment, *Standing to Sue in Antitrust Cases: The Offensive Use of Passing-On*, 123 U. PA. L. REV. 976 (1975).

First is the burden on trial courts of resolving these issues.[333] If one believes that antitrust cases are using up too much of the scarce and valuable time of judges, then one will seek to simplify and limit the cases they hear. Justice White returns to the theme of the burdens on the courts several times in the opinion[334] and it appears that a device to reduce the number and complexity of antitrust cases in the federal courts rather than a desire to find reasonable ways to handle complex factual issues substantially explains the bar to considering the passing-on issue. The second value adverted to is effective enforcement of the antitrust law which here has primarily a deterrence and not a compensation goal. For deterrence purposes, concentrating recovery in the hands of one victim will be as satisfactory (and perhaps make suit more attractive) as spreading the right around. Having identified the role of damage actions as being primarily one of deterrence, it is then rational to try to eliminate redundancy in achieving that goal.

Having thus explained why whatever rule as to passing-on exists must apply both ways and also having implicitly taken the rule out of the realm of factual analysis despite the factual type of argumentation, Justice White addresses the question of retention of the *Hanover Shoe* rule. Once again Justice White's substantive analysis begins with the assumption that the proper measure of damages is the overcharge collected by the wrongdoer. The opinion then postulates that "potential plaintiffs at each level in the distribution chain are in a position to assert conflicting claims to a common fund—the amount of the alleged overcharge. . . ."[335] But despite the devices of joinder and interpleader, Justice White concludes that it "is unlikely . . . that all potential plaintiffs could or would be joined."[336] This creates risks of "multiple litigation and liability" which presumably are unacceptable to the Court. More serious, however, is the probability of transforming "trebel-damage actions into massive multiparty litigations involving many levels of distribution and including large classes of ultimate consumers remote from the defendant."[337] Apparently assuming that such "remote consumers" would never be "too remote" to have standing once included in the class of "persons injured",[338] Justice White points to a tabulation showing that many price fixing cases involve goods which are at best inputs into inputs which produce consumer goods.[339] This is of course the "slippery slope" argument. It is a valid argument, and it explains why all tort law has proximate cause rules as well as causation rules to limit the class of litigants to those probably injured by conduct not too remote. It is not, however, an argument that

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[333] 431 U.S. at 730-32.
[334] *Id.* at 741-42, 742 n.27.
[335] *Id.* at 737.
[336] *Id.* at 739.
[337] *Id.*
[338] *Id.* at 741 n.24.
[339] *Id.* at 740 n.23.

demonstrates why a large class of litigants need be cut off from all rights unless it can be shown that courts have no other way to control the problem. Certainly Justice White makes no demonstration that such a situation exists in this case. In fact, he argues that in most such cases proof of actual causation will be impossible. But if that is so, then there is not a serious problem. Remote consumers will be easily dismissed because they cannot make out a prima facie case. Still drawing the line "would entail the very problem that the . . . rule was meant to avoid."[340] Once again, the point of reference is the burden on the judiciary of dealing with these problems. Justice White assumes that the *Hanover Shoe* rule provides a judicially easier solution.

Justice White justifies the *Hanover Shoe* rule not only in terms of easing the judicial burden, but also in terms of "effectiveness" of private antitrust litigation. While recognizing that this result may deny recovery to those "actually injured," the opinion again asserts that remote purchasers have little stake in the matter and so will merely dissipate the common fund and thereby discourage direct buyers from suing.[341] The empirical validity of this proposition is as dubious as any, and the effectiveness argument points in reality back to the issue of judicial convenience.

In sum, the opinion, while analytically confused, does contain a clear ultimate message: the Court wants to reduce the workload of the federal judiciary and believes that by eliminating "indirect purchasers" from the class of "persons . . . injured," it can achieve that result without unacceptable compromise to the effectiveness of private antitrust actions. Very important to this conclusion is the premise that the direct purchaser can collect the full amount of any overcharge, trebled, so that the wrongdoers are totally deprived of their ill-gotten gains. Viewed in this light much of the opinion is surplusage and is not truly explanatory of the reasons for the outcome.

Three problems, however, require further consideration. The first is the correctness of equating damages to specific victims with the gain to the wrongdoer. Second, is the role and significance of the 1976 amendments to the antitrust laws as they may have altered rights to the overcharge fund. Finally, it is important to define as rigorously as possible what the court means by "direct purchaser" so that it is possible to determine what this case may mean to other types of cases and other damage theories.[342]

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[340] *Id.* at 745.

[341] *Id.* at 745-46.

[342] Justice Brennan's dissent presents §4 as having "broad objectives: to compensate. . . and to deter . . .", and it "was clearly evident to operate to protect individual consumers . . ." *Id.* at 748. He points to the 1976 legislation based on that premise and accuses the majority of flouting the will of Congress. *Id.* at 748-49. Justice Brennan also stresses the need to have a class of plaintiff able to deprive the wrongdoer of his full overcharge which he equates with "the full social cost of. . . illegal conduct. . ." *Id.* at 752, thus giving *Hanover Shoe* a relevance to defensive passing-on claims only.

Justice Brennan takes issue with the majority's implicit premise that excluding remote buyers will reduce litigation, pointing out that most of the same problems exist in estimating

3. *The Overcharge as a Measure of Damages*

Both majority and dissent assume that the overcharge is a fair measure of the total damages caused by an unlawful restraint of trade. The gain to the wrongdoer is indeed a measure of the damage done to the economy as a whole in terms of the amount of cash diverted to the wrongdoers. But if that cash were used in socially desirable ways or even paid out to shareholders, the ultimate bad effect may not equal the initial diversion.[343] In any event there is no reason to believe that it is an accurate measure of the damage done to any particular victim.[344] To the extent that an overcharge is passed on without loss of sales or margin, the intermediary has lost nothing and has not suffered real economic damage. If sales are reduced or margins affected, or both, to that extent the party has absorbed the overcharge.[345] Such absorption can result, of course, in total business failure. In that case, the damage to such victims may exceed the total gain to the wrongdoers. The loss is even greater if one adds in the ultimate "indirect" effects of such business failures. Conversely, where each level passes on the price raise and the final consumer takes the same amount as before,[346] the damage can be said to have come to rest on whatever producers and distributors of other goods which lost sales to those final consumers. Obviously, a claim by any such seller would, absent very special facts, run into insuperable problems of proof of causation for the injury is really only general and not specific.

It was this ultimate damage which the State of Hawaii sought to collect in *Hawaii v. Standard Oil*[347] when it sued a group of alleged price fixers.

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the basic overcharge. Therefore, because he believes compensation is very important and a central part of the statutory command, Justice Brennan would open the court house doors and invite indirect buyers to try to prove their losses, but "there is a point beyond which the wrongdoer should not be held liable." *Id.* at 760. This is the reason for requiring "standing" which is "not unlike . . . proximate cause . . ." *Id.* But whatever scope is given to §4, "surely it must render the defendant liable to those within the defendant's chain of distribution." *Id.* Thus Justice Brennan would draw a line of remoteness much further out and only employ causation as limit on recovery. This would probably be too sweeping a result unless it were coupled, as it is not, with a fairly rigorous test for causation. Justice Brennan apparently gives inadequate consideration to the problems of excessive classes and redundant claimants.

Justice Brennan also evaluates in some detail the risks of multiple recovery in excess of §4's authorization and concludes that risks are as "a practical matter, remote." *Id.* at 763-64.

[343] We would have to perform a sort of social cost benefit analysis based on an ultimate tracing of the effects, good and bad, of the wrong.

[344] The error of equating X's gain to Y's loss is an obvious point in most accident cases. The initial confusion in antitrust arises from the fact that the initial injuring impact is in the form of an overcharge in some cases. But just as the value of a car tells nothing definitive about the injury it has done, so to the amount of an overcharge is not definitive of the economic loss that has resulted.

[345] This would seem the better measure of initial economic loss. *See* Pollock, *supra* note 298.

[346] Such a case of total inelasticity of demand may seem unlikely, but it is perhaps exemplified by the antibiotics case. *See* note 331 *supra*.

[347] Hawaii v. Standard Oil, 405 U.S. 251 (1972).

The Court, correctly perceiving that the ultimate effects of a wrong could be multiplied many times over as they spread through the entire economy, rejected this claim.[348] Moreover, in adopting the parens patria legislation, Congress did not reverse that holding[349] despite Justice Brennan's contrary suggestion.[350] Such damage is "too remote" to be collectable, and it would impose too great a cost on the wrongdoer for the benefit to be gained.

There is a second generally recognized but harder to define limitation on liability. It is a sort of reverse privity bar. Thus those in continuing privity with the victim of a wrong have no right to make a separate claim and can only look to the primary victim to act for them. This includes situations in which the secondary victim is a shareholder or creditor of the primary victim[351] or belongs to a class of continuing customers as in the case of public utilities or public housing agencies.[352] Similarly, those who are suppliers of a victim but who are not themselves in the direct line of production and distribution of the affected item, generally cannot pursue claims either for the lost business with the victim or for any consequential injury.[353] Here too, the fact that these secondary victims had a contractual relationship which defined their rights and interests in the victim's business, seems to provide a basis for excluding any general concern for the consequences to them and for requiring that they rely on the victim or its trustee in bankruptcy to assert whatever claim the victim has and to apportion the results as required. Predictably the resulting hard cases are those in which the arguably secondary party is more nearly a joint venturer or partner with the victim and so appears more like an independent victim.[354] Not surprisingly the right of such a "partner" to sue on its own for

[348] *Id.* at 262-64.

[349] The new section limits liability to: "injury sustained . . . to . . . property . . ." 15 U.S.C. §15c (a) (1) (1976). Damage moreover may be measured "by the computation of illegal overcharges . . ." 15 U.S.C. §15d (1978). The House Report makes it very clear that the purpose of the law is to reverse California v. Frito-Lay, 474 F.2d 774 (9th Cir.), *cert. denied,* 412 U.S. 908 (1973) which denied the right of a state to seek any damages in a parens patria capacity. H.R. REP. No. 94-499, 5, *reprinted in,* [1976] U.S. CODE CONG. & ADMIN. NEWS 2572, 2574. The measure of damages is implicitly limited by the rule in Hawaii v. Standard Oil, 405 U.S. 251 (1972), and this is evident from the view that the new law will deprive wrongdoers of " . . . all measurable fruits of . . . illegal activity . . ." H.R. REP. No. 94-499, p. 14, *reprinted in,* [1976] U.S. CODE CONG. & ADMIN. NEWS. 2583.

[350] 431 U.S. at 756.

[351] Loeb v. Eastman Kodak Co., 183 F. 704 (3rd Cir. 1910). *See* McGuire, *The Passing-On Defense and the Right of Remote Purchases to Recover Treble Damages Under Hanover Shoe,* 33 U. PITT. L. REV. 177 (1971).

[352] *See* Commonwealth Edison Co. v. Allis Chalmers Mfg. Co., 315 F.2d 564 (7th Cir. 1963) (ultimate consumers denied standing when public utility already suing for damage); *cf.* Illinois Brick Co. v. Illinois, 431 U.S. 741 n. 24.

[353] Harrison v. Paramount Pictures, Inc. 115 F. Supp. 312 (E.D. Pa. 1953), *aff'd,* 211 F.2d 405 (3rd. Cir. 1954). *See also* Billy Baxter, Inc. v. Coca-Cola, 431 F.2d 183 (2nd Cir.), cert. denied, 401 U.S. 923 (1970) (franchisor had no standing to sue for injury to it inflicted via injury to franchisee).

[354] Congress Building Corp. v. Loew's Inc., 246 F.2d 587 (7th Cir. 1957). *See also* Karsdal Corp. v. Richfield Oil Corp., 221 F. 2d 358 (9th Cir. 1955) (franchisor held to have standing for injury to it through franchisee).

its loss is not uniformly resolved, but interestingly, the damage measure seems to focus on the loss to that joint venture and not other consequential injury to the party,[355] thus illustrating the force of the basic limitation even if its application is obscure in certain circumstances.

It thus becomes clear that the overcharge bears only a fortuitous correlation to the total economic dislocation that a wrongful act causes.[356] The overcharge does nevertheless measure the gain to the wrongdoer and to the extent that wrongdoers expect to be deprived of their entire gain, trebled, they should be discouraged from wrongful conduct. By equating damages to the overcharge, the law creates a penalty designed to deter conduct and not to compensate loss.

Absent a specific statutory plan for allocating the penalty, it would seem that the fairer result is to allocate it to the most remote victim with standing having deducted therefrom the claims paid for actual damage to other intermediate victims. Since the intermediate victim is only injured economically to the extent that sales volume or profits per sale are affected, proof of damage for such victims would be unrelated to the amount of the overcharge and would require a very different line of proof. Thus in *Illinois Brick,* the plaintiff's proof of damage would relate to how much taxes were raised or what other activity was foregone by virtue of this wrongful conduct. To the extent that such injury exists and can be shown it is only fair to compensate for it. Indeed, if the effect was more serious, e.g., total failure, that too ought to be compensated even if compensation to victims exceeds the benefits to the wrongdoer. The most remote victim, to which injury can be traced, however, can argue that its passing-on took the form of doing without other goods or buying less of the overpriced goods and that the specific effects cannot be traced further, and so it is entitled to the residual fund because there is no other way to measure its economic loss.

The practical problems with such a result are first that the class of residual victims will be large and disparate with both little individual financial interest and little capacity for self organization. Second, to the extent that many distribution levels intervened, each would have a potential claim which, if unprovable, would suggest that that level is the final one. This reverses incentives to prove specific injury and is likely to make it practically impossible to determine the proper resolution of the claims. The *Hanover Shoe* result if read as a rule which allocated the penalty to the first victim except as other claimants could show specific damage served to solve the practical problem of assigning the right to a party likely to exercise it while not depriving more distant victims of compensation where injury occurred. Such a reading makes the plaintiff's right to prove

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[355] 246 F.2d at 591-93.

[356] *See* Morkovits, *A Basic Structure for Microeconomic Policy Analysis in Our Worse-Than-Second-Best-World. A Proposal and Related Critique of the Chicago Approach to the Study of Law and Economics,* 1975 WISC. L. REV. 950.

passing-on integral to the rule while also justifying the denial of such a right to defendants and so could rationalize a double standard. This pragmatic view turns very much on the incapacity of final consumers or some remote class of distributor to organize and make their collective claim for the penalty. Congress sought to solve this problem by the 1976 legislation.

4. *The Parens Patria Legislation*

The Antitrust Improvements Act of 1976 contained a provision by which Congress[357] created a specific right for state attorney generals to bring suit to collect the damages to ultimate consumers; the amount of these awards were to be reduced by the amount of other damages paid for the same conduct.[358] The residual fund would then be available to final consumers who had been demonstrably overcharged with the state claiming the remainder. Accepting at face value the statement that this statute created no new liability for defendants,[359] what sense does it make? Arguably Congress accepted the view that one proper measure of damages was the amount of the overcharge, but this sum, less payment for actual injuries, should go to the states as representatives of the final consumers and others who were as a class injured in their property in some degree. The effect then was to allocate the penalty to a public body and to allow nonremote parties to prove actual damages.

On this reading, even if individual consumers could not prove actual losses, the state could claim and retain their presumptive collective "direct" loss. "Direct" here means the initial overpayment and not the consequential damage to the economy. In this way the legislation could have become the first step toward the kind of economically rational enforcement system envisaged by Elzinga and Britt.[360]

This construction of section 4(c) would not have been precluded by the majority's outcome in *Illinois Brick* if that outcome were put in terms of a rule of proof on causation or in terms of a rule defining remoteness, barring private parties who were otherwise "persons . . . injured." The reading suggested here requires only that ultimate consumers be deemed capable of being "persons . . . injured." If that is so, then the state can make its collective claim even if the individual is too remote. Thus, even while barring this suit by Illinois as representative of specific buyers, the Court could have allowed it to refile in its parens patria role to claim that portion of the overcharge not allocable to other victims. The deterrence function would thereby be served, and the Court could thus rationalize a very tight limit on which possible victims can take judicial time trying to prove their particular injury.

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[357] 90 Stat. 1383. P.L. No. 94-435; 15 U.S.C. §15 (1970).

[358] 15 U.S.C. §§15c, 15d (1970).

[359] 431 U.S. at 733 n.13.

[360] K. ELZINGA & W. BRITT, THE ANTITRUST PENALTIES: A STUDY IN LAW AND ECONOMICS (1976).

Having chosen, however, to cast the issue in terms of defining "persons injured" the Court has made much more difficult any accomodation of the apparent Congressional scheme for assigning claims to the penalty fund. It has defined the losses to consumers as not being legal injuries under the antitrust laws.

The actual treatment of the 1976 act in the opinion is for a more limited purpose. Justice White rejects the argument that the Act and the underlying Congressional understanding of who has a legal claim for damages is dispositive of the meaning of section 4. Justice Brennan similarly used the statute as part of an argument that Congress intended at all times to include ultimate consumers among the class of those who could sue under section 4.[361] Thus, neither opinion puts the new statute into the context of the problems of depriving the wrongdoer of gain and compensating victims when only private parties are litigants. While it is still open to the Court to reread the legislative history in light of a broader analysis of what was being accomplished thereby, such a prospect seems most unlikely.

5. *Defining the Standard in* Illinois Brick

In order to generalize about the limits of damage liability under section 4 it is necessary to define what relevant attributes explain when a party is not injured within the meaning of the section. Two prospects suggest themselves. The first is that some notion of privity is involved here so that one might look to *Winterbottom v. Wright*[362] and its progeny for guidance. The second is that "directness" is the important concept so that common law distinctions between trespass and case might be useful.

If one wanted to argue privity here, one would point to the use of the phrase "direct purchaser" as indicative of an underlying notion that there ought to be actual, contractual dealings between the parties.[363] The exceptions to the rule reinforce this for they involve cases in which the buyer is a de facto agent, for either some other buyer[364] or for the seller.[365] The problem of buying from a seller other than the one sued could be solved by treating the conspiracy as a unit and asserting that dealing with one was the legal equivalent of dealing with all. Moreover, it is very clear that the test for rejecting a claim rests on the lack of actual dealing, i.e., privity, with a wrongdoer. Thus privity in some degree is at least implicity in the

[361] 431 U.S. at 758.

[362] Winterbottom v. Wright, 10 M & W 109, 152 Eng. Rep. 402 (Ex. 1842).

[363] In one pre-*McPherson* antitrust case, a quasi-privity standard for measuring standing (proximate cause) was employed. Chattanooga Foundry & Pipe Works v. City of Atlanta, 203 U.S. 390 (1906). A similar rule exists for collecting freight overcharges, e.g., Southern Pacific Co. v. Darnell-Taenzer Lumber Co., 245 U.S. 531 (1918), but that is explicable in substantial measure by the nature of the statutory right involved. *See* Pollack II, *supra* note 303, at 24.

[364] This is the cost plus case which is made an exception in *Hanover Shoe*, 392 U.S. at 494 and *Illinois Brick*, 431 U.S. at 735-36.

[365] *E.g.*, Perkins v. Standard Oil Co., 395 U.S. 642 (1969) (where direct purchaser is controlled by seller, then next buyer can assert a claim).

formulation of the specific rule and it would appear to be an essential idea. The citadel thus created is not so procrustean as that in *Winterbottom*, but it has the capacity of making decision simple and the test of liability straight forward.

It would nevertheless seem that a privity requirement is as objectionable here as in products liability. Cardozo reject it as a reasonable rule in *McPherson v. Buick Motor Co.*[366] His words are applicable here:

> The defendant knew the danger. It knew also that the car would be used by persons other than the buyer. This was apparent from its size; there were seats for three persons. It was apparent also from the fact that the buyer was a dealer in cars, who bought to resell. The maker of this car supplied it for the use of purchasers from the dealer. . . .The dealer was indeed the one person of whom it might be said with some approach to certainty that by him the car would not be used. Yet the defendant would have us say that he was the one person whom it was under legal duty to protect. The law does not lead us to so inconsequent a conclusion.[367]

It cannot be denied that the wrongdoers in antitrust cases know or ought to know that some or all of their overcharge will come to rest on others. Use of a privity bar permits escape from liability for the consequences of this conduct. Moreover, there is good reason to believe that the immediate buyer may be unwilling or uninterested in vigorously prosecuting the claim or taking more than nominal damages. These buyers are likely to have a substantial stake in their continuing relationship with their supplier. The relative interest in vigorous pursuit of these claims probably explains why it is believed that the bar on class actions and parens patria claims for overcharges will reduce costs and exposure of wrongdoers. There is a parallel to other tort cases which preserve the privity requirement.[368] Denial of liability on lack of privity grounds is explicable in terms of a policy judgment that liability should be greatly limited.[369] Such cases leave rights only with parties who suffered no real damage and so have no claim for compensation. The antitrust situation is slightly different, but the effect of reducing claims is similar. Requiring privity as a basis for recovery is a device to limit liability. It is, however, such an arbitrary line that it has lost favor in most areas of tort law, and it is useless as a general guide in antitrust.

The typical boycott case illustrates the irrelevancy of privity. The complaint of the victim is that it lacked privity with someone. Similarly, in cases of predatory pricing or other monopolization conduct which is harm-

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[366] 217 N.Y. 382, 111 N.E. 1050 (1916).

[367] *Id.* at 391; 111 N.E. at 1053.

[368] *E.g.*, Ultramares Corp. v. Touche, 255 N.Y. 170, 174 N.E. 441 (1931); Moch v. Rensselaer Water Co. 247 N.Y. 160, 159 N.E. 896 (1928).

[369] Gregory, *Gratuitous Undertakings and the Duty of Care*, 1 DE PAUL L. REV. 30, 60 (1951).

ful to an actual or potential competitor of the monopolist, the effect is quite independent of privity. Indeed, privity is unlikely to exist between the wrongdoer and any victim of its wrong. Surely, the Court does not mean that the beneficiary of the predatorily low price, because it was a "direct purchaser" and is also a favored "private attorney general," has the right to claim the value of the damage to its supplier's competitor trebled.

Had Illinois recast its damage theory to show how much taxes were raised or what other expenditures were foregone as a result of this wrongful conduct, it would have shown that its damages were unrelated either to the overcharge fund or to the line of privity by which the wrongdoers had an impact. Indeed, in cases of territorial or customer allocation or other restraints indirectly affecting price, the victim's harm, whether victim is a direct purchaser or some more remote party, will not necessarily correspond to the gain of the seller, direct or remote, but to the losses suffered.

If one rejects privity as a useful guide for other cases, but is still persuaded, as seems evident, that the Court intends to limit the scope of liability, then one must assume that directness is the test. For centuries tort law sought to use the distinction between direct and indirect injury as a guidepost. In common law, directness referred to the force of an act. When that force was spent, the act ceased to be a direct cause. But by the late 1700s it was clear that life was too complex to sort easily or consistently according to such mechanical analysis. The famous squib case of *Scott v. Shepherd*[370] is but an example. In that case Blackstone argued that an object thrown by two intervening actors (passed on, if you will) had caused only an indirect injury while the majority with equal logic treated these actors as responding inevitably to a situation (much as a middle man reselling might be said to respond to price fixed goods) and so the force was a continuous one making the injury "direct." The lesson which American courts soon drew was the degree of directness ought not affect the substance of liability because it is not a rational or convenient distinction.[371] The ultimate victim in a passing-on case is thus a direct victim of the economic force of the wrongdoer if a court says so and not if a court says not. "Direct" is thus a conclusionary label employed to describe a class which is to be favored.[372]

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[370] Scott v. Shephard, 3 Wils. 403, 95 Eng. Rep. 1124.

[371] *See*, Brown v. Kendall, 60 Mass. 292 (1850).

[372] It should be added that the circuit court's standard of "reasonably foreseeable" victims is no more useful as an operational tool. Reasonable foreseeability involves a factual question which focuses the inquiry on the expected injury. But except for the rare case of an actor operating under a wrong but reasonable factual premise the resolution of a "reasonable foreseeability" inquiry turns upon notions of policy and not fact. The fundamental question is one of responsibility. Should this actor be held responsible for this outcome? If the conclusion is that there ought not be responsibility, then the court will say there was not "reasonable" foreseeability and the reverse if the opposite result is reached. Thus in the famous *Palsgraf* decision, the arguments of majority and dissent can justify either conclusion in the case, but it is Andrews who captures better the truth of the process:

The result is that while it is understandable that a line be drawn to exclude remote victims neither "privity" nor "directness" explain why the line is drawn where it is or what considerations would justify its location elsewhere in other cases. We do know that judicial burden, a lack of significant, adverse effect on the desired level of deterrence, and the undisturbed, theoretical capacity of the remaining private attorney generals to enforce that penalty provision are advanced as explaining the specific outcome. We also know from other decisions this term that three of the justices voting for this position have, in general, a low regard for the value of the policies antitrust seeks to vindicate while another, the Chief Justice, is ambivalent in substantial measure. On the other hand, Justices White and Stevens, who also voted with the majority, have in other contexts supported antitrust and the competitive policy it entails. Such substantive support comports with a view that damage rights should be narrowly defined. Such a narrow definition may make less fearsome strict substantive requirements. This suggests in turn that the value adverted to in the opinion may not in fact be the major factors that underlie the conclusions of this heterogenous majority.

Thus while the broad message of limited scope for liability is clear its form permits neither the abstraction of a general rule nor a model for identifying relevant values and interests and relating them to each other in a way which establishes relative weights. In short, the decision is a fundamentally ad hoc one, having no immediate explanatory or guiding capacity for other situations. This in turn suggests the Court has not solved the problem of judicial burdens, although it has to be sure removed one set of burdens with respect to one class of case. But plaintiffs can develop "direct damage" theories, i.e., lost sales or other specific injury unrelated in value to the amount of the overcharge, and they may not be excluded from court. Such cases after all present different judicial burdens. Alternately, these victims may sue the direct purchaser on theories of constructive trust or some similar exotic contract notion.[373] More likely, defendants in a great range of cases may seek to eliminate classes of plaintiffs. Thus an accused monopolist may urge that its competitors could not be legally "injured" since they did not purchase from the putative monopolist. To eliminate this class of case, would of course reduce judicial burdens; and, since the Justice Department, FTC and, perhaps, state attorney generals can bring injunctive cases, a judge could conclude that the effective en-

> What is a cause in a legal sense, still more what is a proximate cause, depend in each case upon many considerations, as does the existence of negligence itself. Any philosophical doctrine of causation does not help us. . . .What we do mean by the word "proximate" is, that because of convenience, of public policy, of a rough sense of justice, the law arbitrarily declines to trace a series of events beyond a certain point. This is not logic. It is practical politics.

Palsgraf v. Long Island R.R., 248 N.Y. 339, 162 N.E. 99 (1928) (Andrews, J., dissenting).

[373] Some states are already trying to obtain in their purchase contracts assignment of any antitrust claims the vendor may obtain by virtue of the transaction. 834 ANTITRUST & TRAD. REG. REP. D-3 (Oct. 13, 1977).

forcement of antitrust laws will not suffer.

It is doubtful then that the Court has in fact reduced the judicial burden in antitrust litigation when the totality of the problem is considered. In addition, as already suggested, initial buyers in fact may be unlikely to exact the full penalty and thus fail to deter as fully as they ought wrongful conduct, especially when its economic impact has largely been passed on. Moreover, by inviting defendants to seek to escape liability by claiming that no legal injury occurred rather than focusing on the actual economic impact and substantive lawfulness of the conduct, the Court creates an added route of escape for wrongdoers and so reduces the certainty of liability and damages for wrongful conduct. The net result may still be that an "effective" remedy exists but such a conclusion only emphasizes the fact that the Court is striking a fairly complex balance within and among antitrust policy goals, broader social interests in continuity of business and avoidance of excessive or unfair burdens on business, and judicial institutional interests.

6. *Conclusion on Illinois Brick*

Even if no right or wrong answer exists when courts engage in rule making, there are cases to evaluate. We have seen that the Court did a bad job of identifying the concerns with which it dealt. As a result its own arguments and analysis hardly justify or explain its resolution of the problem it ultimately addressed. Worse, the solution adopted would appear to transfer litigation and other problems into new areas without any way resolving them.

Despite the weaknesses of the *Illinois Brick* opinion in its particular context and the impossibility of using a direct injury test as a tool of analysis or predictable guide to decision in other cases of antitrust damage claims, the opinion does raise a real and serious problem for all commercial tort litigation. In an interconnected economy, each antitrust wrongdoer is part of the entirety of the economy. Its conduct affects, for good or ill, many others over a long time. For this reason alone some boundary lines must be drawn around the liability of specific wrongdoers. They should reflect the social interest in having an open and competitive economy (deterrence) and in compensating those firms and individuals who suffer actual, specific damages without jeopardizing the functioning of significant sectors of the economy or introducing excessively distorting costs. Equally compelling, ultimately is the argument that the judicial system must not be totally encumbered by intractable problems of antitrust damage apportionment. However, to set up a boundary based on directness, privity, or the first sale, is to employ an overly simplistic solution to a complex problem of adjusting interests. If private antitrust damage actions are to remain workable and defensible, it is very likely that *Illinois Brick* will require great elaboration and interpretation or legislative limitation.[374]

[374] Indeed, several bills are already pending in Congress to reverse this outcome.

B. Permissible Damages: Polemis, Wagon Mound, *and the Antitrust Law*

The problem of which losses from a wrongful act are compensible has long existed in general tort law. The famous *Polemis*[375] case required compensation for all damage resulting from a wrongful act even if the damage was not foreseeable. The *Wagon Mound*[376] decision reversed that holding, and decreed that damages had to be of a kind related to the risks that one might expect from a particular wrongful act. It is still generally the case that plaintiffs can recover all of their damages even if they are much more than was likely in such an injury. The distinction between kind of damage and degree of damage is a nice one. It reflects underlying policy about the role of the tort action and the degree it is to be encouraged or discouraged.

In antitrust, the price fixer who caused a business to fail will be held liable for the lost value of the concern, but if the firm survives it collects the lost profits on sales. As in the case of the egg-shell-skull victim of the traffic accident, the antitrust wrongdoer takes its victim as it finds him if it inflicts expected harm. However, if the injury is not of the type that normally would be expected to flow from the wrong, or if the injury, while predictably flowing from this wrong, is not one which the law wishes to acknowledge as a legal right of the victim, then the injury is said to be of a different kind and not merely another degree. The issue is one of legal causation or responsibility. Given an act which is wrongful to the victim and which causes a loss, is the wrongdoer is to be held responsible for the loss?

1. *Background of* Brunswick

During the late 1950's and early 1960's the bowling alley business grew rapidly; the makers of equipment engaged in a great many credit sales; and when the market turned down found themselves with many credit problems on their hand.[377] The result was litigation in many areas of business law.[378] Brunswick, one of the largest of the equipment makers, survived the market decline and resulting defaults. In some cases it resold the bowling alleys which it had had to take over, but in other cases it undertook to operate them. In total, it operated less than two percent of all bowling alleys in the country. Nevertheless it was the largest single operator and, by virtue of its overall size, was very much larger than any other operator.[379] Brunswick came to operate alleys in three cities, Pueblo, Paramus, and Poughkeepsie in competition with ones operated by Treadway. Tread-

[375] In re Plemis and Furness Withy & Co., [1921] 3 K.B. 560 (C.A.).

[376] Overseas Tankship (U.K.) Ltd. v. Morts Dock and Engineering Co. Ltd., [1961] A.C. 388.

[377] 429 U.S. at 479.

[378] *E.g.*, Escott v. Bar Chris Corp., 283 F. Supp. 643 (S.D. N.Y. 1968) (established the basic guidelines for prospectus disclosure and the liability of various parties for the failure to conform to these obligations).

[379] 429 U.S. at 480.

way sued for damages, divestiture and other injunctive relief with respect to these acquisitions.

At trial a jury found the mergers illegal, and the resulting damages to be $2.3 million before trebling.[380] Despite a finding of error in the jury instructions, the Court of Appeals upheld the substantive theory of the plaintiff that a deep pocket "giant" which enters a market of pygmies by acquisition may thereby violate Section 7 of the Clayton Act.[381] The four examples of the ways competition might be lessened are instructive: three clearly described ways in which the larger firm can be more efficient than the smaller firm, while the fourth, a greater capacity to absorb low or negative returns for a long period of time, is not inconsistent with ordinary and acceptable competition.

The Court of Appeals also endorsed as the proper measure of damages for this violation a determination of the lost opportunity of Treadway to make profits in excess of those it had made because of the continued existence of the Brunswick alleys in the markets.[382] The court of appeals accepted all "causally linked" damages thus adopting a *Polemis* approach. Interestingly, this theory required Treadway to prove that these alleys would have failed and been removed from the market. This theory does not quite square with the theory of substantive violation which addressed only the risks to competition from the acquisition. The Supreme Court agreed to examine the case only with respect to the damage issue and so did not consider the merits of the merger case or the kinds of equitable relief that might be in order.[383]

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[380] Treadway Companies v. Brunswick Corp., 389 F. Supp. 996 (D.N.J. 1974).

[381] NBO Industries Treadway Companies v. Brunswick Corp., 523 F.2d 262 (3d Cir. 1975). Vertical and congolmerate mergers rules are only remotely connected to the traditional concerns of antitrust policy. For this reason, this area of law has been extensively criticized, *See, e.g.*, P. STEINER, MERGERS: MOTIVES, EFFECTS, POLICIES (1975). Bork & Bowman, *The Crisis in Antitrust*, 65 COLUM. L. REV. 363 (1965); *see also* Turner, *Conglomerate Mergers and Section 7 of the Clayton Act*, 78 HARV. L. REV. 1313 (1965). Even its defenders do not try to justify much of the case law. *See, e.g.*, Blake & Jones, *Towards a Three-Dimensional Antitrust Policy*, 65 COLUM. L. REV. 422 (1965). Yet the Court of Appeals theory of violation would condemn even acquisitions of failing firms normally lawful. *See* United States v. Greater Buffalo Press Co., 402 U.S. 549 (1971); Citizens Publishing Co., v. United States, 394 U.S. 131 (1969); International Shoe Co. v. FTC, 230 U.S. 391 (1930). Moreoever, the condemnation of combinations resulting in disproportionately deep pockets rests on the fear that the merged firm will be more efficient than existing firms. The theory is not necessarily bad as merger law doctrine especially if courts are not sure about economics and efficiencies in a local market or in an industry of small firms. It makes sense to insist on a fair fight to determine that kind of firm and industry structure will prevail, and a deep pocket entrant which buys its position rather than competing for it is a distorting element. *Cf.* Union Leader v. Newspapers of New England, Inc., 180 F. Supp. 125 (D. Mass. 1960), *aff'd in part*, 234 F.2d 582 (1st Cir. 1961). But the theory does press the law and logic of the law to an extreme, particularly in the context of the bowling alley business which has low levels of concentration, heterogeneous ownership patterns, and lost cost of entry—all of which suggest that merger is not likely to have a radical effect on local or general industry structure.

[382] *Id.* at 272-73.

[383] The Court granted Brunswick's petition for certiorari 424 U.S. 908 (1976), and never acted on Treadway's, *see* 429 U.S. at 484.

2. *The Opinion*

The Court through Justice Marshall unanimously rejected the *Polemis* approach: a wrongful act of the defendant does not make all consequences of that act a proper basis for damage recovery.[384] The Court pointed out that the plaintiff was in fact asserting a theory that it was wrongfully denied a monopoly or oligopoly position in a market and that its "damages" represented the lost profits of that wrongfully denied monopoly. The Court, adopting the *Wagon Mound* approach, held that damages must relate to the antitrust problem that gave rise to the suit. Since the anti-merger rules relate to protection and maximization of competition, the profits of a lost monopoly opportunity cannot represent the proper measure of damage. Indeed, "[i]t is inimical to the purposes of these laws to award damages for the type of injury claimed here."[385] In order to claim damages the injury must flow "from that which makes defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of the anticompetitive acts made possible by the violation".[386] The absurdity of the *Illinois Brick* approach of equating the gain to the wrongdoer with the amount of injury to the victim is evident in this case.

The problem thus becomes what damages could result in this kind of case. Marshall suggests that if the unlawful merger results in "anticompetitive behavior" victimized competitors "may be able to prove antitrust injury before they actually are driven from the market. . . ."[387] His specific example of such behavior is "predatory below cost pricing", but it should be recalled that the court of appeals identified as other competitive evils such things as "cost-savings," so that it may be possible for a firm to recover damages upon a showing that its "normal profits" were lost or it failed because its competitor became more efficient as a result of a merger.

Examining the record, the Court found no evidence of "any cognizable damages" despite some conclusory efforts to show abuse of the deep pocket by Brunswick.[388] Therefore the Supreme Court entered a directed verdict on the damage issue and remanded for consideration of the lawfulness of the mergers and any injunction as to future conduct which might then be appropriate. This kind of cut off of the opportunity to have the trial court decide whether a new trial on damages is in order raises a question of whether the Supreme Court has dealt adequately with the case. The plaintiff could try to show that some or all of the lost earnings it had previously demonstrated were lost because of some "anticompetitive" behavior such as "cost-savings" achieved by the competitor. By refusing to allow the trial court to decide whether the damage case should be considered again, is the

[384] 429 U.S. 477.
[385] *Id.* at 488.
[386] *Id.* at 489.
[387] *Id.* at 492 n.14.
[388] *Id.* at 490.

Court perhaps not signaling its own lack of confidence in the merits of the purported violation? If Brunswick can achieve "cost-savings" for its alleys, a court is very unlikely to bar that because it adversely affects existing competitors. Thus, the lower court could be trusted to ignore most of its wild rhetoric insofar as injunctions were concerned where the absurdity of the command would be obvious, but in light of that same rhetoric one cannot be sure how either the trial court or the circuit court would treat the damage issue. In such a case it is perhaps preferable not to find out and so foreclose that option.

3. *Damage Policy*

Even under a *Wagon Mound* approach, the Court's *Brunswick* decision is not free from objection. Some monopoly is both permissible and lawful. To the extent that it is legal, should it not be protected from loss imposed by wrongful acts? Because one has a legal right to something, if it comes one's way, does not, of course, mean it necessarily follows that its loss is a compensable event. A classic common law case was that of the *Schoolmasters of Gloucter*[389] who objected to a new competitor in their market whose presence had produced a substantial price cutting on education. While acknowledging the loss that resulted the court found that no legal wrong was done because no interest entitled to legal protection had been invaded. So too in the *Brunswick* case, the existing competitor can complain only of losses resulting from unfair conduct that makes the competitive race inequitable but not generally of the lost opportunity to make excess profit.

However, in this instance the monopoly or oligopoly right is lost as a result of a wrongful act which should never have occurred. Even though one has no general right to be free from competition, should there nevertheless be a right to be free from this competition, and the losses that result? While as an abstract principle this sounds dubious, it has the pragmatic value of rewarding more completely, and so encouraging litigation of this sort. If the result of the litigation would be clearly and always socially desirable, then expanding the damage categories would be a sensible policy tool. However, it is probably not the case that private suits will necessarily serve the public good. In the traditional cartel cases in which a true per se analysis applies, the undesirability of the conduct is clear. A broader range of damages might therefore be logically allowable to anyone who identifies and proves the underlying violation.[390] This in turn suggests that damage rules ought to focus on the competitive and efficiency implications of classes of conduct and narrow the damage reward wherever necessary to

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[389] Anonymous, "The Schoolmaster Case," Y.B., 11 Hen, IV f. 47, pl. 21 (Ct. of Com. Pleas, Hilary Term) reprinted in M. HANDLER, H. BLAKE, et al., *supra* note 40, at 42-43.

[390] The fact that lost profits may have involved an element of oligopoly power, for example, should not necessarily mean that they be discounted when they were lost as a result of, for example, a boycott.

insure that private litigation will be as consistent as possible with the fundamental public policy goals of antitrust. In the case of merger, this view suggests that damages[391] and conduct injunctions[392] be disfavored and only divestiture be allowed as relief in the usual case.[393]

Two other examples come to mind, the Robinson-Patman Act is one. The *Utah Pie* case[394] has been well described as an anticompetitive re-

391 To prove a damage claim in a merger case, the plaintiff must, in effect, show that defendant is able to serve the market at a lower cost than existing competitors which means that customers would prefer, presumably, the illegal merger and so any competitive effect will be entirely incidental to the greater efficiency of the new firm. If no efficiency exists, then losses will involve either disruption of a monopoly or tacitly collusive oligopoly, or an attempt by the new entrant to achieve market dominance. In the first case, the merger has made the market more and not less competitive so that whatever social concern there may be with problems of injury to general social values that result from conglomeratization, there is no effect on the local firms or market that is cognizable in antitrust. In the second case, the real complaint is that one firm interferred with the others access to finance, supplies, customers, etc., for the purpose of acquiring market power. But that is a case of attempted monopolization and ought to be governed by those standards. Therefore, an unlawful merger ought not to give rise to damages unless some other statute is also violated.

392 A injunction to bar "deep pocket" conduct in the future would bar, on the circuit court theory of the risks of such a merger, conduct which involves generally efficient use of resources; assuming that injunctive relief is granted, the courts will be commanding wasteful conduct. This seems highly objectionable as a matter of policy. Whatever values are to be protected by a limit on this kind of merger if they do not warrant the prohibition of the merger ought not warrant judicial regulation of the conduct of the business so as to produce inefficient behavior. It would be better, cheaper, and more administrable to tax, in the form of annual damages, the efficient firm and pay that subsidy to the inefficient ones and then allow each to go its own way.

393 Divestiture returns the market to status quo ante and leaves those in and out free to compete, to enter, or to leave as they see fit.

The divestiture remedy provides not only a more easily administered solution but insures that the plaintiff is serving a public interest. A plaintiff seeking only lost monopoly profit and/or an injunction barring its "illegal" competitor from effective competition is not serving the public interest in promoting and protecting competition. But a plaintiff seeking to undo a merger, while it obtains its legal expenses (15 U.S.C. §16 (1970)), is otherwise saying it wants to retain a competitive environment. This conclusion may be qualified as to cases in which the plaintiff is the management of a company seeking to avoid being taken over. Motives in such cases are probably not at all altruistic and greater judicial circumspection is in order. *Cf.* Missouri Portland Cement v. Cargill Inc., 498 F.2d 851 (2nd Cir.), *cert. denied,* 419 U.S. 883 (1974); *see,* ABA ANTITRUST SECTION, MONOGRAPH NO. 1, THE PRIVATE ENFORCEMENT OF SECTION II OF THE CLAYTON ACT POLICY AND LAW, 29-42 (1977) [hereinafter cited as ANTITRUST SECTION MONOGRAPH I.] Hence absent extreme cases involving violations of other provisions of the antitrust laws, divestiture and related incidental injunctive relief is the preferred solution to an illegal merger problem. Regretably the present state of the law makes it hard to achieve that result.

It is, therefore, unfortunate that the Court did not address the troublesome issue of whether or not divestiture is a permissable form of equitable relief in private cases. The Ninth Circuit in a procrustian reading of the provisions of the law has held that such relief is not available. International Tel. & Tel. Corp. v. General Tel. & Elec. Corp., 518 F.2d 913 (9th Cir. 1975), *accord,* Calmetics Corp. v. Volkswagen of America, Inc., 532 F.2d 674 (9th Cir.), *cert. denied,* 429 U.S. 940 (1976); *see* ANTITRUST SECTION MONOGRAPH I. The circuit court in *Brunswick* held that it was, but that the instant case was not appropriate for such relief. 532 F.2d at 279.

394 Utah Pie Co. v. Continental Baking Co. 386 U.S. 685 (1967).

sult.[395] The plaintiff there established a rule which makes competition less and not more possible, and collected damages from new competitors. In effect that claim, like the one in *Brunswick,* was for something akin to lost monopoly profit. To award damages in that case, then, was to penalize desirable competitive behavior. Even if the substantive conduct is wrongful under Robinson-Patman, it need not give rise to damage liability if the loss suffered is defined as being outside the scope of concern of the law.[396]

A second example of this problem is damage claims by competitors of monopolists charged with predatory pricing.[397] While limit pricing whether above or below marginal cost would seem to be evidence of monopoly power, it proves at most conscious retention of such power. If the monopolist has not otherwise abused its position or if structural or other injunctive

[395] Bowman, *Restraint of Trade by the Supreme Court: The Utah Pie Case,* 77 YALE L. J. 70 (1967).

[396] In that connection consider the contrasting postitions of a plaintiff which sought to enter a market and was discriminated against as opposed to a plaintiff which was an established firm facing a new entrant which used discriminatory methods. In the first case, the concerns of the law for competition could justify damages but in the second damages could discourage competition and injunctive relief could satisfy the concern for fair competition in the local market. Similarly, a bar on future misconduct would seem adequate if both firms were and are viable competitors. Greater emphasis on this kind of damage limitation might permit the limiting of claims under Robinson-Patman into a more competitively acceptable range. *See* Gifford, *Promotional Price—Cutting and Section 2(a) of the Robinson-Patman Act,* 1976 WIS. L. REV. 1945.

[397] In the great debate on predatory pricing that took place recently between Professors Turner and Areeda on one side and Professor Scherer on the other, it became clear that the protagonists were in substantial measure talking past each other. Areeda & Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act,* 88 HARV. L. REV. 697 (1975); Areeda & Turner *Scherer on Predatory Pricing: A Reply,* 89 HARV. L. REV. 891 (1976); Scherer, *Predatory Pricing and the Sherman Act: A Comment,* 89 HARV. L. REV. 869 (1976); Scherer, *Some Last Words on Predatory Pricing,* 89 HARV. L. REV. 901 (1976). Turner and Areeda were apparently concerned with the case of a private damage action in which the evidence showed the price charged by a confessed, but not otherwise unlawful, monopolist was above its marginal costs and so was an economically rational price but this price had the effect of causing loss or failure to some marginal competitor which then sought damages. Turner and Areeda feared that in such a case a broad definition of predatory pricing which focused on the intent or effect of pricing above marginal cost but below the theoretical short run, profit maximizing point would force a lawful monopolist seeking to avoid liability to raise its price to that maximum, and allow entry by firms unable to produce as efficiently as the monopolist with a consequent economic misallocation. Moreover if any of those marginal firms lost sales due to price cutting by the monpolist, they could get damages. Turner and Areeda sought to describe predatory pricing, as a matter of substantive law, in very restrictive terms so that only limited cases would fall within the definition.

Scherer, who was apparently concerned with the problems of proving existence of monopoly and determining its lawfulness, was correctly horrified by this narrow definition of predation recognizing that it would severely limit the proof of violation in § 2 cases if limit pricing above marginal cost was neither evidence of monopoly nor an abuse of monopoly power sufficient to make a not otherwise explicitly lawful monopoly unlawful. Scherer, therefore, showed how such limit pricing could protect and promote monopoly in inefficient ways.

Had the protagonists been less economic and more legal in the analysis they might have sorted out the issues and found less disagreement.

relief is not to be obtained,[398] then it is not clear that such conduct by a monopolist is itself necessarily wrongful (because as Turner and Areeda demonstrate there is good reason to be concerned about the efficiency implications of a contrary conclusion) or should, under those circumstances, make the monopoly position unlawful. Thus the question properly becomes whether and when damages should flow as a result of a monopolist's use of limit pricing. Where the lawfulness of a monopoly is conceded, and the only complaint is its limit pricing, the plaintiff ought not to have damages unless the proof conforms on the Turner-Areeda standard.[399] If the claim is that the defendant is an unlawful monopolist, the plaintiff, in order to establish such wrongful monopolization, needs to show that the market situation would probably have been competitive and could be restored to workable competition.[400] Such a proof, which is very relevant to injunctive and divestiture actions, tends also to establish that absent the unlawful monopoly, price would have been more nearly approximated by the marginal cost of the product than by the monopolistic price. This in turn means that above marginal cost limit pricing even by a unlawful monopolist does not prove damage. Only if prices were below marginal cost should damage liability based on prices alone exist, even in the case of an unlawful monopoly.[401]

A special significance of limiting the damage rights of competitors of monopolists or merging firms is that it makes it more possible to seek effective relief in government cases without concern that a judgment of substantive violation will impose a risk of unreasonable damage claims.

[398] Proof that structural relief is possible on terms not involving any great inefficiency establishes that the monopoly is not economically necessary and is also strong evidence that the monopoly is unreasonable and ought to be unlawful. In such a context, whatever additional proof of wrongfulness is needed to establish the violation ought not to be very substantial and so a showing of limit pricing should suffice. *See* United States v. Aluminum Co. of America, 148 F.2d 416 (2d Cir. 1945); *cf.* United States v. United Shoe Mach. Co., 110 F. Supp. 295 (D. Mass. 1953), *aff'd per curiam,* 347 U.S. 521 (1954).

[399] Perhaps also the only damage is that which is demonstrably caused by the below marginal cost price, so that a competitor whose injury would have resulted even if price were above marginal cost, should not recover.

[400] If such proof is not available, the present monopoly position is a "natural" one and not of itself wrongful even if its achievement or maintenance at some point in time was wrongful.

[401] Thus, for example, one might argue that the Tenth Circuit rightly decided the *Telex* case but not on the grounds asserted. Telex Corp. v. IBM, 510 F.2d 894 (10th Cir. 1975) (per curiam). Assuming that IBM had priced above marginal cost at all times, even if this was done to monopolize unlawfully, *Telex* has not proven any damages since either IBM is a lawful monopoly despite this or if unlawful, its unlawful existence did not cause injury, and in the competitive world, *Telex* would never have existed. This very narrow reading of the *Telex* case is designed to be suggestive of the application of the damage theory being discussed and is not proposed here as a serious analysis of that lengthy case because pricing can be part of a larger and more complex effort to limit or remove competitors; and if that is shown, liability for the damages may exist quite independent of specific price levels. Moreover, once a monopolist is shown to be an unlawful one, the plaintiff as in *Brunswick* will be entitled to future oriented injunctive relief.

C. The Emerging Proximate Cause Issues

As the number and variety of private antitrust suits grows, limits on who may sue whom for what need to be established. The use of legal causation rules whether labeled rules of standing proximate causation duty or statutory construction is one method of achieving such definition. But this approach ought to be used with great care and circumspection, a sense of the history of the evolution of general tort law concepts, and awareness of the experience with specific rules and approaches in other areas of law, a reflection upon the goals of the statutory scheme being implemented by the decisions, and a consideration of alternative ways to achieve the same policy objective are all necessary. It is also important that the courts face squarely that fact that in deciding these cases they are in fact legislating, establishing rules, whose ultimate basis is not primarily in prior decision or statute but in the judicial policy analysis. This in turn means that the analysis ought to be explicit and the crucial considerations fully stated.

Limits other than legal causation exist and can and should be developed more fully. The first is the requirement of causation in fact. It is evident that in many of the cases in the lower courts and in *Hanover Shoe* and even in *Illinois Brick* another basis for decision would have been that the probability of establishing a causal connection between any part of the price paid by a consumer and the antecedent overcharge was unlikely. While finding cause in fact is the province of the jury when that issue is in doubt, the courts are not precluded from insisting that at the pleading stage and at the pre-trial, post-discovery stage there be pleading and evidence that would support a jury in more than mere speculation. Courts use the causation requirement as a method of deciding how many and what kind of cases will get into court;[402] burdens of proof and presumptions can create barriers or let them down in a way that does not foreclose the rare but foreseeable case in which the problem of causation is resolvable.

A second limit on causes of action that needs fuller consideration in relation to the damage issue is that of the substantive rules. It is noteworthy that the effect of both *Sylvania* and *Fortner II,* which were also private damage actions, was to deny damage recovery to plaintiffs not only in those cases but in other similar cases unless the plaintiff made a different substantive showing. Similarly, the *Brunswick* case with its restrictive reading of allowable damages is explicable, perhaps, in terms of the doubts the Court ought to have about the validity and applicability of the substantive theory of liability in that case. Generally by refining the rule of reason and the other substantive standards of antitrust using competitively relevant criteria, the courts can define the substance of the wrong so that they can be more sure when a genuine wrongdoer is before them.

Even with these limiting devices it is still going to be necessary to develop rules of limitation whether in terms of standing or in terms of the property or business interests which section 4 is said to protect. These rules

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[402] Malone, *Ruminations on Cause-in-Fact*, 9 STAN. L. REV. 60 (1956).

will have to define the outer limits of liability in terms both of the potential claimant and the kinds of damages. *Brunswick* rejected the measure of lost monopoly profit and so is in conflict with *Illinois Brick* which was premised on that equation, illustrating the judicial confusion on the proper measure of damages.

Even if damages were better defined to reflect the true interests of the parties, with a residual claimant to any remaining overcharge fund, the courts would still face the problem of deciding which of those with some causal claim ought to be allowed to sue. This is the hard problem of proximate cause. It is not soluble in any final way because the policy interests that underlie the resolution shift in weight and change in character over time. The vice which ought to be avoided and was not in *Illinois Brick* is the promulgation of non-rational distinctions as rules. *Illinois Brick* propounds an ad hoc rule which cannot be generalized usefully to other contexts in which some rule or policy guidance is needed. The use of make weight and empirically questionable arguments together with the failure to identify the relevant issues in the case greatly weaken the utility of the opinion.

Since the antitrust laws are constitutional in character, their development is largely through judicial interpretation. But in trying to make the antitrust laws relevant and useful in the last quarter of the twentieth century, the courts need to avoid the errors of the past. They need to think more fully about the goals they wish to achieve and how those goals are best served. The problem is never going to be solved, but it can be approached in more or less rational ways. *Brunswick* points one way while *Illinois Brick* points the other.

V. Conclusion

The Court is moving in a number of ways to limit the scope of the antitrust laws as they affect business. While clarification, and definition and redefinition of the law is in order, it may be questioned whether the overall approach of the present majority is reasonable or proper. Looking at the music and not the words of the opinions, they reflect a result oriented refusal to employ principled lines of analysis. Thus, the direct-indirect distinction is advanced in one case as useful, but title passage, a similar distinction, is rejected in another as too mechanical. Market power is analyzed in one case and ignored in a second. A "rule of reason" is announced without being defined. State courts are freed to wreak havoc on competition but the first amendment is found to contain an implicit mandate for economic competition so that regulation not liked by the majority can be voided. The net effect is that the antitrust defendant wins and the damage plaintiff loses or is obliged to prove a good deal more. But the states may not bar lawyer advertising and price competition. The policies are inconsistent, the rationales unconvincing. Professor Posner may after all be right: the Court may not know what it is doing.[103]

[103] Posner, *supra* note 25.