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DOMINANT FIRM DISTRIBUTION: STRIKING A BETTER BALANCE

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I. INTRODUCTION

As an antitrust community we have long been of two minds about monopoly. On the one hand, the evils of monopoly are widely recognized: restricted output, higher prices, perhaps diminished incentives to pursue cost-cutting measures and innovation, and increased incentives to pursue rent-seeking strategies, as with predation.[1] As Judge Learned Hand remarked in *Alcoa*:

> Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone.[2]

Yet, we also are aware of the potential dangers of too readily condemning the actions of monopolists for fear that legal standards will erode the very incentive that drove them to compete hard and succeed in the first place. As Judge Hand observed in *Alcoa*, "[t]he successful competitor, having been urged to compete, must not be turned upon when he wins...."[3]

Identifying operative legal rules that resolve the obvious tension between these two competing values has proven to be an elusive goal. Some of the classic cases, such as *Alcoa*, *United States Steel*,[4] *American Tobacco*,[5] and *Grinnell*,[6] approach the task in the context of monopoly "acquisition." Others, however, focus on monopoly "maintenance," as was true in *Standard Oil*,[7] *Lorain Journal*,[8] *Otter Tail*,[9] *United Shoe Machinery*,[10] and *Aspen Skiing*.[11] Cutting across both groups, however, is a distinct subset of cases in which dominant firms responded to new or expanded

competitive challenges through new, reworked, or refined "distribution strategies," which were used either to secure or perpetuate monopoly positions. *Standard Oil* and *Alcoa*, as well as *Lorain Journal*, *Otter Tail*, *United Shoe Machinery*, *Aspen*, and *Kodak*[12] all can be fairly and usefully viewed as such "distribution" cases.

This paper explores the intersection of these two bodies of antitrust law: distribution and monopolization. The law of distribution and marketing practices - largely a creature of Section 1 of the Sherman Act,[13] Section 3 of the Clayton Act,[14] and Section 2(a) of the Clayton Act, as amended by the Robinson-Patman Act[15] – intersects with the law of monopolization – a product of Section 2 of the Sherman Act[16] – when dominant firm distribution strategies are challenged. Because the threshold requirement of a claim of monopolization is monopoly power, and because the law of distribution largely presumes that when market power is present, distribution strategies can harm competition, challenges to dominant firm distribution strategies pose obvious, immediate and significant competitive concerns.

Indeed, in a series of recent cases in the courts of appeals, dominant firm distribution strategies have come under increased scrutiny. Simultaneously, however, antitrust enforcers, counsel to dominant firms, and commentators have sought to use these and other recent Section 2 cases to resolve Section 2's underlying tension by tipping the balance decidedly in favor of greater tolerance of aggressive dominant firm conduct that excludes. In briefs, articles, speeches, and public presentations, they have vigorously argued that the law should tread lightly on dominant firm distribution strategies lest it over-deter "efficient" practices.

By focusing on the Section 2 distribution strategy cases, however, I will demonstrate that this effort is at best troubling from the point of view of protecting competition as a process, and is

primarily based on non-empirical assumptions about the assumed benefits of dominant firm behavior. A Section 2 standard that is animated by greater tolerance of aggressive dominant firm distribution strategies that exclude will, therefore, very likely lead to under-deterrence, with uncertain, but very likely substantial, adverse consequences for the nascent competition that is often its target.

In Part II, I briefly examine the well known current legal framework for both monopolization and distribution. In Part III, I more closely examine seven recent cases from the federal courts of appeals, all of which focused on dominant firm distribution strategies. I argue that there are observable patterns in these cases, and that despite some controversy, these decisions are largely unexceptionable, i.e., they have reached consistent and reasonable results.

Part IV turns to the current battleground – the exclusionary conduct "definition" war. In it, I will seek to demonstrate how a change of definition is unwarranted by any evident outbreak of "bad" cases, i.e. false positives that could result in over-deterrence. Quite to the contrary, some of the approaches being advocated could seriously undermine Section 2's vitality as a shield that guards the competitive process. Part V concludes by offering some suggestions for refining rather than displacing the developing approach in the courts, by better integrating the substance of monopolization law with a more coherent procedural framework under Section 2.

II. THE CURRENT LEGAL FRAMEWORK FOR EVALUATING DISTRIBUTION STRATEGIES

A. THE CENTRALITY OF MARKET POWER IN THE MODERN LAW OF DISTRIBUTION AND MARKETING

Traditionally, distribution strategies have been addressed as "vertical agreements," subdivided based on their tendency to restrict "intrabrand" or "interbrand" competition. Until 1977,

the U.S. Supreme Court addressed both kinds of distribution strategies with hostility, even per se condemnation. This was so, for example, with minimum resale price maintenance,[17] maximum resale price maintenance,[18] non-price restrictions,[19] and tying[20] for many years. The Court treated exclusive dealing, which was never subjected to a per se rule, relatively harshly, even when there was only a modest degree of interbrand "foreclosure."[21]

In these early cases, the Court sought to justify its hostility to intrabrand restraints based on notions of property and contract rights, as well as fairness grounds.[22] But since the Supreme Court's watershed 1977 decision in *Sylvania*, these traditional concerns have for the most part given way to a focus on competition and competitive effects.[23] Although the law remains harsh in its treatment of intrabrand price restraints, it has been transformed in the area of non-price restraints.

Sylvania justified this change of heart by recognizing that vertical intrabrand restraints can enhance interbrand competition and therefore often serve legitimate competitive goals. Specifically, the Court found that they can do so by: (1) inducing competent retailers to carry new products, (2) inducing retailers to promote existing products more zealously; and (3) defeating market imperfections, such as free riding, which might impair the first two.[24] These critical justifications for non-price intrabrand restraints were all tied to a broader notion: that interbrand competition was the "primary concern of antitrust law," and that, as a consequence, restraints on intrabrand competition that enhance interbrand competition should be evaluated under the rule of reason.[25] The rationale was straightforward: so long as interbrand competition is robust, intrabrand restraints cannot be used to exercise market power.[26]

This created something of an inherent contradiction: to work as envisioned, intrabrand restraints would have to lead to somewhat higher absolute prices. Indeed, their very purpose was to

relieve the downward pressure on price that might ensue from discounting by competing dealers who did not provide the desired services.[27] By doing so, however, they would encourage the provision of services and promotional efforts, which in turn would lead to increased output and hence lower prices as interbrand competition intensified. Provided there is sufficient interbrand competition, the manufacturer would have to continually fine tune its distribution strategy to determine the optimal level of services. If it provided too little, its prices might be more competitive, but its product would not necessarily be adequately promoted and it would forgo sales. On the other hand, if it required too much, and hence its price rose to uncompetitive levels, it would lose sales to its rivals. Interbrand competition thus would serve as a modulator for both insufficient and excessive promotion and services that were unresponsive to consumer demand.[28]

The absence of interbrand market power, then, was a critical assumption in *Sylvania's* analytical framework. Indeed, if that assumption was incorrect in a specific case, *Sylvania's* rationale would be inapplicable. In a market where a firm possesses interbrand market power, intrabrand competition may provide the only significant source of competition, such as downward pressure on price. Its elimination through the use of non-price restraints, therefore, could facilitate the exercise of market power. In truth, however, *Sylvania* offered little guidance as to how the rule of reason should be applied in such circumstances.[29] And there has been only one reported case since *Sylvania* that concluded, based on the defendant supplier's market share, that its use of intrabrand restraints was unreasonable.[30]

For purposes of evaluating dominant firm distribution strategies, however, *Sylvania's* analytical framework presents a challenge. By definition, a "dominant" firm already possesses interbrand market power. Hence, in the case of dominant firm distribution strategies, protecting

"intrabrand" competition may become essential, precisely because interbrand competition is not a viable check on the exercise of market power.[31] If that is the case, several critical questions arise. For example, should the law recognize a presumption that dominant firms are disqualified from utilizing vertical intrabrand non-price restraints as part of their distribution strategies? If not, on what ground(s) can they be justified, and how can their liberal use be squared with *Sylvania*? Finally, how can Section 1 and Section 2 standards be harmonized around *Sylvania's* core values and assumptions?

As noted above, the second traditional area of antitrust concern in distribution and marketing involves arrangements that affect "interbrand" competition. Treatment of interbrand restraints is complicated by several factors. First, the principal competitive concern with intrabrand restraints is their ability to facilitate the direct exercise of market power by the supplier – "collusive effects." In contrast, interbrand restraints can raise concerns about exclusionary as well as collusive effects.[32] Second, the economics of interbrand restraints is arguably more complex than that of intrabrand restraints, and has been characterized by intense and long-standing academic and judicial debate. Third, whereas intrabrand restraints are largely evaluated under Section 1 of the Sherman Act, alone, interbrand restraints have been evaluated under Sections 1 and 2 of the Sherman Act, as well as Section 3 of the Clayton Act, which incorporates the Clayton Act's "incipiency" language.[33] A final factor that complicates the evaluation of interbrand restraints today is a relatively contemporary development. Although in the past these kinds of arrangements were typified by tying, exclusive dealing, outputs and requirements agreements, today the category has been broadened to include various kinds of promotional strategies that are designed to secure some degree of exclusivity, such as market share and loyalty discounts, and product bundling, which also may be accompanied by a

discount.[34]

As noted above, because the courts early recognized the competitive utility of exclusive dealing, it was never subjected to the per se rule, as was tying.[35] Nevertheless, in early cases like *Standard Stations*, courts treated exclusive dealing with skepticism, and readily condemned exclusive dealing contracts based on what today would appear to be a very low threshold of "foreclosure."[36] The modern trend, which began with *Tampa Electric*, demands far more evidence of injury to competition before exclusive dealing warrants condemnation. Today, moving beyond the Supreme Court's "foreclosure" based framework,[37] courts will typically inquire into the defendant's market power, evaluating such evidence as continued access to alternative sources of supply or distribution, the duration of the exclusive dealing arrangement, conditions of entry, and evidence of actual anticompetitive effects. As a consequence, it has become quite difficult to prevail in an exclusive dealing challenge.[38] Even in a tying case, which may in some circumstances be judged under a per se standard, market power in the tying product is essential.[39]

Hence, both exclusive dealing and tying have evolved similarly, and have now come close to converging, at least in practice. Simply put, in order to raise serious antitrust concerns, a plaintiff challenging a vertical interbrand restraint must demonstrate that the defendant possesses significant market power. As noted above, that is also the case for intrabrand restraints. The common question in almost any viable challenge to a vertical practice today, therefore, is "does the defendant have market power?" By definition, dominant firms do.

B. The Traditional Monopolization Paradigm

The basic framework for Section 2 monopolization cases has remained stable over the last 50 years.[40] The familiar concepts set forth in *Alcoa*, and later reduced to a formula in later cases,

requires proof of (1) monopoly power; (2) willfully acquired or maintained. Consistently interpreting and applying this formula, however, has proven to be more challenging than a simple restatement of the rule would suggest.

1. *Monopoly Power*

Under *Cellophane*, monopoly power was defined as the "power to control prices or exclude competition."[41] Traditionally, such power was established circumstantially through inferences drawn from high market shares. Hence, classic cases like *Alcoa* and *Cellophane*[42] paid great heed to market definition, which could well determine whether the court would or would not infer the power necessary to move on to an analysis of conduct.

Once a market was defined, the next step was to calculate market shares and determine whether the defendant's share was sufficient to infer the requisite monopoly power. Judge Hand's rules of thumb in *Alcoa* – 33% or less, insufficient; 64% doubtful; 90% certainly, were synthesized from prior case law,[43] such as *Standard Oil*,[44] *American Tobacco*,[45] *International Harvester*,[46] *United States Steel*,[47] *Standard Oil of Indiana*,[48] and *Appalachian Coals*.[49] *Cellophane* itself later appeared to suggest a threshold of about 70% for viable claims of monopoly power.[50]

Although proof that a firm possesses a very substantial share of a properly defined relevant market remains a touchstone of monopolization law, such proof is circumstantial, not direct evidence of power. For the last two decades, courts have increasingly focused on *direct* evidence of the exercise of market power for purposes of both Sections 1 and 2 of the Sherman Act. In *NCAA*,[51] and *Indiana Federation of Dentists*,[52] which both arose under Section 1, the Supreme Court declared that market share evidence was merely a "surrogate" used to infer market power, from which in turn anticompetitive effects could be inferred. Such a surrogate is unnecessary when there is significant

direct evidence of actual anticompetitive effects, i.e., evidence that market power has actually been exercised.[53] The Court repeated this reasoning in *Kodak*, a case that involved claims under both Sections 1 and Section 2,[54] and it has been recently endorsed by the FTC.[55]

More recently, the lower courts have recognized that the principle that direct evidence may obviate the need for the circumstantial has equal application to the monopoly power element of Section 2.[56] The strongest case for a finding of monopoly power, however, is established when the circumstantial and direct evidence appear to be aligned. This was the case, for example, in *Microsoft*. Although the D.C. Circuit noted that direct evidence is not a requirement for a finding of monopoly power, it credited both circumstantial evidence, in the form of market shares calculated in a properly defined relevant market, and more direct evidence, such as the fact that Microsoft had actually exercised its market power, in reaching its conclusion to affirm the district court's finding of monopoly power "in its entirety."[57]

This trend in the case law has great significance for the analysis of dominant firm distribution strategies. Although the Court has continued to represent that surely what is needed to establish "monopoly" power is something more than what is required to demonstrate "market" power,[58] the difference seems at best to be one of degree, and is more readily apparent in a world of market shares and inferences. When direct evidence is used, "market" and "monopoly" power may be difficult to distinguish as a matter of law, and economists generally do not recognize the two as distinct.[59]

The critical role of circumstantial and direct evidence has emerged not only in cases of collusive effects, but in exclusionary effects cases,[60] as well as in merger analysis.[61] In such cases, evidence of actual anticompetitive effects may be sufficient to establish the "monopoly" power element of a Section 2 offense. When such evidence is present, the various elements of offenses

under Section 1 and Section 2 collapse into a unitary inquiry. Assuming no issues of causation are present, evidence that conduct has in fact diminished competition, such as lower output and higher prices, and perhaps lower quality or less consumer choice, will tend to establish both the power requirement of the offense and anticompetitive effects.[62] In the case of conduct that excludes, the question will be whether actual "exclusion" is the equivalent of "exclusionary."

2. *"Exclusionary" Conduct*

As noted above, by attaching the label "willful acquisition or maintenance," the courts have sought to draw a distinction between merits and non-merits based competition that excludes. Over time, however, efforts to more specifically differentiate the two have divided into two lines of cases: price predation and non-price exclusionary conduct.

a. *Price Predation*

Today's law of predatory pricing is shaped largely by the Supreme Court's decisions in *Matsushita*[63] and *Brooke Group*.[64] In these two cases, the Supreme Court developed a two part test for predatory pricing. To be actionable under the antitrust laws, such pricing must be (1) below some appropriate measure of cost;[65] and (2) it must be probable that the alleged predator will be able to recoup its losses through the later exercise of market power.[66] This paradigm assumes that successful predatory pricing is a two step process. In stage one, the "short run," the predator lowers its price in order to exclude its rivals. In stage two, the "long run," the predator, having vanquished its rivals, will be in a position to exercise market power and hence "recoup" its short run losses.

The presumption that such strategies are generally "implausible" follows from the supposition that significant losses are certain, yet recoupment is not. Indeed, assuming the predator cannot price discriminate, as the strategy succeeds and the predator's market share expands, so will

its losses. To be in a position to recoup those losses, the predator will have to raise its price long enough and high enough to recoup its losses and then some, without inviting entry.[67]

Critics of harsh predatory pricing rules thus concluded that predatory pricing is "rarely tried, and even more rarely successful."[68] The more likely explanation of aggressive pricing behavior, this line of reasoning goes, is that the alleged predator is engaged in competition on the merits.[69] Rarely, if ever, could a firm incur the kind of losses necessary to sustain a predatory pricing plan and then exercise market power for long enough to recoup its losses. Hence, a plaintiff, public or private, who challenges conduct as exclusionary must make a threshold showing of the claim's economic "plausibility."[70] As is discussed at greater length, *infra*, this skepticism of the likely success of exclusionary practices has expanded in some circles to encompass non-price conduct, as well – even though those practices may not involve the kind or degree of loss associated with predatory pricing.[71]

Adoption of this framework was largely influenced by sharp academic criticisms of prior case law and commentary.[72] Those critics argued that low prices are of the essence of competition. Hence, antitrust rules that punish low prices would tend to lead to false positives and "over-deter" desirable competition. In the end, stringent rules against price predation, therefore, would harm competition and consumers.[73] Critics also pointed out the anomalous remedial problem in predatory pricing cases: court-ordered higher prices.[74]

The import of the *Matsushita-Brooke Group* framework is now well-established: above cost pricing that excludes is by definition desirable "competition on the merits." Moreover, even below cost pricing will be presumed to be "competition on the merits" if the plaintiff cannot establish that the alleged predator will probably be able to recoup its losses and then some, i.e., that it will be able to exercise market power for long enough, and to a sufficient degree, to make the strategy profitable

in the long run.

Although the *Matsushita-Brooke Group* test has been criticized as unduly permissive of the scope of above-cost pricing conduct that excludes,[75] it is now well-entrenched, and has proven to be very difficult to satisfy. As a consequence, since *Matsushita* there have been no reported cases of successful challenges to alleged predatory pricing behavior.[76] A legitimate question remains, however, whether this quest to avoid over-deterrence has led to under-deterrence of pricing strategies that unreasonably and unnecessarily exclude rivals.[77] Also debatable is whether wholesale importation of the predatory pricing approach to non-price exclusionary conduct would be a good fit given its characteristics, or a very poor fit likely to lead to significant under-deterrence.

2. *Non-price Exclusionary Conduct*

Non-price exclusionary conduct, on the other hand, has been defined by *Aspen*, *Kodak*, and to some degree the Supreme Court's recent decision in *Verizon*.

Justice Stevens' majority opinion in *Aspen* sought to synthesize a contemporary definition of "willful acquisition or maintenance" from the Court's prior case law and from the principal commentators, notably Professors Areeda and Turner, and Judge Bork. In its penultimate passage, the Court reasoned:

> The question whether Ski Co.'s conduct may properly be characterized as exclusionary cannot be answered by simply considering its effect on Highlands. In addition, it is relevant to consider its impact on consumers and whether it has impaired competition in an unnecessarily restrictive way.[32] If a firm has been "attempting to exclude rivals on some basis other than efficiency,"[33] it is fair to characterize its behavior as predatory. It is, accordingly, appropriate to examine the effect of the challenged pattern of conduct on consumers, on Ski Co.'s smaller rival, and on Ski. Co. itself.[78]
>
> [32] "Thus 'exclusionary' comprehends at the most behavior that not only (1) tends to impair the opportunities of rivals, but also (2) either does not further competition on the merits or does so in an unnecessarily restrictive way." 3 P. Areeda & D. Turner,

Antitrust Law 78 (1978).

[33] Bork [The Antitrust Paradox] 138.

From the first quoted sentence, it seems clear that in the Court's view "exclusion" is not the same as "exclusionary." Competition on the merits and exclusionary conduct alike will produce winners and losers. So to judge whether conduct that excludes is exclusionary, the majority offers these guiding questions:

1) What was the impact of the conduct on consumers?

2) What was the impact of the conduct on the alleged predator?

3) What was the impact of the conduct on the rival?

Inherent in this approach is a framework that involves shifting burdens of production: the plaintiff demonstrates exclusion or impairment of rivals and consequent actual or likely impact on consumers. The defendant must then come forward with "business justifications." The approach is suggestive of a kind of "balancing," at least when the defendant can meet its burden of production and presents evidence of legitimate purposes. Aspen Ski Company, however, failed to meet its burden, so the case offers no guidance on how such a "balancing" would be implemented. As will be discussed, *infra*, the D.C. Circuit's opinion in *Microsoft* tried to build on this implicit *Aspen* framework, making it more explicit.[79]

Upon a more careful read of the case, additional specificity can be associated with each of the three questions it posed.

Impact on Consumers. If the antitrust laws are to realize their potential as a "consumer welfare prescription,"[80] evidence of consumer harm should be given great weight in identifying conduct that violates the Sherman Act. In both *Aspen* and *Kodak*, the Court concluded that

consumers were clearly worse off as a consequence of the defendants' conduct. In *Aspen*, consumers lost a product package that they had demonstrated an affinity for over time. Hence, product quality and consumer choice were compromised.[81] Moreover, as in *NCAA*,[82] the changed product was no longer responsive to consumer demand – further evidence that the defendant was exercising market power. Similarly, in *Kodak*, there was evidence that Kodak's aftermarket service was of lower quality and provided at higher prices.[83]

Surely there would also be situations where consumer harm could be readily inferred from the nature of the dominant firm's conduct and its dominant position.[84] To hold otherwise would undermine the Sherman Act's ability to deter conduct that harms competition. Moreover, in contrast to predatory pricing, which arguably benefits consumers in the short run, it is hard to see how the exclusion of rivals can ever be affirmatively "good" from the point of view of consumers, unless it is accomplished through superior efficiency. At best, it might have a neutral effect – i.e., provided there is sufficient remaining competition, the elimination of a single rival may have little effect on consumers. In any event, before a final judgment can be reached about the legality of conduct that both excludes rivals and does not clearly benefit consumers, evidence of justification sufficient to meet a burden of production should be required from the dominant firm.

Impact on Rival. Specifically, the Court asked whether the predator's conduct impaired the prey's competitive opportunities in an "unnecessarily restrictive" way. Here the inquiry focuses on the actual effects of the conduct on the prey and whether the conduct was more restrictive than necessary to achieve the dominant firm's legitimate purposes, assuming it can establish that it had any. The first point - effects on the prey – might include actual and total exclusion, as it did in *Kodak*, or impairment, in the form of raising rivals' costs,[85] or, as in *Aspen*, reducing rivals'

revenues. The "unnecessarily" qualification, connotes something akin to the "less restrictive means" test used in the final stage of the analysis under the rule of reason.[86]

Impact on Predator. *Aspen* placed great weight on the fact that Ski Company "did not persuade the jury that its conduct was justified by any normal business purpose."[87] Similarly, in *Kodak*, the court concluded that "none of Kodak's asserted business justifications...are sufficient to prove that Kodak" was entitled to judgment as a matter of law on Image Technical's Section 2 claim. Indeed, the evidence seemed to directly contradict some of those assertions.[88]

For the *Aspen* Court it was also significant that "[t]he jury may well have concluded that Ski Co. elected to forego...short run benefits because it was more interested in reducing competition in the Aspen market over the long run by harming its smaller competitor."[89] As will be discussed in Part III, *infra*, this passage recently has taken on greater meaning in light of efforts to urge the courts to embrace a "sacrifice" standard for defining exclusionary conduct.[90] It need not and should not be read, however, as *requiring* a showing of sacrifice. Rather, it stands for the more simple proposition that sacrifice by a dominant firm, coupled with lack of legitimate business justifications, will often prove sufficient to support a finding that dominant firm conduct is "exclusionary:" "Thus the evidence supports an inference that Ski Co. was not motivated by efficiency concerns and that it was willing to sacrifice short-run benefits and consumer goodwill in exchange for a perceived long-run impact on its smaller rival."[91]

Structuring the Inquiry. *Aspen's* framework had broader meaning than the narrow holding in the case. More so perhaps than any Section 2 decision from the Court since *Alcoa*, *Aspen* attempted to outline a structured approach to applying Section 2, one that implicitly embraced a methodology for allocating burdens of production. Once the plaintiff had demonstrated actual adverse effects on

both consumers and the targeted prey, it was incumbent upon the predator to justify its conduct – and it failed to do so in both cases. Weighed on the "scale of competition justice," there was nothing on the predator's side to counteract the damage that had been done to rivals and consumers.

But *Aspen* does not directly answer the question: what if the defendant had in fact offered and supported a cognizable justification? In other words, what is the proper approach to assessing dominant firm conduct under Section 2 when it produces *both* anticompetitive effects on rivals and consumers (i.e., inefficiencies) *and* procompetitive effects for the alleged predator (i.e., efficiencies)? Nothing in *Aspen* supports the view that *any* evidence of justification will necessarily rebut the inference of harm that arises from injury to consumers and rivals. As is the case under Section 1, some kind of "weighing," "comparing" or "balancing" might need to be done, and it would most likely need to be done by the jury.[92]

The combined impact of *Aspen* and *Kodak*, therefore, was to bring Section 2 closer to Section 1, and perhaps Section 7 of the Clayton Act, in approach. This important insight was recognized by the D.C. Circuit in *Microsoft*, where it proposed a four part test for structuring the Section 2 inquiry based not only on *Aspen* and *Kodak*, but on a careful consideration of a full range of Supreme Court and court of appeals decisions addressing Section 2 over time. The test first requires the plaintiff to establish "anticompetitive effect," which also harms "competition." If it does so, the burden of production shifts to the defendant, who can offer evidence of a "procompetitive justification." Only at that point, if the justification stands "unrebutted," must the plaintiff "demonstrate that the anticompetitive harm outweighs the procompetitive benefit."[93]

This important framework, derived as it was from a synthesis of the key cases on price and non-price exclusion, has been largely overlooked by the courts – and that is unfortunate. Its

significant virtue lies in its ability to translate Section 2's economic concerns into an operative legal framework that is compatible with judicial process and that addresses the essential issue of burden allocation. As was true in *Microsoft*, itself, it does little to alter the approach when the evidence is lopsided. Indeed, with respect to virtually all of the specific acts evaluated in *Microsoft*, the court of appeals found anticompetitive effect and no procompetitive justification and hence affirmed the district court's conclusion that those acts violated Section 2.[94] With respect to a few acts, the court found the government's evidence of anticompetitive effect to be insufficient and reversed,[95] and when Microsoft did proffer a non-pre-textual and truly procompetitive justification, the court found that the plaintiff failed to rebut that showing and also reversed.[96] So in truth, the court did not reach Step 4 – "weighing" anticompetitive effect and justification.

Yet, as will be discussed *infra*, the D.C. Circuit's core insight – that cases involving both inefficiency and efficiency must be assessed through some kind of balancing process – addresses the most intractable issue under Section 2, and perhaps all of antitrust, today. Because it did not proceed to apply that balancing step, however, it offers little specific guidance on how that balance should be struck.

C. Recognizing "Dominant Firm Distribution"

The law of distribution and marketing practices intersects with the law of monopolization when dominant firm distribution strategies are challenged. Because the threshold requirement of a claim of monopolization is monopoly power, and because the law of distribution largely presumes that when such market power is present distribution strategies can harm competition, dominant firm distribution strategies may pose significant competitive concerns. Indeed, based on everything we understand about the law and economics of these two fields, such cases should be subject to careful

scrutiny.

Instead, there has been a concerted effort to persuade the courts of quite the opposite: that the law should tread lightly on dominant firm distribution strategies lest it over-deter "efficient" practices. The various tests that have been proposed to move the law in that direction tend to emphasize potential efficiencies while downplaying – even dismissing – evidence of actual competitive harm. In doing so, these advocated approaches presume a substantial threat of false positives and hence over-deterrence from the current state of the law, even though there is little or no evidence to support that fear in recent judicial treatments of dominant firm conduct. This difference of opinion over the treatment of dominant firm distribution strategies can be attributed to a failure to attend to the need to integrate the monopolization and distribution cases, perhaps some over-zealous advocacy, and some persistent differences of opinion about the economic plausibility of exclusionary strategies.

To further explore these issues, the next section profiles seven recent court of appeals decisions that lie at the intersection of distribution and monopolization law.

III. DOMINANT FIRM DISTRIBUTION IN THE COURTS

Like all firms, dominant firms active in markets that involve differentiated functions have to make certain choices about inputs, production, packaging, marketing, and distribution. For the most part, of course, these kinds of decisions do not pose serious antitrust concerns. But precisely because these firms are dominant, distribution strategies that significantly impair or exclude rivals have led to antitrust challenge and litigation, both public and private. The issue is this: to what degree should antitrust constrain the distribution strategies a dominant firm can employ, especially when they are adopted in response to competitive challenges from its much smaller rivals?

A. An Overview of the Cases

Seven recent cases from the courts of appeals illustrate some of these issues.[97] In every instance, the dominant firm employed a "distribution strategy," and in all but one instance it did so by marketing its product through some kind of distribution chain, i.e., by cooperating to some degree with upstream or downstream partners. And in every case, the distribution strategy was focused on and/or had its principal impact upon interbrand competition.[98] These distribution strategies can be separated into roughly three categories, but as will be demonstrated, for antitrust purposes it is unclear whether these categories are helpful:

(1) Pricing

- above cost discounts, simple rebates, and related behavior
- predatory pricing

(2) Non-Price

- exclusive dealing
- tying and bundling

(3) Mixed

- loyalty and market share discounts, rewards, and other incentives
- capacity shifting

Certain patterns are evident in these cases. First, although the mechanism varied to some degree from case to case, in each the challenged strategy was designed to, and was challenged for, securing a degree of *exclusivity* for the dominant firm. Also, in each case, that strategy went beyond simply trying to defeat rivals in the market place.[99] Second, each case involved allegations that the exclusivity pursued by the dominant firm impaired the competitive opportunities of its rivals and either defended or enhanced the defendant's market power.[100] Third, market shares still matter a

great deal and may even predict outcomes. In each case in which the defendant was found to have a market share of 75% or more in a properly defined market, the plaintiff won.[101] When the definition of the market was successfully challenged, however, or where the defendant's share was found to be below that threshold, the defendant prevailed.[102] The fourth and less clear pattern was the degree to which the definition of "exclusionary" mattered. Some cases involved raising rivals' costs,[103] whereas others involved reducing rivals' revenues.[104] Some involved near costless strategies,[105] whereas others involved some "sacrifice," i.e. cost.[106] Some of the challenged practices benefitted consumers in the short run,[107] whereas others either had no impact or arguably harmed consumers.[108] Finally, in every case in which the plaintiff prevailed, it appeared from the court's discussion and analysis that, contrary to the cornerstone assumption of *Sylvania* concerning intrabrand restraints, the *interests of rivals and consumers were aligned*, i.e., both rivals and consumers would be worse off in the long run as a consequence of the dominant firm's distribution strategy.[109]

B. Common Analytical Elements and Outcomes

The plaintiffs secured significant victories in only three of these cases – less than half – *LePage's*, *Conwood*, and *Microsoft*, and only one of the cases that resulted in unequivocal defense victories went to trial.[110] Defendants prevailed on summary judgment in *AMR*, *Pepsico* and *Virgin Atlantic*, and on judgment as a matter of law in *Concord Boat*.

As noted above, several factors appeared to be of critical importance in the courts' analysis. When plaintiffs prevailed – in *Conwood*, *LePage's* and *Microsoft* – there was sufficient evidence to support findings that: (1) the defendant had very substantial monopoly power; (2) its conduct resulted in actual anticompetitive effects on rivals and consumers; (3) conditions of entry were difficult, which in turn reenforced the finding of both market power and anticompetitive effects; and

(4) the defendant had either failed to offer evidence of any procompetitive justifications for its actions, or failed to support its stated justifications with evidence.

The defendants conceded their monopoly power in *LePage's* and *Conwood*. Although it was contested in *Microsoft*, the defendant's monopoly power was readily apparent, and the circumstantial and direct evidence were aligned. In other words, the finding of power was supported by both circumstantial evidence, i.e. market shares, and direct evidence, i.e. the defendant's actual exercise of market power, and these two kinds of evidence were reenforcing of each other.[111] Indeed, in all three cases, the defendant had enjoyed its dominant position for quite some time, and in all the challenged conduct was undertaken as a specific response to a new competitive challenges to that dominance.

As to effects, there was not only significant evidence of actual exclusion, but there was also evidence sufficient to support a finding of actual or probable consumer harm.[112] Third, as is the case with merger analysis, each court deemed it important to evaluate conditions of entry. In each instance, the court found barriers to entry, which meant that the defendant's market power was likely to prove durable, and hence the market was unlikely to correct for the anticompetitive effects observed.[113] Finally, in every plaintiff victory, the defendant either failed to offer any justifications for its actions, or failed to support stated justifications with evidence.[114] Significantly, because the evidence was almost uniformly lopsided in favor of the plaintiff, none of the three cases required the court to "balance" pro- and anti-competitive effects in order to reach its conclusion.[115]

In contrast, the cases in which defendants prevailed presented quite differently. For example, in *Pepsico* and *Virgin Atlantic*, the court found a lack of evidence of monopoly power that was fatal to the plaintiffs' claims.[116] In *Concord Boat*, the court found an absence of exclusivity, and hence no actual adverse effects on rivals or consumers.[117] Significantly, although some courts credited

defendants' assertions of business justifications, no defendant prevailed by establishing business justifications where the court also found substantial anticompetitive effects. Either the burden of production never shifted to the defendant or, if it did, the defendant either lost, as noted above, for lack of such evidence, or won because the anticompetitive effect was deemed slight.

A stark factor that also appeared to affect outcome was "characterization." When the court viewed the conduct as "price predation" it applied *Matsushita* and *Brooke Group* and the defendant prevailed.[118] On the other hand, when the court viewed the conduct as non-price exclusionary behavior, it applied *Aspen* and *Kodak* and the plaintiff prevailed.[119] The importance of characterization was especially apparent in *AMR* and *Virgin Atlantic*. In both cases, once the courts categorized the challenged conduct as "predatory pricing," they focused on the plaintiffs' evidence that the defendant's pricing was below cost. Finding that it was not, judgment was entered for the defendants.[120]

There was, of course "another side" to each of the seven cases. In the plaintiffs' victories, the defendants vigorously contested many of the courts' findings, as did the plaintiffs in the defendant victories. But if we are to accept the resolutions following appellate review, these cases as a group hardly present a very controversial set of applications of Section 2.[121] There is, in short, little evidence here of either substantial over or under-deterrence, and while one could quibble with the consistency and quality of the reasoning in some of these cases, they can as a general matter be reconciled.[122]

IV. THE CURRENT BATTLEGROUND: DEFINING "PREDATORY/EXCLUSIONARY" CONDUCT

A. ANTITRUST AS NARRATIVE

Antitrust law has surely benefitted in the last generation from an infusion of economic sophistication. But economics does not obviate the influence of values, and, as is true elsewhere in the law, the legal rules supported by economics also may be influenced by more intangible, ideological and attitudinal, as well as institutional factors.[123] How one strikes the balance between error costs, between over and under-deterrence, for example, may be more a product of viewpoint than hard economics.

One such non-economic factor is literary: antitrust is a narrative. To illustrate the point, consider how antitrust law once aggressively sought to protect individual dealers, viewing them as bulwarks against impersonal corporate dominance, and wrapping them in "rights," such as liberty of contract and freedom from restraints on alienation.[124] In this "narrative," suppliers were viewed with suspicion, and dealers with some degree of trust.

Sylvania did not simply alter the economics of vertical restraints, therefore, it altered the distribution narrative.[125] Suppliers were no longer viewed as impersonal and bullying corporate giants. To the contrary, a critical element of *Sylvania's* rationale was the view that manufacturers' interests were in fact aligned with those of consumers.[126] This re-casting of the manufacturer, however, was but one step in the process of re-writing the narrative of vertical restraints. The second step concerned the dealer. The traditional image of dealers as hard-working, autonomous pillars of the local business community, who were entitled to certain rights and freedoms, was supplanted by a very potent and decidedly derogatory counter-image: the dealer as "free-rider."[127] Although one could certainly argue that this change in the narrative was a consequence of new economic insights, the ability of those insights to displace the previous narrative owed in large part to the power of its portrayal of the manufacturer as aligned with the consumer and the dealer as someone less worthy of

protection. In a real sense, the narrative amplified the insights and effects of the economics, making them more powerful and sweeping than they otherwise might have or should have been. Indeed, the actual record in any given case can become subservient to the narrative, rather than the narrative adapting to the record.[128]

Narrative is, of course, an integral part of the original fabric of antitrust. In one of his most well known orations in the Senate urging adoption of the Sherman Act, Senator John Sherman launched the narrative that came to dominant antitrust for much of its first century. In that narrative, large corporate enterprises – specifically the trusts – were inclined by their very nature to exploit consumers, predate against rivals, and even undermine the very foundations of political democracy:

> The sole object of [a trust] is to make competition impossible. It can control the market, raise or lower prices, as will best promote its selfish interests, reduce prices in a particular locality and break down competition and advance prices at will where competition does not exist. Its governing motive is to increase the profits of the parties composing it. The law of selfishness, uncontrolled by competition, compels it to disregard the interest of the consumer....
>
> ...If we will not endure a king as a political power we should not endure a king over the production, transportation, and sale of any of the necessaries of life. If we would not submit to an emperor we should not submit to an autocrat of trade, with power to prevent competition and to fix the price of any commodity....[129]

Although there has been much debate about the particulars of antitrust law in its century plus of existence in the United States, certain principles that share common ancestry with Senator Sherman's narrative remain constant. Consistent with that tradition, the Sherman Act has been variously labeled the "Magna Carta of free enterprise,"[130] "a comprehensive charter of economic liberty,"[131] and a "charter of freedom."[132]

1. *Monopolists and Their Rivals as Literary Figures*

This traditional narrative was built in part upon common assumptions about the incentives of

the firm possessing what today we would label market power – assumptions that remain widely held today. Standard case law and treatises assume that the profit-maximizing incentives of a monopolist (today we would also say especially one protected by difficult conditions of entry) will lead it to restrict output and raise price.[133] In doing so, the monopolist will generate allocative inefficiencies and benefit from a transfer of wealth from consumers. Moreover, as noted in *Aloca,* market power may also function as a "narcotic" that deadens initiative.[134] Hence, whether owing to reduced incentives or reduced ability, a policy that tolerates monopoly runs the risk of less innovation and less production efficiency.[135]

Finally, the monopolist's incentives will also incline it to maintain or elevate barriers to entry to exclude rivals or otherwise impair competition on the merits, for fear that its market power will otherwise erode. We can expect, therefore, that the monopolist may well invest some significant portion of its monopoly profits on socially undesirable rent-seeking conduct, designed first and foremost to maintain barriers to entry and perpetuate its monopoly.[136] Those expenditures may take the form of conduct that raises rivals' costs, reduces rivals' revenues, or simply bars rivals from the market. Lower output, higher prices, allocative inefficiency, wealth transfers, less innovation, lower efficiency, and socially undesirable rent-seeking – monopolies, it appears, are "bad."[137]

Then why do we tolerate monopolies at all? Again, as Judge Hand observed in *Alcoa*, antitrust law should not attack monopoly power that is the consequence of skill,[138] and the successful monopolist should not be turned upon lest the incentive to compete aggressively be undermined.[139] These two observations from *Alcoa* combine narrative with economics. From a narrative point of view, the "skillful" monopolist should be permitted to reap the rewards of its ingenuity. It is "fair" that it be able to do so. From an economic viewpoint, Hand's rationale also reflects the "carrot"

theory for tolerating monopoly, a theory that has proved to be durable. As Carlton & Perloff explain, "[T]he prospect of receiving monopoly profits may motivate firms to develop new products, improve products, or find lower cost methods of manufacturing. Were it not for the quest to obtain monopoly profits, firms might innovate less."[140]

Antitrust law's past tolerance of monopoly, however, has at best been grudging. Although it was clear that the law might permit the "honest" and "skillful" monopolist to ply its trade, the law also recognized that the existence of monopoly warrants a watchful eye. As Justice Scalia observed in his dissent in *Kodak*: "[b]ehavior that might otherwise not be of concern to the antitrust laws – or that might even be viewed as procompetitive – can take on exclusionary connotations when practiced by a monopolist."[141] The traditional narrative, therefore, is a cautious one, informed by a great deal of cumulative economic insight.

Perhaps what is most significant about the nature of more recent efforts to reformulate the definition of exclusionary conduct is their articulation of a "counter-narrative." In this counter-narrative, the monopolist is portrayed without suspicion. Quite to the contrary, competition, itself, is portrayed as a rough and tumble process, and monopolists are portrayed as "aggressive" or "hard" competitors whose inclination to exploitation and exclusion should be proven rather than presumed. Moreover, legal rules that too readily allow for the condemnation of the dominant firm's business strategies, no matter how "aggressive," are likely to over-deter through false positives, and hence dampen competitive zeal in the long run. The likelihood of false negatives is discounted, often based simply on the general assumption that successful exclusionary strategies are rarely successful and hence rarely attempted. Finally, typical of this counter-narrative is the view that dominant firms are under siege from their rivals big and small, and should have a "right" to defend themselves rather

than to merely surrender the fruits of their superior skill.

And what of the contenders? In this new narrative, rivals are typically portrayed as less deserving and presumptively less efficient than the dominant firm. Intimidated by the prospect of real competition, they have sought the intervention and protection of courts to compensate for their own inherent weaknesses as competitors. In some instances, rather than compete on the merits, they seek to free ride on the success of the incumbent by gaining access to some fruit of *its* success, such as coveted intellectual property. They are whiners, wimps and free riders. They are demonized and dominant firms lionized. In this manner, the counter-narrative transmutes suspicions from the dominant firm to its rivals. As is discussed *infra* in Part V, the counter-narrative takes concrete legal form by elevating the plaintiff's burden of proof, and sometimes by shifting the burden of proving justifications from the dominant firm to the plaintiff.

To illustrate the point, note how a change of word can alter the tale. What if the rival is viewed not as a less efficient, free riding interloper, but as a "maverick."[142] "Mavericks" are brash, creative, and self assured. They are iconoclasts and worthy opponents. To protect a maverick from a predator is to protect the creative spirit, itself. Here's another example of the power of the narrative. What if the rival is a "nascent" competitor? The image of the independent, committed, and creative start-up business also is quite powerful. What can this infant, this toddler yet achieve as a mature competitor? We may never know, unless the law nurtures it and protects it from being "smothered in the cradle." Suddenly the "predator" who would even attempt such an act is suspect.

Another potent element of the counter-narrative is the idea that "markets are self-correcting." In the case of dominant firm strategies that lead to market power, the assumption is that market power will invite entry, and entry will erode market power. Hence, if we "get it wrong," i.e. we fail

correctly to identify a practice as exclusionary, nothing much will be lost – in the long run.[143]

By contrast, the argument goes, over-deterrence will harm competition for years to come – precisely because it takes the form of antitrust condemnation of conduct that may be aggressive, but potentially efficient. As a consequence, dominant firms, fearing treble damage liability, will recoil from the most aggressive competitive strategies. Competitive zeal will be chilled; competition will be hobbled; consumers will pay the price – and markets will not correct for the over-deterrence, precisely because the law has forbade them to do so. Hence, because conduct that even approaches the line may never be implemented by risk averse dominant firms, consumers will lose the benefits of competition.[144]

These assumptions about the relative costs of over- and under-deterrence – of false positives and negatives – are invoked to justify a philosophical preference for markets as the most efficient regulators of competition. Antitrust enforcement, in contrast, is portrayed as a clumsy and crude tool, prone to human error.[145] This line of reasoning places entry at the heart of antitrust analysis, and is often repeated today in briefs to the courts. It also undergirds the courts' reasoning in many instances when it rejects Section 2 liability. These assumptions, however, are hardly the self-evident "economic" truths they are often presented to be. Indeed, they may in large part be little more than myth – potent, and especially pernicious in the context of dominant firm distribution strategies.

As a general matter, there is little empirical basis to support a sweeping and unqualified presumption that market power invites entry, and that entry will erode market power. First, committed entry is never a costless or immediate response to market power. There will almost always be some lag time before markets identify new competitive opportunities and react accordingly. Moreover, the reaction time and magnitude of the reaction will be affected by a

complex mix of factors ranging from the skill of entrepreneurs in identifying new opportunities, to the opinions of investors, to interest rates, and access to needed know how and perhaps intellectual property. Finally, new competitors act at great peril if they fail to anticipate both the effect that their own entry will have on prices and likely strategic price and non-price responses to that entry by any incumbent, dominant firm. Post-entry prices are likely to be lower than the pre-entry above competitive level prices owing to both the increased capacity that the new entrant brings to the market and aggressive responses by the incumbent firm. Indeed, those responses may be very specifically targeted at the new entrant, designed to deter its entry, or the entry of any other firm, by undermining its success.[146] Hence, entry can be deterred, even if the pre-entry price is above the competitive level.[147] For these and other reasons, the Merger Guidelines do not simply presume that market power necessarily invites entry. To the contrary, whether entry will be "timely, likely, and sufficient" to dissipate market power naturally through entry is a question of fact to be ascertained in each case. Sometimes it will be, and sometimes it won't be. A supposition that it will *always* be is unwarranted.[148]

For several reasons, this is especially true in cases of exclusionary distribution practices by dominant firms. First, in order to prevail in challenging such conduct under Section 2, a plaintiff today must prove that conditions of entry are indeed difficult.[149] This requirement already compensates for the possibility that markets can be self-correcting by requiring the plaintiff to demonstrate that conditions are not conducive to natural correction via entry.

Second, and almost universally, the nature and goal of the challenged conduct in Section 2 cases is that it bars or impairs entry. Hence, even if structural barriers to entry did not already exist in the market for other reasons, the dominant firm's conduct may be an effort to erect them.[150]

Third, the likelihood that markets will be self-correcting in these circumstances is substantially undermined by the failure of courts to quickly and cost-effectively condemn entry-deterring strategies, i.e. to protect the challenger, who may very well be the personification of the market's presumed power to self-correct. Indeed, impairing the market's effort to self-correct may have been the essential goal of the dominant firm's strategy. As a consequence, courts must be armed with the tools to act quickly to preserve the competition of new entrants. Those tools include substantive standards that recognize the price of lost opportunity for competition, procedural devices that are adaptable to the circumstances, and the right attitude. The importance of preserving new and resourceful entrants may be particularly acute in fast-moving technology industries, where once an opportunity for competitive challenge is lost, the conditions that produced it may be difficult, if not impossible, to replicate.[151]

Before embracing the "self-correcting market" narrative, therefore, it is essential to ask: What firm will undertake – and what investor will seriously support – entry into a market occupied by a dominant firm that has already demonstrated its penchant for entry-deterring strategies – especially if it has received the imprimatur of the courts? When will Dallas-Fort Worth again see a low cost new entrant into its airline hub? When will we all see a serious effort to design and market a new desktop operating system for Intel-compatible personal computers? When will another vibrant source of private label transparent tape emerge to replace LePage's? Because ease of entry is essential to self-correction, the courts should be especially sensitive to conduct that impairs or bars it, and especially skeptical of dominant firms arguing that "the market will take care of it."

There is another reason to be hesitant to embrace the "markets are self-correcting" aspect of the counter-narrative: antitrust laws have proven to be quite impotent at resurrecting dead or hobbled

rivals.

Exclusionary strategies can cause two distinct types of antitrust injury, injury to rivals and injury to consumers.[152] Rivals may suffer the most immediate harm – their ability to compete is impaired or destroyed. But consumers pay the ultimate price of exclusion in the form of diminished competition. For their exclusionary injury, rivals typically seek lost profits, or, if they have been entirely driven from the market, "going concern value."[153] The essential characteristic of these damages, however, is their common focus on the exclusionary strategy's effect on its targeted rival or rivals.[154] Rivals, however, act only as an early trip wire for harm to consumers. Consumers will seek to recover for the overcharge, or other value of diminished competition, that the exclusion of rivals facilitated. But for that exclusion, they typically argue, prices would have been lower, or quality and choice higher.[155] Rival and consumer injury and damages involve different types of harm and even different types of evidence, but they share common causation: they are both efforts to quantify the injuries that flow from the dominant firm's exclusionary conduct.

Damages, however, do not restore the competition that may have been lost – that is the province of injunctive relief. But courts have proven hesitant to use their equitable powers in such cases, even though the Supreme Court has directed them to do so.[156] In short, because recoverable damages will be limited to the four year statute of limitations period, consumers in affected markets may have to endure the uncompensated consequences of exclusion for years.

While the courts' hesitance to venture into the world of structural remedies may be well placed given past experience,[157] the greater significance of the challenge of restoring competition lies in its relevance to Section 2 standards and debates about false positives and negatives.

Precisely because it can be so difficult for courts to restore competition once it has been lost,

the true cost of exclusion to consumer welfare – and its benefit to dominant firms – are likely to be understated. This in turn suggests that the price of under-deterrence in exclusionary conduct cases, too, has been seriously understated. To illustrate once again – the price of under-deterrence in the Dallas Fort-Worth airline market is difficult to estimate, but is likely to be very substantial and very durable if low cost carriers are deterred by AMR's success in the courts. It is unlikely that Netscape will ever again attain the market momentum it once had, and hence Microsoft may well have prolonged its monopoly over Intel compatible PC operating systems for a decade or more – and even if it erodes, it may erode very slowly.[158] The supply of private label transparent tape may well have been disrupted for years by LePage's untimely demise.

The real price of exclusion may be especially aggravated in cases of nascent competition that challenged the dominant firm. Indeed, the convergence of factors that spawned that competition may never come again – the competitive "moment" may be lost, and the dominant firm's position fortified for years to come. To embrace standards of Section 2 liability misinformed by an unfounded fear of over-deterrence, therefore, puts a large thumb on the scale in favor of incumbent monopolies by effectively insulating their entry-deterring strategies from judicial scrutiny and correction. In short, even if it results in liability and treble damages, the strategy may prove to be so profitable that it will not be deterred if remedies are confined to damages and prospective behavioral restrictions.

And what of the costs of false positives? Of over-deterrence? First, whereas the damage to competition from under-deterrence in cases of dominant firm distribution strategies is immediate and quantifiable, the damages to competition from over-deterrence are inherently speculative and longer term. Presumptions about the self-correcting market may or may not turn out to be true – and as

noted above, the standards for proving liability already compensate to a large degree for those concerns.

In addition, if a court indulges those assumptions in reaching the conclusion that no liability should attach to the dominant firm's conduct, it will have no ongoing jurisdictional power to revisit that judgment and later act to restore competition if they prove to be misguided. In contrast, if liability is found, the court may place time limits on any injunctive relief, and if the injunctive remedies prove to be too constraining, the parties may at least return to the court and petition for modifications. "Over-deterrence" is hence subject to more active management, whereas under-deterrence can only be policed by starting from scratch with costly future investigation or litigation.

Moreover, arguments by dominant firms premised on their superior efficiency may prove too much. As will be discussed *infra*, the point is hardly that dominant firms should be forced to fight with one hand tied behind their backs. If they truly are more efficient than their rivals, as they often claim, they will have many potent tools available for the competitive struggle: they can readily lower price (without strings), improve product quality, and innovate in design, production and distribution. If they are truly more efficient than their rivals, the "self-correcting" market will favor them, and their rivals will fade of their own accord. No "push" via a distribution strategy from the dominant firm will be needed. The only constraint will be on their use of complex distribution strategies – "schemes" – whose "efficiency" is at best uncertain.

2. *Verizon as Counter-Narrative*

A final and critical component of this counter-narrative is its pejorative view of courts and to a lesser extent government enforcement agencies. Emphasis is placed on the limits of judicial process. Courts should avoid becoming mired in "regulation." Markets, and perhaps specialized

regulatory agencies charged with oversight, are superior to judicial intervention and can be relied upon to correct any competitive problems more accurately and more cost-effectively than courts. This was a critically important element of the plot in *Verizon*, which powerfully illustrates the influence of this new counter-narrative.

The long term significance of the Supreme Court's decision in *Verizon* is difficult to predict. On the one hand, it addresses a very narrow legal question in a very unique fact setting. At its core, it suggests little more than that courts should be reluctant to scrutinize pure, unilateral refusals to assist rivals[159] by firms in industries subject to extensive, competition-focused regulation. Indeed, there is already evidence in the lower courts that this view of the case is taking hold,[160] and the government has cautioned that the "but for" test for exclusionary conduct that it advocated to the Court in *Verizon* should be confined to its narrow context - a refusal to assist a competitor.[161] If it remains so confined, *Verizon's* significance will be limited. If it has more sweeping significance for Section 2, that significance will flow from its affinity for certain critical elements of the exclusionary conduct counter-narrative – some old, and some new.

For example, as the Court initially argued in *Verizon*:

> ... The opportunity to charge monopoly prices – at least for a short period – is what attracts "business acumen" in the first place; it induces risk taking that produces innovation and economic growth. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive *conduct*.[162]

The core idea of this passage – that monopolization standards should be tolerant of monopoly lest we erode the incentives of firms to innovate – provides the foundation upon which the Court ultimately reaches its definition of "exclusionary conduct." If the Court means only that the hope of achieving some competitive advantage is an essential spur to innovation, it seems hardly

objectionable. However, the reference here is to "monopoly prices," and the context is Section 2 monopolization standards, which address not mere competitive advantage, but monopoly power. Moreover, *in this case*, the defendant is not a firm that has secured some temporary competitive advantage, but is a durable monopolist. So it is perhaps worth inquiring whether the presumed connection between the dream of monopoly and innovation is in fact warranted as a general proposition.

First, is it really true that the hope of monopoly profits is the principal engine that drives innovation and economic progress? If it is, most business leaders are delusional dreamers, and the incentives to sharpen their business acumen are weak – because monopoly thankfully remains the exception, not the rule in most industries. True, the association between monopoly and the incentive to innovate is a long-standing article of faith in antitrust that is at least as old as *Alcoa*, and that it may well be true in some circumstances. But unless firms are hopelessly disconnected from the real world, the pipe dream of "monopoly" can hardly be the major incentive that drives most firms to innovate.[163] *Profits*, not monopoly profits, are the principal spur to innovation that "attracts 'business acumen.'" One need only observe the rapid pace of innovation in highly competitive and dynamic markets – where no real hope of monopoly exists – to know that something less than the hope of monopoly appears quite adequate to drive firms to create. Protecting monopoly because it is necessary to spur innovation, therefore, is a dubious across-the-board proposition upon which to build the law of monopolization, especially if it is invoked to justify permissive conduct standards in all cases.

Moreover, once monopoly has been achieved, the consequences will be predictably damaging in terms of allocative efficiency and consumer welfare, and perhaps diminished efficiency and

innovation. The Court's approach makes no concession to these more certain consequences of a tolerant policy towards monopoly. It appears instead to simply postulate that the amorphous risk of loss of incentive to innovate will necessarily outweigh any damage done. What truly is the empirical basis for this presumptive calculation?

A generous view might be that through lack of care in its rhetoric, the Court has simply conflated the hope of normal, temporary competitive advantage, and hence profitability, with "monopoly prices." After all, the Court seems to qualifies itself, inserting "at least for a short period." But the remainder of the opinion – and Justice Scalia's sophistication – strongly suggests that his deliberate goal was to build the case for a more tolerant monopolization standard. That case cannot be convincingly made, however, based on any imperative to protect incentives to innovate.[164]

The Court next wove together four themes to continue building its narrative: (1) Verizon was in possession of valuable "infrastructure;" (2) "forced" sharing tramples on the dominant firm's "right" to be free to choose its trading partners, and erodes its incentive to innovate; (3) the presence of an elaborate regulatory scheme directed at competition obviates the need for private antitrust enforcement; and (4) antitrust rules must be crafted to minimize the threat of false positives, the danger of which is amplified by the institutional limitations of courts.[165] In advocating these four themes, the Court not only embraced Verizon's self-narrative, but it used the case to promote a broader, non-empirical philosophy that views antitrust enforcement with deep skepticism. Each of these assertions is subject to serious challenge.

Valuable Infrastructure. The Court accepted Verizon's characterization of its "infrastructure" as an "economically beneficial" facility that had been developed over many years through substantial investment. To "force" it to "share" those "assets" with rivals, indeed to provide "affirmative

assistance" to them, it argued, was unprecedented in antitrust law and would undermine its incentive to innovate, not to mention the incentive of its rivals to innovate, because they would prefer of course to "free ride" on Verizon's efforts, if possible. The Court elaborated:

> The unbundled elements offered pursuant to...[the Telecommunications Act] exist only deep within the bowels of Verizon; they are brought out on compulsion of the 1996 Act and offered not to consumers but to rivals, and at considerable expense and effort. New systems must be designed and implemented simply to make that access possible – indeed, it is a failure of one of those systems that prompted the present complaint.[166]

A very passionate, forceful prelude to the Court's ultimate conclusion; one that seems hard to question. After all, what court would want to practice proctology against its corporate patient's will? On the other hand – how would the Court know any of that? Recall that Verizon never answered the complaint filed by Trinko. Instead, it moved to dismiss under Federal Rule 12(b)(6) for failure to state a claim – a fact wholly ignored by the Court.[167] The Court's main sources for these details, therefore, were Verizon's briefs in the Supreme Court.

If decisions of the Supreme Court are to turn on narrative, the narrative should at least be a work of non-fiction, as determined by evidence. Verizon's "infrastructure" might indeed turn out to be valuable – or it may consist of outmoded technology, little more than the guarded product of years of government protected monopoly. Yet there was no possibility of local exchange competition without access to that infrastructure. Its "value," therefore, may not be inherent. To support the narrative of the "valuable infrastructure," the Court thus had to downplay the importance of "access" to that infrastructure, despite the contrary allegations of the complaint, and fashion a contrary image, one of a gleaming, state of the art infrastructure, obtained at great sacrifice, through diligence and technical innovation, as well as a free-riding rival and interloper, who sought the help of the courts to

pry open access to that infrastructure without any willingness to share in its true cost. Fact or fiction?

The critical point is that the Court simply bought into Verizon's narrative, without any evidentiary basis for doing so and in derogation of the facts alleged by Trinko. It may well be that the narrative Verizon presented was non-fiction, but the only way to tell would have been to allow at least some discovery. It is predictable that every dominant firm, regardless of the evidence, will now invoke *Verizon* when challenged by its rivals or their customers, declaring that its own "valuable infrastructure" should be treated as presumptively inviolable by the courts.

Freedom to Select Trading Partners. The invocation of this second theme by the Court in *Verizon* is done deceptively and with notable irony. It derives, of course, from the Supreme Court's decision in *United States v. Colgate & Co.*, which the Court quotes in *Verizon* for the proposition that "as a general matter, the Sherman Act 'does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.'"[168] There are two difficulties with the Court's reliance on *Colgate*. First, it simply ignores the proviso that immediately precedes the quoted language: "*In the absence of any purpose to create or maintain a monopoly*," a proviso that unambiguously limits the relevance of *Colgate* in the context of a Section 2 claim. The obviousness of the omission demonstrates how far the Court was willing to go in an effort to wrap its narrative in legitimacy.[169]

Second, the theme of "trader independence" is drawn from a time when contract and property rights greatly influenced antitrust discourse.[170] Yet that kind of thinking has been resoundingly rejected as a cloak that protects downstream dealers.[171] It is unclear why the narrative should be

resurrected to defend dominant firms, yet remain anathema for their customer-dealers, other than a simple preference for the "freedom" of suppliers.

Deference to Regulation. Drawing heavily on Justice (then Judge) Breyer's decision in Town of Concord v. Boston Edison Co.,[172] the third leg of the Court's reasoning was deference to the regulatory scheme.[173] Having rejected an outright grant of implied immunity, the Court nevertheless argued that the presence of an elaborate regulatory scheme focused on competitive concerns counseled against "extending" antitrust law to address Trinko's allegations:

> Where...[a regulatory structure designed to deter and remedy anticompetitive harm] exists, the additional benefit to competition provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny. Where by contrast, '[t]here is nothing built into the regulatory scheme which performs the antitrust function,' ... the benefits of antitrust are worth its sometimes considerable disadvantages.[174]

This passage – largely *dicta* – is infused with narrative, not simple law or economics. The narrative appears to be the brain child of Justices Scalia and Breyer, both of whom bring strong views to the table on the efficacy of government regulation. It seeks to establish a hierarchy in which regulation of competition is preferred to antitrust, and in which antitrust is denigrated as an effective tool of competition policy – its benefits "small" and "less plausible," and its use replete with "considerable disadvantages." These are hardly self-evident economic propositions that warrant universal acceptance. At best they reflect the authors' personal intuitions – and perhaps now the Court's – about the role and efficacy of various forms of government regulation. But those intuitions have, and continue to be, the subject of debate.

The reasoning of the passage also suggests that regulation and antitrust perform the same "function." Although there can be some overlap, as is surely the case in the context of the

Telecommunications Act, that will not necessarily be true in other regulatory contexts. More importantly, it denigrates the role of antitrust enforcement in remedying and deterring anticompetitive conduct – even in the Telecommunications context – particularly the compensatory role of the private right of action. Finally, it arguably reflects a poor understanding of the Court's institutional role. The Court's grudging recognition that Congress inserted a savings clause to preserve antitrust remedies as a supplement to the remedies of the Telecommunications Act is largely subsumed in the narrative.[175] Contrary to the Court's view, Congress surely appeared to believe that antitrust remedies would serve a valuable, and distinct, "function," wholly apart form those of the Telecommunications Act.

Of False Positives, the Limited Expertise of Courts, and their Limited Utility as "Central Planners." The final step in the construction of the *Verizon* narrative combines three factors that all relate to the presumed limitations of courts as economic regulators. First, in recognizing antitrust claims, the Court instructs us to be attentive to the danger of "false positives," which may seriously inhibit the incentives for aggressive competition. Second, this threat of false positives is amplified by the courts' limited ability to evaluate the true effects of aggressive conduct. And finally, the Court warns that the design of remedies for some kinds of conduct may draw the courts into protracted and complex decision making that will in effect transform them into "central planners."[176]

As a first question, it is fair to ask: what does this passage have to do with the facts alleged in *Verizon*? If the plaintiff had been permitted to proceed to discovery, what "conduct that the antitrust laws were designed to protect" would have been "chilled"? By its own admission, Verizon had breached its interconnection agreement with AT&T, and done so, according to the plaintiff, in a way that impaired the quality of services provided to AT&T's customers. Its only justification appeared

to be a frontal assault on the wisdom of the Telecommunications Act, especially the "discounted" rates that must be offered to its rivals.[177] It remained to be proved, however, whether the discounted rates were, in fact, unreasonably low, and, in any event, whether there was any causal connection between those rates and Verizon's conduct. So it was not clear *in this case* and *at this stage of the case* that there was any substantial threat of a false positive.

As to the competence of a "generalist antitrust court,"[178] it is hardly clear that antitrust is any more complex than many other areas of federal regulatory law. Hence, the Court's narrative is again revealing of its ideology and philosophy, but is not based on hard economics. Courts, it seems, should simply avoid oversight of expert agencies that undertake competition analysis. This line of reasoning would justify a kind of abstention that hardly seems consistent with the long established thrust of the federal antitrust laws, which by design *presume* courts competent to undertake the very kind of decision-making about difficult economic issues that the Court seems to decry. Where, in any event, is the empirical basis for the Court's sweeping assertion that "[j]udicial oversight under the Sherman Act would seem destined to distort investment and lead to a new layer of interminable litigation, atop the variety of litigation routes already available to and actively pursued by competitive LECs [Local Exchange Carriers],"[179] and why would that be a judgment that the Court, not Congress should make?

A final point concerns the ability of courts to remedy antitrust violations – the specter of "courts as central planners." Again, the assertion appears to be disconnected from the facts in *Verizon* and hence is *dicta*. The terms of dealing with rivals were well established by the relevant federal and state regulatory agencies. The courts needed to add little other than a calculation of damages, if any, for Verizon's failure to do adhere to those conditions, and an injunction against

further breaches. The FCC was not abdicating its role as the "day-to-day enforcer of these detailed sharing obligations."[180]

If this aspect of the Court's holding is limited to its facts – enforcement of complex regulatory provisions relating to competition through antitrust claims brought in the courts – the damage may be containable.[181] But the Court seems emphatic that courts should practice self-restraint in the area of antitrust, in recognition of the supposed limits on courts' abilities to assess and remedy anticompetitive conduct. This expression of philosophy runs contrary to antitrust's "common law tradition," and openly invites abstention in place of common law case development.[182] No crystal ball is needed to see that that Court's *dicta* is likely to be advocated in equally sweeping terms by defendants in a wide variety of Section 2 claims, and perhaps in non-antitrust cases, as well, defendants whose interest will be in weakening antitrust standards. To so openly invite courts to abdicate the critical role they play in the antitrust enforcement framework is nothing less than irresponsible.

This counter-narrative is a product of over-zealous advocacy, carefully authored by dominant firms and their counsel and wrapped in "economics" for legitimacy's sake. In the Court's expression of it in *Verizon*, it is also a collection of carefully chosen invectives. No doubt the current wave was triggered at least in part by a few high-profile prosecutions, such as *Microsoft*, *AMR* and *LePage's*. Of course, we might expect that there would be a few cases that would generate some debate. Cases like *AMR* and *LePage's* are clearly examples of cases as to which reasonable people might differ. But such differences only amount to "over-deterrence" in the minds of those who simply disagree with the outcome of the judicial process. As was demonstrated in Section III, *supra*, the very few successful prosecutions are not so wildly and obviously wrong that a major re-write of the definition

of exclusion, or major pronouncements on the efficacy of antitrust enforcement, are warranted. Indeed, as was noted, in some of the most prominent Section 2 verdicts, the dominant firm simply failed to introduce evidence sufficient to persuade a jury that it really had anything other than illegitimate exclusion of rivals in mind. Even in *Verizon*, the assertion of "legitimate" business justifications was quite suspect, and never even put to the test of evidence.[183]

This new movement, therefore, is an over-reaction. It is well grounded neither in economics nor policy. There is no data to support the accusation that Section 2 is over-deterring some kind of "legitimate" conduct.[184] Section 2 prosecutions by the government are exceedingly rare. And as was demonstrated above, few Section 2 cases proceed to trial, and of those, only very strong cases make it to verdict and survive appeal. In short, the Court in *Verizon* seized upon what should have been a simple case presenting a narrow question of law and transformed it into a vehicle for its own sweeping manifesto of competition policy. In doing so, it also permitted itself to be lobbied by Verizon, and stood persuaded by arguments that were better directed as an institutional matter to the FCC and Congress.

The importance of these competing monopolization narratives is quite evident in the tension that now exists in Section 2 law between price predation and cases of non-price exclusionary conduct.[185] In a real sense, traditional narrative undergirds the *Aspen/Kodak* approach to non-price exclusionary conduct, whereas the newer counter-narrative pervades the law of price predation. This battle of narratives is evident in recent efforts to reform the definition of exclusionary conduct.

B. Selecting the Appropriate Standard

As has already been discussed, *Alcoa's* "skill, foresight, luck or business acumen" formulation gave way after a generation to *Aspen's* "non-efficiency based competition," a

formulation that derived from a fusion of Robert Bork's Antitrust Paradox and Phillip Areeda's original antitrust treatise.[186] At roughly the same time, the price predation formula emerged in *Matsushita*. For a time, the two lines of cases developed independently – *Aspen* was followed by *Kodak* and *Matsushita* by *Brooke Group*. More recently, these two lines of cases have begun to converge, prompted in part by the characterization challenge of distribution practices lying at the intersection of pricing and exclusivity. That convergence has spawned four arguably distinct approaches.

1. *The "But For" Test*

In its brief in support of the petition for a writ of certiorari in *Verizon*, the Department of Justice and the Federal Trade Commission appeared to advocate a "but for" test for defining exclusionary conduct in all Section 2 cases. According to that brief, "[c]onduct is 'exclusionary' or 'predatory' in antitrust jurisprudence if the conduct would not make economic sense for the defendant but for its elimination or softening of competition."[187]

The but for test asks a simple question: would the monopolist have undertaken the conduct *but for* its anticompetitive effects? Put another way, it asks whether there was any legitimate business reason for the conduct. The but for test thus focuses exclusively on the incentives of the dominant firm, largely ignoring the effects of its conduct on rivals or consumers.[188] As a consequence, it seemingly would credit any efficiency gains to the monopolist as a complete defense to charges of monopolization. It would disregard the amount of those gains and the degree to which the challenged conduct also may have resulted in significant anticompetitive effects on rivals and consumers. There would be no "weighing" or "balancing." It also would shift the burden of pleading and producing evidence of gains from the defendant to the plaintiff.

To illustrate the point, assume that the total value to a dominant firm of a specific strategy is $100. Assume further that $25 of that value can be attributed to efficiency gains, such as lower costs, but $75 is attributable to the conduct's exclusionary effect on rivals, i.e. the exercise of market power. How should the conduct be treated under Section 2? A straight-forward application of the but for test would conclude that the conduct is *not* exclusionary, because the monopolist would still have undertaken the conduct even without the anticompetitive gains – the $25 having provided an adequate enough incentive for it to do so. In fact, the test would produce that same result even of the efficiency gains were only $1 and the gains from market power were $99. In a pure application of the test, therefore, *any* efficiency gain will be credited completely, even when the anticompetitive effects of the conduct far outweigh that gain.

This appears to be so obvious a flaw in the approach, that one has to ask whether this could have been what the government really intended. There are two possibilities. First, the government did not intend for the but for approach to be applied so rigidly. There is reason to believe that although it may have so intended initially, it altered its position by the time of the merits briefing.

As will be discussed in greater depth *infra*, in its merits brief, instead of a sweeping but for test, the government endorsed a "disproportionality" test as the general standard for all Section 2 cases.[189] It thereafter again endorsed the "but for" approach, but with some critical qualifications that would make it a far more limited tool:

> Where, as here, the plaintiff asserts that the defendant was under a duty *to assist a rival*, the inquiry into whether conduct is "exclusionary" or "predatory" requires a sharper focus. In that context, conduct is not exclusionary or predatory *unless* it would make no economic sense for the defendant but for its tendency to eliminate or lessen competition.[190]

So limited, the but for test can perhaps be justified if the government simply doubts the

ultimate merits of "refusals to assist" claims by rivals and is inclined to credit the legitimacy of dominant firm strategies for fear of over-deterrence and judicial error – in this particular context.[191] Drawing parallels from the law of predatory pricing, which the government's merits brief does,[192] such a philosophy with respect to predation rules simply proceeds from a set of assumptions that remain implicit. But this is more political economy than economics or law, and if it remains implicit it will not be subjected to the degree of scrutiny that it deserves.

Moreover, such a philosophy is at odds with the approach to efficiency defenses set forth in both the Collaboration Among Competitors and Merger Guidelines.[193] First, both documents commence with a consideration of anticompetitive effects.[194] As a consequence, efficiencies are never considered in a vacuum: there is no unidimensional framework. They are always considered relative to the anticompetitive effects of the conduct under scrutiny. This is a reflection in part of the widespread acceptance of the insight developed by Oliver Williamson in the merger context: some conduct can simultaneously produce efficiency gains *and* losses attributable to the exercise of market power, i.e. *inefficiencies*. Some kind of "weighing" or judging of the relative costs and benefits of such conduct thus is an inherent characteristic of the hardest antitrust cases.[195]

Second, both sets of Guidelines evidence a healthy skepticism for claims of efficiency – precisely because the efficiency analysis comes only after there is already reason to suspect the conduct will be harmful to competition – just as will be the case in Section 2 challenges. Both thus mandate that evidence of efficiency be *conduct-specific* and *verifiable*, strongly implying that the defendant will have to bear at least the burden of production to demonstrate that the efficiencies could not be achieved any other way than by the conduct, and that they are in fact "real."[196]

Finally, *all* forms of the but for test are objectionable on procedural grounds. The but for test

immediately directs the plaintiff to evaluate the impact of the conduct on the internal incentives, intentions, and accounting of the defendant, dominant firm. In the above hypothetical, for example, in order to be able to allege that "but for the anticompetitive gains from the conduct the dominant firm would not have undertaken it," the plaintiff would have to be able to more specifically allege that there were no production efficiencies associated with the conduct – whether $25 or $1. It is difficult to see how, consistent with Rule 11 obligations, a plaintiff preparing a complaint could allege that – which is precisely what the government demanded of Trinko in the *Verizon* case. Without any opportunity for discovery, the critical evidence necessary to make such an allegation would almost always lie behind the locked doors of the dominant firm. As is discussed *infra*, for this and other reasons, to the extent the but for inquiry might be relevant at all under Section 2, the risk of non-persuasion should be allocated to the dominant firm, not the plaintiff.

2. *The Sacrifice Test*

The most direct effort to extend the predatory pricing approach to all exclusionary conduct is the "sacrifice" test. Under this test, as with predatory pricing, short term sacrifice of profits would be a necessary, though not sufficient, element of any claim of "exclusionary" conduct.[197] A sacrifice test could serve as a unitary framework that would unite price and non-price predation standards and close the gap between *Matsushita-Brooke Group* and *Aspen/Kodak* – but it would do so by embracing *Matsushita/Brooke Group's* framework of sacrifice and recoupment.[198]

The sacrifice test is also related to the "but for" test. In its certiorari brief in *Verizon*, for example, the government supported its articulation of the but for test by citing to *Matsushita*, and then stating: "For example, exclusionary conduct normally involves the sacrifice of short-term profits or goodwill in order to maintain or obtain long-term monopoly power."[199]

Although the sacrifice test has its supporters,[200] it has been met with substantial criticism, both as a standard for judging price behavior,[201] and as an appropriate test for non-price exclusionary conduct.[202] Even Professors Ordover & Willig, who were instrumental in developing and advocating sacrifice as a test of predation,[203] endorse it today only as a presumption, objected to its application to *Verizon*, and argue that it should not always be viewed as a necessary condition of Section 2 liability.[204]

The principal flaw of a sacrifice test is its assumption that "predation" is never of concern to the antitrust laws if it is costless. Yet examples abound in the cases and commentary of conduct that is unreasonably exclusionary, yet involved either little or no sacrifice of profit, or some sacrifice in a context where recoupment could be achieved simultaneously.[205] In *Conwood*, for example, what "sacrifice" did UST make when its representatives disposed of its competitors' advertising racks? And in the *Microsoft* case, Microsoft did not appear to sacrifice any profits when it imposed various exclusionary licensing and contractual restrictions on its various classes of customers, or when it integrated its various programs into its operating system. Neither was there any sacrifice involved in its threats to Intel and Apple. In fact, these acts were facilitated by its market power. Ironically, it is that very market power which, especially in extreme cases, can permit a dominant firm to exclude at no or little cost.

Indeed, the government's retreat from a sacrifice test in its Brief on the Merits in *Verizon,* and endorsement of a disproportionality test, may have been motivated in part by the realization that the test was over-inclusive to the point of undermining important precedent and even pending government prosecutions. For example, as an example of conduct that violates Section 2 – and illustrates the application of a disproportionality test – the government referred to fraud on the patent

office claims under *Walker Process Equip., Inc. v. Food Mach. & Chem. Corp.*,[206] as well as sham petitioning, *California Motor Transp. Co. v. Trucking Unlimited*,[207] and abuses of private standard setting processes, *Allied Tube & Conduit Corp. v. Indian Head, Inc.*[208] These cases are relevant to ongoing FTC prosecutions of Rambus and Unocal, and may often involve conduct that requires no or little "sacrifice."

As is true of the "but for" test, the sacrifice test is also objectionable on procedural grounds, because it shifts the burden of production from the defendant to the plaintiff. As will be discussed, *infra*, the presence or absence of sacrifice does not make either the defendant's monopoly power or the effects of its conduct on rivals and consumers any more or less probable. It is actually the *absence of sacrifice* that may be relevant to a Section 2 case, because it suggests that the defendant was engaged in competition on the merits. But the evidence to support such an allegation will be entirely in the hands of the defendant. "Absence of sacrifice," therefore, if relevant at all, is relevant as a defense, because it tends to demonstrate that any exclusion was the consequence of potentially efficient conduct.[209]

Hence, although evidence of sacrifice may indeed support a finding of exclusionary conduct, it should not be viewed as a necessary condition for all cases of exclusion. It is a good rule of inclusion, but not necessarily a good rule of exclusion.

Also as noted above, if absence of sacrifice is properly understood as a kind of efficiency defense, it should be subject to the kinds of production standards incorporated in the Competitor Collaboration and Merger Guidelines. In this sense, efficiency would be subject to an "inverse *Matsushita* plausibility" test. In *Matsushita*, the Court justified the imposition of an elevated standard of proof of conspiracy because claims of predatory pricing are inherently implausible. If in

cases of implausible economic harm, such as predatory pricing, plaintiffs are subjected to such elevated burdens of proof, it may well be appropriate in cases where harm is quite plausible – even established – to subject defendants to an analogous burden, especially with respect to claims of efficiency. If a dominant firm wants to rebut evidence that its distribution strategies have had anticompetitive effects, it would be prudent to ask that it do so with some greater degree of certainty. "Economic plausibility" should be a two way street.

Nevertheless, despite these substantial shortcomings and limitations, the sacrifice test appears to have found some favor in the Supreme Court for non-price exclusionary conduct. In characterizing its *Aspen Skiing* decision in *Verizon*, the Court noted:

> The unilateral termination of a voluntary (*and thus presumably profitable*) course of dealing suggested a willingness to forsake short-term profits to achieve an anticompetitive end.... Similarly, the defendant's unwillingness to renew the ticket *even if compensated at retail price* revealed a distinctly anticompetitive bent.[210]

The observation that Aspen's sacrifice of profits evidenced its anticompetitive intentions, however, is a far cry from a wholesale endorsement of "sacrifice" as a *necessary* condition for all allegations of exclusionary conduct. The Court may be saying nothing more than that sacrifice may be a relevant, perhaps even a *sufficient* condition, because it tends to show intent, and intent informs judgments about effects. But that is far short of a holding that sacrifice is a *necessary* condition, given the possibilities of low or no cost exclusionary strategies.

3. *The "Less Efficient Rival" Test*

Judge Richard A. Posner has advocated a two part standard for establishing exclusionary practices:

> ...[I]n every case in which [exclusionary conduct] is alleged, the plaintiff must prove first that the defendant has monopoly power and second that the challenged practice

> is likely in the circumstances to exclude from the defendant's market an equally or more efficient competitor. The defendant can rebut by proving that although it is a monopolist and the challenged practice is exclusionary, the practice is, on balance, efficient.[211]

This proposal may have some appeal as a purely economic matter. But it will be difficult to translate into practice.[212]

First, measuring "comparative efficiency" is a tricky business, at best, and is likely to prove a very difficult standard to apply in practice. Moreover, it may not be appropriate at all to focus on the comparative efficiency of the rivals as a general matter. If any comparison is to be done, it is of the inefficiencies and efficiencies of the challenged conduct. Nevertheless, Judge Posner's approach seems to put the injured rival to a "worthiness" test – it must first establish its own efficiency in order to challenge the inefficiency of the dominant firm's *practice*.

Second, it is difficult to imagine how a plaintiff would at the pleading stage possess the information necessary to allege that it was at least "equally efficient" as the defendant. Indeed, in terms of allocating the risk of non-persuasion, it would seem more appropriate to require the defendant to assert and prove that it was superior to its vanquished rival from the point of view of efficiency. A comparative efficiency advantage would not alter the fact that the defendant is a dominant firm and that it is acted in a way that has harmed rivals and consumers – all prerequisites that the plaintiff can and should be required to allege and ultimately prove. If the comparative efficiencies of the two rivals is relevant at all, therefore, it is only relevant as a "defense."

Third, a "less efficient rival" standard suffers from being but a snap shot of competition at a brief moment in time. The dominant firm's motivation may well have been to preclude the rival from reaching a point of equal efficiency by, for example, impairing its ability to reach minimum

efficient scale. It would surely be anomalous in such a case to presume that the exclusion did not harm competition. True it might not have harmed competition *at that precise moment*, because the rival had yet to reach its potential, but Section 2's horizon should not be so clipped if it is to function as an adequate deterrent to strategic behavior that impairs long run competition.

Finally, and perhaps most fundamentally, if the rival is truly less efficient, its demise should come about naturally over time, with no help from targeted marketing practices. The dominant firm – if truly more efficient – will always have an arsenal of ample alternate strategies that are more clearly a product of its superior efficiency and can be more readily evaluated by courts. Viewed another way, the danger of over-deterrence is small when a dominant firm's defense of "no harm done," premised on the alleged deficiencies of its prey, is rejected. If those claims are true, the prey will vanish of its own accord. One also has to wonder about the plausibility of the dominant firm's claim to superior efficiency if it elects to target its supposedly less efficient rival for premature elimination, a common feature of many challenged distribution strategies. As noted above, it may be, for example, that the rival is currently less efficient because it has yet to reach full scale economies – and that is precisely what the dominant firm is trying to forestall. Moreover, there may be many reasons why the rival cannot formulate an adequate counter-strategy in response to the dominant firm's distribution scheme, and they may have little or nothing to do with its comparative efficiency. Consumers is such circumstances, can be the big, long run losers from lenient standards, owing to the loss of unrealized future competitive benefits.

Hence, the antitrust laws should be suspect of a dominant firm that undertakes targeted efforts to eliminate rivals only to claim that they were not "equally efficient" and therefore that their loss is immaterial. This is especially apropos in the case of nascent competition. As the D.C. Circuit

observed in *Microsoft*:

> We may infer causation when exclusionary conduct is aimed at producers of nascent competitive technologies as well as when it is aimed at producers of established substitutes. Admittedly, in the former case there is added uncertainty, inasmuch as nascent threats are merely potential substitutes. But the underlying proof problem is the same--neither plaintiffs nor the court can confidently reconstruct a product's hypothetical technological development in a world absent the defendant's exclusionary conduct. To some degree, "the defendant is made to suffer the uncertain consequences of its own undesirable conduct." 3 AREEDA & HOVENKAMP, ANTITRUST LAW ¶ 651c, at 78.[213]

A "less efficient rival" standard could lead to false negatives in such circumstances and pose a significant threat of under-deterrence. Ironically, the standard evidences something of a lack of faith in the capacity of markets to correct for inefficiency, something markets may in truth be better equipped to do than courts.

4. *The Disproportionality-Balancing Debate*

These first three tests all can be faulted for being unidimensional – they focus largely, if not exclusively, on measuring the effects of allegedly exclusionary conduct on the alleged predator. They tend to ignore or downplay the impact of that conduct on prey and consumers. They thus emphasize production and distribution efficiencies at the expense of the arguably more salutary concern for allocative and consumption inefficiencies.

Two more promising models – which are both three dimensional – are the "disproportionality" and balancing tests.[214] The disproportionality test has been variously advocated by the government and has been attributed to Professor Herbert Hovenkamp, who has proposed that "[e]xclusionary conduct" be defined as actions that:

> (1) are reasonably capable of creating, enlarging, or prolonging monopoly power by impairing the opportunities of rivals; and

(2) that either (2a) do not benefit consumers at all, or (2b) are unnecessary for the particular consumer benefits that the acts produce, or (2c) produce harms disproportionate to the resulting benefits.[215]

Note that the first step in Hovenkamp's test focuses on monopoly power and anticompetitive effects. Before a case proceeds any further, therefore, a plaintiff would have to allege and be prepared to prove that the defendant has undertaken conduct that has injured its rivals, and that as a consequence of that conduct it is in a position to injure consumers – i.e. to wield monopoly power. These are important initial filters that will limit exclusion cases from the start.[216] The approach, therefore, is consistent with traditional Section 2 doctrine, but also with more contemporary developments, such as the framework proposed by the D.C. Circuit in *Microsoft*, at least as an initial inquiry.

Hovenkamp next moves to a more particular assessment of the conduct's effects on both consumers and the dominant firm, and describes three circumstances where the conduct should be condemned. His first circumstance is conduct that produces no benefits for consumers – i.e. it has no plausible efficiency justification. This is "lop-sided Option #1" – harm and no benefit – and is an easy case for condemnation. Second, if the conduct and its attendant harms are not necessary to achieve its benefits, the conduct also should be condemned. This is akin in part to a less restrictive means test, and again might lead to condemnation, but is likely to be more controversial than the case of no justification.

An assessment of "proportionality" would be necessary only where the benefits and harms of the challenged conduct are both pronounced, and the harms are necessary to achieve the benefits. In this instance, Hovenkamp asks whether the harms are "disproportionate to the resulting benefits." In

its brief on the merits in *Verizon*, the government put it this way: "the harm to competition must be disproportionate to consumer benefits (in terms of providing a superior product, for example) and to the economic benefits to the defendant (aside from benefits that accrue from diminished competition)."[217]

Like the *Microsoft* framework, but with less clarity and with less specific attention to burdens of production, Hovenkamp and the government thus acknowledge the possibility that conduct that excludes could lead to both inefficiencies and efficiencies. So there appears to be some emerging consensus that we must have a mechanism for "weighing"in such cases, at least as a general rule. Perhaps as a concession to the uncertainty and imprecision of measuring and comparing inefficiencies and efficiencies, however, Hovenkamp and the government would in such cases demand – presumably of the plaintiff – that the evidence demonstrate that the harms not merely outweigh the benefits, but that they *disproportionately* outweigh them.[218] Close cases, it would seem, should go to the dominant firm, for fear perhaps of lost efficiencies and incentives to innovate in production and especially distribution.

This is where Hovenkamp and the government appear to part company with the *Microsoft* court. In its final step, the D.C. Circuit would require the plaintiff to demonstrate that "the anticompetitive harm of the conduct outweighs the procompetitive benefit"[219] and it likens that process to the "similar balancing approach" of the rule of reason.[220] The government has distanced itself from that approach, most emphatically in its certiorari brief in *Verizon*.[221]

The disproportionality and balancing approaches thus represent both consensus and conflict. There is consensus that, as a general rule, the law of Section 2 cannot turn a blind eye to conduct that has mixed consequences.[222] There also appears to be consensus that an operative Section 2

framework must start with some screens and also must specify the relative burdens of production of the plaintiff and defendant. Monopoly power and anticompetitive effect appear to be consensus screens. Perhaps some modification is required, therefore, of the "willful acquisition or maintenance" prong of the traditional Section 2 framework in order to more expressly recognize that consensus. Once adverse effects are supported by evidence, there appears to be further consensus that in some fashion the dominant firm should be invited to present its evidence of "justifications." Finally, there appears to be agreement that those justifications must be assessed in some fashion against the anticompetitive effects of the dominant firm's conduct. Screens will necessarily limit the cases that proceed to discovery and trial, as will a shifting burden of production that permits – and demands – evidence of justification.

Differences remain, however, in how the law should best go about assessing mixed cases that present significant evidence of both harm and benefit. If there are in fact "close cases," a simple balancing test would presumably be a more lenient standard, and hence a more stringent rule, whereas a disproportionality test would entail a higher burden of proof and hence be more permissive. For example, whereas "balancing" suggests that a preponderance of harm (harm "outweighs" benefit) would be enough to establish a violation – 51% harm to 49% benefit – "disproportionality," of course, suggests that the harms must *really* outweigh the benefits in order to warrant condemnation. But "disproportionality" is hardly an inherently certain formula. Is 55-45% "disproportionate" enough? Or do proponents of the test think 75-25% is more what they have in mind? Moreover, as noted above, there may be some continuing disagreement about how much and what sort of evidence of anticompetitive effect is sufficient to shift a burden of production to the defendant to justify its conduct.[223]

It is essential to realize, however, that economics does not clearly point the way to either disproportionality or balancing. The choice of approach is instead a matter of policy, one that could largely turn on views of whether close cases should go to the plaintiff or the defendant. That in turn may reflect more fundamental differences about one's assessment of such factors as (1) the relative dangers of false positives and negatives, (2) the economic plausibility of exclusionary strategies, (3) the economic plausibility of efficiency defenses, and (4) the utility of judicial assessment of allegations of anticompetitive harms and competitive benefits. These factors should be recognized, however, for what they are: intuitions that derive from philosophical and ideological leanings and values, not necessarily economics.

As will be further explored in Section V, *infra*, this difference of opinion is largely theoretical. It fundamentally misperceives the reasonable role of the fact finder and, as a consequence, resolving it in favor of one or another standard is unlikely to make much of a difference in most cases.

V. DESIGNING OPERATIVE LEGAL RULES FOR DOMINANT FIRM DISTRIBUTION STRATEGIES

A. FOUR SOURCES OF WISDOM FOR DESIGNING ANTITRUST RULES

Antitrust rules of decision should not be constructed in a vacuum or based on a single perspective. At least four factors – "sources of wisdom" – inform the choice of a particular rule.

Substantive Legal Rules. First and foremost, antitrust rules must comport with the antitrust statutes and controlling cases as they exist. To ignore the statutes and "old" case law is to ignore the rule of law, which in turn undermines both the certainty and legitimacy of competition policy. It is well known in antitrust, for example, that we pay almost no mind to merger decisions prior to

General Dynamics, but even though that may be sound as an economic matter, it is nothing to be especially proud of and it is not an ideal circumstance. It bears repeating, therefore, that the process of identifying antitrust rules should commence with the language of the relevant statutes, and the decisions of the Supreme Court and the courts of appeals interpreting it.

Economic Goals. Perhaps the most significant change in antitrust law in the last generation, however, has been a more focused effort to integrate economic learning into those rules. To be sure, the inherent malleability of the antitrust laws themselves - especially Section 1 of the Sherman Act – facilitated that change. It is not, of course, that economics was irrelevant to antitrust before the late 1970s and now is central. To the contrary, the oldest of antitrust decisions grapple with the economics of markets and market participants. Rather, following a period of intense criticism from economists and lawyers alike, the methodology and content of antitrust economics has been transformed.

Today antitrust is driven more by economic concepts than by the particulars of the antitrust laws and the categories of conduct that they spawned. Drawing from the law of monopolization and mergers, concepts such as market power, entry and efficiency are now quite central to all but the most blatant, per se offenses. To be recognized as sound and "contemporary," therefore, antitrust rules must fit well within the modern economic framework.

Economic Decision Theory. Economics influences antitrust rules in yet another way. Apart from the substantive analysis of conduct and its competitive effects, economics has influenced how we think about antitrust as a process. Examples of this influence can be found in efforts to evaluate the costs and benefits of antitrust enforcement, concern about the competency of judges and juries to make accurate complex economic decisions, and most prominently in the related concern for the

law's ability to balance error rates, i.e. to assess the relative costs of false positives and false negatives.[224] It is rare today in cases where fundamental questions are raised about the "right standard" that the parties and courts do not assess these issues.

Procedural Theory. Finally, when the statutes, substantive economic goals and economics of process are all added into the mix, we must address context: antitrust as complex litigation. To be effective, antitrust rules must be "operative," i.e. they must work reasonably well in the context of litigation where they are ultimately going to be applied. That means they must be structured to take into account such basic litigation features as due process, burdens of pleading, production and proof, and rules of evidence. Rules that make perfect sense as a matter of economics may not make sense from the point of view of procedure. They may also be manipulated to the point where the underlying economic goals can be frustrated.

For example, *Monsanto* and *Matsushita* require plaintiffs to introduce evidence "tending to exclude the possibility" that the defendants acted unilaterally.[225] This test is a product of both substantive economic analysis and economic decision theory.

There can be little doubt that the standard was adopted in *Monsanto* in large part to counteract the harsh treatment accorded minimum resale price maintenance.[226] In that sense, it likely reflected the Court's underlying concern about the wisdom of the per se rule and provided something of an "equilibrating" force.[227] But the standard was also embraced in *Monsanto* for reasons related to economic decision theory. Because the competitive consequences of price and non-price vertical intrabrand restraints can be so alike, and because the latter are subject to more lenient treatment under *Sylvania*, any lower standard of proof of an RPM conspiracy[228] could pose a significant threat of "false positives," i.e., pro-competitive or competitively neutral instances of vertical behavior that

would nevertheless be condemned, which in turn would undermine *Sylvania*.[229] To minimize the incidence of such false positives, the Court fashioned an elevated standard of proof.

In *Matsushita*, where the *Monsanto* formula was extended to predatory pricing conspiracies, the Court's rationale was more transparent, and it embraced all three elements: substantive economics, process economics, and legal process. As a *substantive economic matter*, the Court concluded that predatory pricing is rarely successful and hence rarely tried.[230] From the point of view of *economic decision theory*, it reasoned that the cost of false positives would be especially great, owing to the fact that lower prices provide immediate benefits to consumers. A lenient rule, therefore, would chill aggressive pricing behavior and harm consumers. Finally, the Court's reasoning also incorporated legal process – the standard for summary judgment. Reflecting its economic analysis both on the merits and as a matter of economic decision theory, the Court posited that anything less that a bright line standard that could be readily applied early in litigation would fail to protect consumers and aggressive rivals from attack. "Process," too, served an important equilibrating function to counter-act potentially harsh substantive prohibitions.[231]

Today, however, the *Monsanto-Matsushita* standard has bled over into run of the mill cartel cases, where the Court's underlying economic rationale does not appear to apply. In these cases, the conduct is allegedly concerted action by rivals to raise, not lower prices, a category of conduct that has uniformly been of concern to antitrust throughout all of its history and remains a consensus, foundation reason for its existence.[232] As a matter of substantive economic analysis, therefore, the conduct is presumptively harmful to competition – not potentially beneficial as is the case with some minimum RPM and lower prices. How does it fare then as a matter of economic decision theory? In contrast to minimum RPM and especially predatory pricing, there is almost no possibility of short

run benefit to consumers, yet the threat to them is quite substantial. Hence, concern about false *negatives*, not false positives should be the greater concern, i.e. if a conspiracy standard is assigned that is too stringent, competitively troublesome price raising strategies by rivals may go unpunished and hence undeterred. Under these circumstances, the "tending to exclude the possibility" standard simply cannot be justified – yet defendants and some courts have applied it as if it were rote.[233]

The conspiracy standard example illustrates the importance of all four sources of wisdom, but it especially illuminates the risk of being inattentive to process. Economics must be translated into law, and process is the translator. If in this final step in the development of operative antitrust rules we are insensitive to factors such as the parties' likely access to the evidence necessary to meet the assigned burden of proof, the fashioned rule may over-correct, i.e. it may lead to false negatives that are more significant than the economics predicted. Similarly, if we adopt standards that shift and/or elevate burdens of production and proof to plaintiffs, we must carefully assess whether the resultant allocation of burdens, taking into account factors such as likely access to evidence, will yield an optimally balanced and operative rule of decision.

B. Towards A More Uniformly Integrated Model for Developing Antitrust Rules

The debate about formulating the optimal standard for defining "exclusionary" conduct has been inattentive to all four sources of wisdom – especially economic decision theory and legal process. The consequence has been a tendency to advocate rules that may well lead to under-deterrence, owing in part to the unreasonably elevated – even unsatisfiable – burdens being placed on plaintiffs, owing to the fear of false positives. A more nuanced approach is required that recognizes that rules of exclusion may need to be more flexible and adaptable to the facts of particular cases.

1. *The Imperatives of Legal Process: Revisiting the Sacrifice Standard*

Consider for example the "sacrifice" standard. From the point of view of substantive economics, the attraction of a sacrifice standard as a measure of exclusionary intent is straightforward: firms presumably motivated by a desire to maximize profits won't undertake strategies that involve sacrifice unless they view those sacrifices as an investment in future profitability.[234] From the point of view of economic decision theory, the attraction is also straightforward: an exclusionary conduct standard that reaches conduct not involving sacrifice may result in false positives and hence will chill legitimate, albeit aggressive, competitive behavior. The seemingly logical result is a policy choice to impose on plaintiffs the burden of alleging "sacrifice," and probably a plausible strategy for recoupment, similar to the current test for predatory pricing.

Although both assumptions can and have been drawn into question on their own terms,[235] they can also be faulted from a procedural point of view.

To begin, in order to allocate the burden of pleading a particular fact, it is necessary first to determine the elements of the offense and the elements of any defenses and/or affirmative defenses.[236] Once those elements are identified, for purposes of discovery, evaluating burdens of production, and for trial, a critical additional issue is "relevance." Of course, it is elemental that a piece of evidence is "relevant" if it makes a "fact that is of consequence" to the action "more or less probable."[237] By identifying the elements of the offense and any defenses and affirmative defenses, the law provides boundaries within which "relevance" can be judged, and this in turn permits litigation to proceed in an orderly fashion. So the issue is, what makes evidence of "sacrifice" relevant, i.e., how does it make more or less probable a "fact that is of consequence"?

Before answering that question, it may be helpful to provide an example, in this instance, one drawn from the law of torts. As I have explored elsewhere,[238] a "defense" typically defeats the

plaintiff's case. The quintessential defense, therefore, is "denial." For example, in the world of tort, a defense to battery is "I deny that there was any physical contact." Such a denial puts the plaintiff's proof to the test – the message is clear: "prove" that I touched you. By defining the offense of battery to include physical touching, the law has allocated the burden of pleading and proof to the plaintiff, and any evidence that tends to make the fact of a touching more or less probable will by definition be "relevant." Hence, a complaint for battery can be dismissed if it fails to allege a touching. If it so alleges, but discovery does not support the allegation, the defendant can seek summary judgment. And if at trial the plaintiff similarly fails to meet its burden of production, the defendant will prevail.

By way of contrast, "consent" and "self-defense" are considered to be affirmative defenses to battery. Affirmative defenses operate "by way of avoidance" – they admit the plaintiff's underlying allegations, but raise some other circumstance that the law has recognized as an "excuse" for the conduct. In the cases of "consent" or "self defense," rather than denying that the touching took place, the defendant is saying "even if I touched you, the law permitted me to do so." Typically, the burden of pleading a *defense* rests with the defendant, but the burden of proof remains with the plaintiff. On the other hand, the burden of pleading *and* proving an *affirmative defense* rests with the defendant. So, for example, the fact that the plaintiff was armed is not relevant to whether there was a touching – it does not make the fact of a touching more or less probable. But it might be very relevant to whether the defendant acted in self-defense. Hence, it would typically be a fact that the defendant would have to allege and prove as part of its affirmative defense of self defense.

How is this example instructive for antitrust? It is of course well-settled that as a threshold matter a plaintiff alleging monopolization must allege and prove monopoly power. Although

traditionally the second element of monopolization has been expressed as "willful acquisition or maintenance," an important shift has been taking place in the courts. Today, although they may cast it in terms of "willful acquisition or maintenance," many courts expect the Section 2 plaintiff to demonstrate actual anticompetitive effects, which, in the case of a monopolization claim, will mean actual exclusion and perhaps at least the probability of consequent consumer harm.[239] As discussed *supra*, this may represent a still evolving movement away from the traditional formulation in favor of one that de-emphasizes characterization and focuses more on actual effects and justifications.

As an economic matter, "sacrifice" is not relevant either to the defendant's market power or the fact that its conduct resulted in actual exclusion or consumer harm. Sacrifice simply doesn't tell us anything about either power or effects and makes neither fact more or less probable. Instead, its relevance lies in its value as a *justification* for the defendant's act. More accurately understood, it is the *absence of sacrifice* that is "relevant" in a monopolization claim. Absent sacrifice, the defendant would argue, the conduct should be deemed presumptively efficient despite its effects on rivals and consumers. It is, in other words, an "efficiency" defense, simply recast.

Another question that must be answered, however, before burdens of pleading and proof can be allocated, is whether "efficiency" is a defense or an affirmative defense. In other words, is it relevant because it tends to defeat the evidence of adverse effects on competition, or is it relevant "by way of avoidance," i.e. because it warrants a privilege of sorts. Many factors point in the direction of "affirmative defense."

For example, when plaintiffs address efficiency, they are focused on allocative and consumption efficiency. To again invoke the Williamson diagram, the allocative efficiency losses associated with the challenged conduct's effects on competition are represented by one box. When

defendants – be they merging parties or dominant firms – advocate recognition of efficiencies associated with their conduct, however, they mean *production* efficiencies – a different box. The Williamson diagram makes the first compelling case for treating efficiencies as an affirmative defense – production efficiencies do not directly defeat allocative or consumption inefficiencies. At best, they represent a set of countervailing incentives.

Surely the defendant can, and often will, assert a "defense," as well, by questioning the anticompetitive effects evidence, arguing in effect that there has been no loss of efficiency, and even if there has, that it cannot be attributed to their conduct. That is simply putting the plaintiff's evidence to the test. It is quite different, however, from asking that production efficiencies somehow be viewed as directly diminishing the otherwise negative effects of the conduct. For that reason, I have argued elsewhere that efficiencies be viewed as an affirmative defense, and that defendants should bear the burden of proving them.[240]

Resolving this question is quite critical today throughout antitrust as efficiency has become an increasingly core feature of so much antitrust analysis. It has long been a festering sore in what we call "rule of reason balancing." It is also at the core of merger analysis, and has reappeared in connection with both the disproportionality and rule of reason style balancing approaches being advocated as tests for judging exclusionary conduct. Once the insight of the Williamson diagram is expanded to non-merger areas, the dilemma is posed: how should we judge conduct that simultaneously results in the exercise of market power, i.e. inefficiencies, and the realization of production efficiencies.[241]

The image conjured is of some kind of mythic "scale of competition justice." On one side of the scale we place "anticompetitive effects," and on the other side "procompetitive effects." We then

wait to observe which way the scale tilts. The image has been rightly criticized. First, we are not in truth comparing anticompetitive effects with procompetitive effects, but inefficiencies of one kind with efficiency of another. Hence, the "comparison" is not of equals, although the Williamson diagram can be read to suggest a simple comparison of the size of the competing boxes. Second, the scale model assumes that we have some reasonable mechanism for accurately engaging in a comparative efficiency analysis. It is not clear that we do, and if we did, it is not clear that an accurate comparison of inefficiencies and efficiencies would lead to a clear basis for condemning or approving the conduct. For example, how much improved efficiency for a producer should outweigh how much allocative and consumption inefficiency? Moreover, should we also ask whether and to what extent any production efficiencies will actually be passed along to consumers?[242] And how should we take into account the comparative quality of the evidence? There will inevitably be winners and losers in competition, and the policy basis for choosing anything other than *ascertainable* consumer welfare is uncertain at best.

Perhaps it is not surprising, therefore, that efficiency defenses – be they raised under Section 1, Section 2, or in the context of merger challenges, rarely if ever succeed in the courts. Indeed, despite nearly a century of devotion to the "balancing" concept, in fact there is a remarkable dearth of examples of courts actually engaging in any kind of balancing. For the most part, litigated cases turn on the absence of sufficient evidence of anticompetitive effects (inefficiencies) or of business justifications (efficiencies). One would be hard pressed to find a reported instance in which a court actually attempted to "balance" both.

Another factor that is critical to consider in allocating burdens is the parties' likely access to the necessary evidence. Typically, burdens of pleading and production are allocated to the party

most likely to possess the necessary information.[243] Hence, in the case of monopolization, it is reasonable for a plaintiff to be required to plead and prove both monopoly power and actual anticompetitive effects. At the very least, it is in just as good a position as the defendant to allege and prove the former, and is perhaps better positioned to meet its burdens as to the latter.

The same cannot be said of efficiencies. The information necessary to plead efficiency will almost always lie in the hands of the defendant – beyond the reach of the plaintiff until some opportunity for discovery. To impose the burden of pleading the absence of efficiency on a private party,[244] therefore, is to shift and perhaps elevate the burden of pleading. It is to impose an arguably unsatisfiable, or rarely satisfiable, burden.[245] It is to establish a rule of per se legality.

Nevertheless, there may be some instances in which such extraordinarily high burdens could be justified. To reach that conclusion, however, the legal framework, substantive economics, economic process theory, and legal process must all be aligned.

This kind of alignment may be present in the case of low prices, for example, or truly pure and simple refusals to assist rivals. In both instances, the substantive economic analysis counsels for caution. Low prices can have immediate benefits for consumers, and although the consumer benefits, if any, of refusals to assist rivals are speculative and predictive, they may preserve some important incentives for the dominant firm. From the point of view of economic decision theory, error costs in both areas might be very high. A loss of incentive to lower prices and/or innovate could have very significant and adverse effects on competition. Economic decision theory also highlights administrative and remedial problems, both of which may be present in the case of low prices and some pristine refusals to assist. Surely in the case of low prices, courts should hesitate to use their authority to order increased prices, not only because of its potentially adverse effects on

consumers, but because it will engage the court in potentially complex and ongoing supervision of the firm's pricing. Similarly, as with simple refusals to deal, the court may have to determine the terms, including price, under which a firm may be required to deal, and have to become engaged in continuing oversight. The presence of these factors may indeed warrant imposition of an elevated burden of pleading and proof. In both areas, the law may want to actively discourage claims for fear of the incidence of false positives and their costs.

But that is not the case with many kinds of distribution strategies by dominant firms. As the Supreme Court observed in *Kodak* - distinguishing its facts from those in *Matsushita*: "In this case when we weigh the risk of deterring procompetitive behavior by proceeding to trial against the risk that illegal behavior will go unpunished, the balance tips against summary judgment."[246]

2. A Proposed Synthesis

The quest for a unitary test for defining all exclusionary conduct should be abandoned – not because the economics of exclusion differs by context, it does not. But rather because the teaching of economic and legal process theory strongly suggests that a unitary and inflexible standard will necessarily under or over-deter. As a basic framework for a more flexible approach, I urge three propositions, two that are quite well established, and a third that is not:

1. The Burden of Persuasion Remains With the Plaintiff Throughout a Section 2 Case;
2. But the Burden of Production may shift; and
3. The Allocation of the Burden of Production and Persuasion May Vary With the Nature of the Exclusionary Conduct at Issue.

To illustrate: a plaintiff in a monopolization case will always have to allege and prove that the defendant has monopoly power, and that it has engaged in conduct that has caused actual

anticompetitive effects, or is very likely to do so. Many cases can be weeded out either at the pleading stage or the summary judgment stage based simply on these requirements.

If the plaintiff has met its burden of production on both elements, the questions becomes: should the burden of production shift to the defendant? My proposed answer is: sometimes yes, and sometimes no, and a useful dividing line can be drawn by considering substantive economic, economic decision theory, and legal process.

Fears of false positives, as well as administrative and remedial challenges, are likely to be most pronounced when the conduct produces readily demonstrable short run benefits to consumers and is truly unilateral in nature. Lower prices without any strings are an example, as are improved quality, choice, and innovation. Simple refusals to deal might also be examples, although only in a truly pristine state, and even then it is not clear that they produce clear benefits to consumers in the short run. In such instances, the law should presume that the conduct is legitimate, even though it is undertaken by a monopolist, and even though it results in actual or likely exclusion. In these instances, all factors appear to indicate that claims should be discouraged, and that a rigorous burden of pleading and proof is warranted. For predatory pricing, for example, the sacrifice plus recoupment test might be justifiable. Some elements of *Verizon's* framework might also be justifiable for refusals to assist rivals in heavily regulated industries.

But there is another class of cases where concern for false negative counsels for a less permissive approach. In these cases there is readily demonstrable exclusion, as well as short or long run harm to consumers, or at best an ambiguous impact.[247] Hence, assessing the competitive impact of the conduct can be difficult from an administrative point of view, presenting challenging economic and remedial issues. Typically, the conduct in these cases is not wholly unilateral at all.

Rather it is bi- or multi-lateral, and may itself be rather complex in nature. Examples include loyalty, bundling and market share discounts, capacity shifting behavior like that in *AMR*, and some forms of tying and exclusive dealing.

The distinction between the effects of these kinds of conduct on the one hand and predatory pricing and refusals to assist rivals was highlighted recently by the government in its brief opposing certiorari in *LePage's*. In doing so, the government emphasized two factors overall – the absence of any conflict in the circuits concerning the competitive consequences of bundled rebates, and the prematurity of the challenge – there is as yet no clear consensus among courts and commentators as to the utility of bundled rebates.[248] Yet as to the latter point, the government argued that bundled rebates are distinguishable from predatory pricing, and hence should not be evaluated, as 3M urged, under the elevated standards of *Brooke Group*, which have been justified by fears of false positives and loss of immediate consumer benefits.[249] Indeed, it argued, although "bundled rebates are widespread and are likely, in many cases, to be pro-competitive...the bundling of rebates (as distinct from the price reductions that may result) is not necessarily procompetitive."[250] The brief continues:

> Unlike a low but above-cost price on a single product, a bundled rebate or discount can – under certain theoretical assumptions – exclude an equally efficient competitor, if the competitor competes with respect to but one component of the bundle and cannot profitably match the discount aggregated over the other products, even if the post-discount prices for both the bundle as a whole and each of its components are above cost.[251]

Similarly, some commentators have argued that loyalty discounts cannot be viewed as presumptively procompetitive, as is the case with simple lowering of prices. Although loyalty discounts may result in lower prices to some customers, they may actually lead to higher prices to others. Hence the net consumer welfare consequences of the practice can be difficult to determine, and as with bundled

rebates, are not therefore *necessarily* procompetitive.[252]

In these cases, it would be inappropriate to presume that the conduct is procompetitive and entitled to the kind of deferential treatment accorded predatory pricing and refusals to assist rivals based on fears of false positives. Instead, upon a showing of monopoly power and anticompetitive effects, at least a burden of production should shift to the dominant firm to demonstrate that the practice in fact yields at least some efficiencies. To do otherwise would be to ignore the potential harm such conduct represents in both the short and long run to competition. Moreover, it would place the burden of proving a negative – absence of justification – on the plaintiffs, in cases where it will be difficult for them to do so and where actual harm is already evident. There is, in short, little justification for the kind of deference shown to dominant firms in the false positive cases. Hence, a more healthy skepticism towards after-the-fact claims of efficiency is warranted.

The approach is not radical or new - it is well entrenched in our approach to efficiencies elsewhere, especially in the Merger and Collaboration Among Competitor Guidelines, which credit efficiencies only if they are conduct-specific and verifiable. In both instances, the efficiency inquiry occurs only after significant competitive concern has already been established, and in both cases, the proponent of the efficiency evidence is expected to come forward with it and meet a burden of production, if not persuasion – what I have labeled "inverse *Matsushita* plausibility."[253]

As noted above, most cases will be weeded out before trial for weaknesses related to the plaintiff's assertions with respect to monopoly power or effects. To the extent a small number of cases proceed any further, most will be decided based on lop-sided evidence – lots of harm and little or no efficiency, or little harm and substantial efficiency. The real challenge – and the focal point over disagreements about standards under Section 2 – are the closer cases, which involve conduct

that yields both significant inefficiencies *and* significant efficiencies.

The key to resolving such cases may lie in a sharper understanding of the very traditional role of procedure. Fact finders in the American system are not inquisitors assigned the task of divining "truth." They are at best asked to evaluate a kind of relative truth - truth relative to the facts that have been admitted and proved. Although it may not be very meaningful, therefore, to ask a fact finder to weigh and compare the degree of relative inefficiencies and efficiencies, for centuries fact finders have been asked to "weigh the evidence." The question then is not how inefficiencies and efficiencies can be "weighed" or "compared," but how *evidence* of comparative inefficiencies and efficiencies can be weighed.

Here is where an appreciation for the role of burdens of production (policed by courts) and burdens of proof (policed by fact finders) becomes essential. Although an expert economist might be asked to quantify comparative efficiencies, a jury will not. Typically, the only evidence the jury will receive on comparative efficiencies will be the contrasting testimony of two economists, likely ones with comparable credentials. The plaintiff's economist will testify as to the magnitude of the "inefficiency" box, and either that there is no efficiency box or that it is substantially smaller than the inefficiency box. The defendant's economist's testimony will be quite the opposite. She will opine that the inefficiency box is small or non-existent, and that the efficiency box looms large.[254]

In this context, the jury – indeed any fact finder – will have no reasonable basis for weighing or balancing the inefficiencies and efficiencies.[255] Instead, it will be asked whether the plaintiff and defendant have proved "by a preponderance of the evidence" what the law assigns to them as their respective burdens of proof. If the law assigns the burden of proving anticompetitive effect (i.e. inefficiency) to the plaintiff, the fact finder will evaluate the relative weight, including credibility, of

the testimony on inefficiency and judge whether the plaintiff has carried the day. Conversely, if the law assigns a burden of production or even proof to the defendant as to efficiency, the jury will similarly evaluate the weight, including credibility, of the testimony on efficiency and judge whether the defendant has carried the day. "Balancing" might only be called for in the unlikely event that the fact finder finds credible *both* the plaintiff's evidence of inefficiency and the defendant's evidence on efficiency. In that event, the choice of a balancing as opposed to a disproportionality standard could well make a difference in outcome.

That event seems highly unlikely to arise, however, given the typical course of antitrust cases. The only "balancing" that is likely to be done is a balancing of evidence through the lens of production and credibility. Indeed, that is what juries generally do in the rare case when they actually see a Section 2 case. "Disproportionality" or "balancing" in this context does not mean comparative efficiencies; it means the "weight of the evidence." If the fact finder concludes that the plaintiff should prevail, it should be because the plaintiff's evidence of inefficiencies was far more plausible and well supported than was the defendant's assertion of efficiencies. In this context, the only meaningful way to demand that the plaintiff's proof of anticompetitive effects are disproportionate to the defendant's proof of efficiencies, is to impose a "clear and convincing" evidence standard on the plaintiff – not to ask the fact finder to compare inefficiencies and efficiencies.

The quantity and quality of evidence of inefficiency and efficiency, of course, is likely to vary along a wide range. That is why in the merger context the courts have recognized something of a "sliding scale." The greater the magnitude of the anticompetitive effect and inefficiency demonstrated by the evidence, the greater must be the magnitude of the defendant's proffered efficiency in order to rebut. In *United States v. Baker Hughes, Inc.*, for example, the D.C. Circuit

observed in the merger context that "the more compelling the prima facie case, the more evidence the defendant must present to rebut it successfully."[256] A defendant can "make the required showing," the court continued, "by affirmatively showing why a given transaction is unlikely to substantially lessen competition, or by discrediting the data underlying the initial presumption in the government's favor."[257] This kind of sliding scale has also been advocated under Section 1,[258] and could be readily adapted to Section 2.

CONCLUSION

Antitrust law should not seek to tie the hands of dominant firms when it comes to distribution strategies. But neither should it naively embrace the view that dominant firms can do no harm. In response to challenges from rivals, dominant firms are and should remain free to lower price, improve quality, exploit any greater efficiency they may have, and of course innovate in their products.[259] Given all of the other general benefits of incumbency, if they are truly possessed of skill, foresight and business acumen, that should be enough to fortify and prolong their dominance.

When instead dominant firms choose to respond to rivals with difficult to evaluate distribution strategies that exclude, antitrust law must be a flexible, swift and potent tool to protect competition, especially the kind of competition that is triggered by the entry of new and promising competitors. In contrast to the more standard arsenal of competitive tools, the consumer welfare consequences of these strategies – which as we have seen are for the most part designed to secure some degree of exclusivity – can be difficult to evaluate. As a consequence, courts will rightly proceed cautiously to evaluate them. When the very survival of a competitor is at stake, however, "cautious" is hardly a neutral course. As litigation stretches on – perhaps with no interim injunctive relief – the competitive moment that brought forth the rival may be lost, and along with it the

prospect of new or improved products and services. Later remedies will likely prove inadequate to restore the competition that may have been lost.

Dominant firms know that. They also know that they can exploit that kind of judicial diffidence by pursuing difficult to evaluate distribution strategies, confident that antitrust challenges will be slow and often ineffective. Indeed, one attraction of such strategies may well become the courts' inability to quickly assess them. Judicial hesitance will therefore reward and hence encourage such strategies in lieu of the simple tools of competition that can be more readily evaluated. More lenient judicial attitudes, therefore, will encourage the adoption of more competitively ambivalent strategies, which in turn will erode the incentive for new rivals to challenge incumbent dominant firms. Those strategies, however, may deliver few obvious benefits for competition and substantial risks of long-term harm to the process.

In this context, the oft-repeated mantra that "the antitrust laws are designed to protect competition, not competitors" is an empty slogan. There can be no competition without competitors.[260] If the antitrust laws are rendered impotent to insulate such firms at their most vulnerable time – when they are the obvious targets of complex strategies that have negative or at best ambiguous consumer welfare consequences – we risk the loss of the long term benefits of the process of competition. To protect competitors in such circumstances *is* to protect competition.

If courts err on the side of protecting long-term competition rather than dominant firms in such cases, and such strategies are deterred, dominant firms will hardly be left to the mercy of their challengers. Instead of devising strategies that are likely to prove difficult to assess and hence difficult to judge quickly, they will channel their competitive energies into more clear cut and simple strategies. Indeed, if they do so, courts will be better positioned to identify clear safe harbors for

aggressive competition. Competitors and competition can flourish together, and consumer welfare will be the beneficiary.

In the movie "Spiderman," Uncle Ben Parker offers the following prescient counsel to his nephew Peter Parker, AKA, Spiderman: "With great power comes great responsibility."[261] For the privilege of the license to charge monopoly profits, it is not too much to ask that dominant firms adhere to a higher code of responsibility. Such an expectation is also consistent with widening awareness of corporate irresponsibility outside of antitrust. Exclusionary conduct is, in this sense, just one more kind of corporate irresponsibility, and should not be actively encouraged by unjustifiably lenient antitrust rules.

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1. *See* notes 133-37 and accompanying text, *infra*.

2. United States v. Alum. Co. of America, 148 F.2d 416, 427 (2d Cir. 1945).

3. *Id.* at 430.

4. United States v. United States Steel Corp., 251 U.S. 417 (1920)(alleging that U.S. Steel achieved its monopoly position through a pattern of anticompetitive mergers).

5. American Tobacco Co. v. United States, 328 U.S. 781 (1946)(challenging mergers and acquisitions to monopoly).

6. United States v. Grinnell Corp., 384 U.S. 563 (1966)(challenging acquisition of monopoly power through series of acquisitions and mergers).

7. Standard Oil Co. of New Jersey v. United States, 221 U.S. 1 (1911)(challenging wide range of allegedly predatory conduct designed to maintain the monopoly power of the Standard Oil Trust).

8. Lorain Journal Co. v. United States, 342 U.S. 143 (1951)(adoption of exclusive advertising policy that deprived emerging and competing radio stations of advertising revenue).

9. Otter Tail Power Co. v. United States, 410 U.S. 366 (1973)(refusal to wheel power to emerging rival power companies).

10. United States v. United Shoe Machinery Corp., 110 F. Supp. 295 (D. Mass 1953), *aff'd per curiam*, 347 U.S. 521 (1954)(implementation of lease only policy for shoe manufacturing machines).

11. Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985)(withdrawal of support from cooperative distribution agreement).

12. Eastman Kodak Co. v. Image Technical Svcs, Inc., 504 U.S. 451 (1992)(mandating use by installed base of customers of Kodak photocopier service and repair services).

13. 15 U.S.C. § 1.

14. 15 U.S.C. § 14.

15. 15 U.S.C. § 13.

16. 15 U.S.C. § 2.

17. *See* Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911). The Court in *Dr. Miles* justified its harsh treatment of resale price maintenance largely on grounds related to dealer freedom. *Id.* at 407-09. That rationale has proved remarkably steadfast, and remains influential, albeit primarily in the context of resale price maintenance. *See, e.g.*, Pace Electronics, Inc. v. Canon Computer Systems, Inc., 213 F.3d 118 (3d Cir. 2000)(termination of dealer for failure to adhere to RPM scheme constitutes "antitrust injury" because prohibition of RPM protects dealer pricing autonomy). Although the per se rule of *Dr. Miles* has survived many years of criticism, it has nevertheless been significantly narrowed by Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752 (1984) and Business Electronics Corp. v. Sharp Electronics Corp., 485 U.S. 717 (1988), which together elevated the standard of proof for establishing an agreement to maintain minimum resale prices.

18. *See* Albrecht v. Herald Co., 390 U.S. 145 (1968), *overruled by* State Oil Co. v. Khan, 522 U.S. 3 (1997).

19. United States v. Arnold Schwinn & Co., 388 U.S. 365 (1967)(extending per se rule to vertical intrabrand non-price restraints).

20. *See, e.g.*, International Business Machines Corp. v. United States, 298 U.S. 131 (1936); International Salt Co. v. United States, 332 U.S. 392 (1947); Northern Pacific Ry. Co. v. United States, 356 U.S. 1 (1958)(tying per se illegal).

21. *See* Standard Oil Co. v. United States, 337 U.S. 293 (1949)("*Standard Stations*").

22. This reliance on contract and property rights is developed in RUDOLPH J.R. PERITZ, COMPETITION POLICY IN AMERICA 1888-1992: HISTORY, RHETORIC, LAW (1996). *See also* James May, *Antitrust in the Formative Era: Political and Economic Theory in Constitutional and Antitrust Analysis, 1880-1918*, 50 OHIO ST. L.J. 257 (1989).

23. Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36 (1977)(overruling *Arnold, Schwinn*, and re-establishing rule of reason as standard for judging non-price intrabrand restraints).

24. The Court also cited: (4) insulating a supplier from product liability exposure by implementing safety standards in connection with a product; and (5) protecting a supplier's reputation by guaranteeing product quality. *Id.* at 55 & n.23.

25. *Id.* at. 52 n.19.

26. *Id.* ("[W]hen interbrand competition exists...it provides a significant check on the exploitation of intrabrand market power because of the ability of consumers to substitute a different brand of the same product").

27. In theory, at least, the "quality adjusted price" would remain the same, owing to the increased benefits consumers would receive from the enhanced services and promotional information.

28. 433 U.S. at 56 & n.24 (manufacturer has interest in minimizing its costs of distribution, which will tend to strengthen its interbrand competitive position).

29. *Sylvania's* lack of analytical guidance was quickly recognized by some commentators. *See, e.g.*, Richard A. Posner, *The Rule of Reason and the Economic Approach: Reflection on the Sylvania Decision*, 45 U. CHI. L. REV. 1, 14 (1977) ("The content of the Rule of Reason is largely unknown; in practice, it is little more than a euphemism for nonliability. Before *Schwinn*, restrictions on distribution were tested under the Rule of Reason, meaning: they were lawful.").

Yet *Sylvania* strongly implies that if a plaintiff can demonstrate that its supplier possesses market power, the burden of production should shift to the defendant to justify its conduct. Under a strict reading of *Sylvania*, however, it is hard to see how any justification would suffice. Absent the check of interbrand competition, vertical restraints that have the effect of eliminating intrabrand competition will surely lead to higher quality adjusted prices. Can they still be justified as addressing free rider problems? To guarantee safety and quality? Almost 30 years after *Sylvania*, these very fundamental questions remain unanswered. Moreover, *Sylvania* provided little guidance for evaluating intrabrand restraints in industries that do not appear to be experiencing free rider problems, or other conditions that might justify the use of intrabrand restraints. To put it in procedural terms: should a plaintiff (most likely a complaining or terminated dealer) be able to shift a burden of production to a restraining supplier by demonstrating a significant diminution in intrabrand competition and a consequent rise in prices?

30. *See* Graphic Products, Inc. v. ITEK Corp., 717 F.2d 1560 (11th Cir. 1983)(striking down vertical intrabrand non-price restraints after finding that supplier had 70% market share). *Cf.* Eiberger v. Sony Corp., 622 F.2d 1068 (2d Cir. 1980)(condemning vertical intrabrand non-price restraints for apparent absence of any justification). As a practical matter, therefore, vertical intrabrand non-price restraints have become per se lawful since *Sylvania*. *See* Douglas H. Ginsburg, *Vertical Restraints: De Facto Legality Under the Rule of Reason*, 60 ANTITRUST L.J. 67 (1991).

31. By today's standards, *Sylvania's* seemingly unidimensional focus on interbrand competition as the sole check on market power would seem to be outmoded. Ease of entry, sales of complements, and other factors, such as efficiencies, might also serve to ameliorate, in whole or part, the dominant firm's incentive and ability to exercise market power. Although the absence of significant interbrand rivalry might, therefore, be deemed sufficient to shift a burden of

production to the dominant firm, the range of justifications for intrabrand restraints by dominant firms might be more expansive today. To be sure, however, these other justifications might not be as potent a means to offset the tendency to raise price as would the presence of interbrand rivalry, which was deemed so critical in *Sylvania*.

32. The "collusive" and "exclusionary" effects terminology is explained more fully in ANDREW I. GAVIL, WILLIAM E. KOVACIC & JONATHAN B. BAKER, ANTITRUST LAW IN PERSPECTIVE: CASES, CONCEPTS AND PROBLEMS IN COMPETITION POLICY 44-47 (2002)("GAVIL, KOVACIC & BAKER").

33. For a more complete discussion of the differences between intra and inter-brand restraint analysis, *see* GAVIL, KOVACIC & BAKER, *supra* note 32, at 689-91.

34. For a general discussion of such strategies, and an argument that they should be analyzed like any other exclusionary conduct, *see* Willard K. Tom, et al., *Anticompetitive Aspects of Market Share Discounts and Other Incentives to Exclusive Dealing*, 67 ANTITRUST L.J. 615 (2000).

35. *See, e.g.*, Standard Stations, 337 U.S. at 305-07 (discussing possible competitive benefits of exclusive dealing and contrasting it with tying).

36. *Id.*, at 314 (condemning exclusive dealing contracts even though they affected only 6.7% of relevant market).

37. *See, e.g., Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984)(O'Connor, J., concurring)("Exclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal.")

38. *See, e.g.*, Western Parcel Express v. United Parcel Service of America, Inc., 190 F.3d 974 (9th Cir. 1999); Omega Envt'l, Inc. v. Gilbarco, Inc., 127 F.3d 1157 (9th Cir. 1997); U.S. Healthcare, Inc. v. Healthsource, Inc., 986 F.2d 589 (1st Cir. 1993); United States v. Dentsply Int'l, Inc., 277 F.Supp.2d 387 (D. Del. 2003), *appeal pending*. Consistent with the literature on raising rivals' costs to obtain power over price, these cases increasingly focus on the probability that exclusive dealing will facilitate the exercise of market power rather than simply inferring anticompetitive effect based on some arbitrary degree of "foreclosure." *See generally* GAVIL, KOVACIC & BAKER, *supra* note 32, at 731-40 (discussing contemporary law and economics of exclusive dealing); Jonathan M. Jacobson, *Exclusive Dealing, "Foreclosure," and Consumer Harm*, 70 ANTITRUST L.J. 311 (2002).

39. *Jefferson Parish*, 466 U.S. at 13-14.

40. In this section I primarily focus on the offense of monopolization. Attempt to monopolize has similarly been stable, especially since Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447 (1993), where the Court clarified that the offense of attempt to monopolize has three elements: (1) predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a

dangerous probability of achieving monopoly power. Because monopolization and attempt to monopolize converge around the core notion of "predatory" or "exclusionary" conduct, the definition of exclusionary conduct will be central to both offenses.

41. *Id.* at 391.

42. United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377 (1956).

43. *See generally* GAVIL, KOVACIC & BAKER, *supra* note 32, at 575-76.

44. *Standard Oil*, 221 U.S. at 33 (monopoly power inferred from 90% market share and other direct evidence of control).

45. United States v. American Tobacco Co., 221 U.S. 106, 157-58 (1911)(monopoly inferred from 90+% market share).

46. United States v. International Harvester, 214 F. 987, 991 (D. Minn. 1914) (85% percent market share deemed sufficient to infer monopoly power). A direct appeal to the Supreme Court was dismissed pursuant to a consent decree, see International Harvester Co. of New Jersey v. U.S., 248 U.S. 587 (1918), and a later petition by the government for additional relief was denied. *See* United States v. International Harvester Co., 274 U.S. 693, 695 (1927).

47. *United States Steel*, 251 U.S. at 439 n.1, 444-45 (41% market share insufficient to support finding of monopoly).

48. Standard Oil Co. (Indiana) v. United States, 283 U.S. 163, 176-77 (1924)(26 percent market share insufficient to support finding of monopoly).

49. Appalachian Coals, Inc. v. United States, 288 U.S. 344, 373-76 (1933)(market shares between 12 and 54%, and no more than 64%, deemed insufficient to infer market power).

50. *DuPont (Cellophane)*, 351 U.S. at 379. *See also* Andrew I. Gavil, *Copperweld 2000: The Vanishing Gap Between Sections 1 and 2 of the Sherman Act*, 68 ANTITRUST L.J. 87, 102-04 (2000)(noting that case law appears to support this 70% threshold).

51. NCAA v. Bd. of Regents, 468 U.S. 85, 109-10 (1984)(plaintiff need not prove anticompetitive effects by first defining a relevant market, calculating market shares and inferring market power, when evidence of actual anticompetitive effects which could only be perpetrated by a firm with market power is present).

52. FTC v. Indiana Fed'n of Dentists, 476 U.S. 447, 460-61 (1986)(market power established through inference from market shares is mere "surrogate" and need not be shown when evidence of actual anticompetitive effects is presented).

53. *See generally* Gavil, *Copperweld 2000*, *supra* note 50, at 95-102.

54. Eastman Kodak Co. v. Image Tech. Servs., Inc., 504 U.S. 451, 469 n.15 (1992). *See also* Steven C. Salop, *The First Principles Approach to Antitrust, Kodak, and Antitrust at the Millennium*, 68 ANTITRUST L.J. 187 (2000)(using *Kodak* to illustrate the point that the market power and anticompetitive effects inquiries are necessarily intertwined).

55. *See, e.g.*, In the Matter of Schering-Plough Corp., Dkt. No. 9297, at 16-17 (F.T.C. 2003)(available at http://www.ftc.gov/os/adjpro/d9297/031218commissionopinion.pdf) (discussing importance of direct evidence of effects of impaired generic drug entry); In the Matter of Polygram Holding, Inc., Dkt. No. 9298, at 20-21 & n.26 (FTC July, 28, 2003)(available at http://www.ftc.gov/os/2003/07/polygramopinion.pdf)("*3 Tenors*").

56. *See, e.g.*, Re/Max Int'l v. Realty One, Inc., 173 F.3d 995, 1018 (6th Cir. 1999)("We agree that an antitrust plaintiff is not required to rely on indirect evidence of a defendant's monopoly power, such as high market share within a defined market, when there is direct evidence that the defendant has actually set prices or excluded competition"). The court went on to observe: "we see no reason to believe that monopoly power in the § 1 context is any different from the § 2 monopoly power the plaintiffs allege here." *Id.* at 1019. *But see* Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 336 (2003)(arguing for continued relevance of market shares in evaluating claims of monopolization and advocating threshold of 50%).

57. United States v. Microsoft Corp., 253 F.3d 34, 51-58 (D.C. Cir. 2001).

58. *Eastman Kodak*, 504 U.S. at 481 ("Monopoly power under § 2 requires, of course, something greater than market power under § 1.").

59. *See* Gavil, *Copperweld 2000*, *supra* note 50, at 102 & n.61.

60. *See, e.g.*, Toys R Us, Inc. v. FTC, 221 F.3d 928, 937 (7th Cir. 2000)(the challenged conduct "was remarkably successful in causing the 10 major toy manufacturers to reduce output of toys to the warehouse clubs, and that reduction in output protected TRU from having to lower its prices to meet the clubs' price levels."). *Toys R Us* involved both collusive and exclusionary effects. There is no doubt that the challenged conduct had the effect of excluding rivals, but the court also emphasized the degree to which it led to collusive effects, i.e. cartel-like behavior by the manufacturers. *Id.*

61. *See, e.g.*, FTC v. Staples, Inc., 970 F. Supp.1066, 1082 (D.D.C. 1997):

> The HHI calculations and market concentration evidence, however, are not the only indications that a merger between Staples and Office Depot may substantially lessen competition...The fact that Staples and Office Depot both charge higher prices where they face no superstore competition demonstrates that an office

superstore can raise prices above competitive levels.

Staples also illustrates, as did *Toys R Us* and *Microsoft*, how direct evidence of the actual exercise of market power can be relevant to both the market power and adverse effects elements of an antitrust offense. *Id.* ("Much of the evidence already discussed with respect to defining the relevant product market also indicates that the merger would likely have an anti-competitive effect."). *See also* GAVIL, KOVACIC & BAKER, *supra* note 32, at 813-22 (discussing direct measures of market power and anticompetitive effect).

62. *See generally Id.*, at 791-810 (excerpting and discussing cases relying upon direct evidence of collusive and exclusionary effects).

63. Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574 (1986)(rejecting as economically implausible claim of 20 year plus conspiracy to engage in predatory pricing by Japanese electronics manufacturers).

64. Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993)(granting judgment as a matter of law on predatory pricing claim for want of plausible theory of recoupment).

65. *Matsushita*, 475 U.S. at 584 n.8 ("'predatory pricing' means pricing below some appropriate measure of cost"); *Brooke Group*, 509 U.S. at 222 (holding that predatory pricing plaintiff must demonstrate that defendant priced "below an appropriate measure of its rival's costs," but declining to "resolve the conflict among the lower courts over the appropriate measure of cost" because "the parties in this case agree that the relevant measure of cost is average variable cost."). *See also* Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 117 (1986). Since Areeda and Turner's watershed work in the field, there has been considerable academic debate about the appropriate measure of cost that should guide the predatory pricing inquiry. *See* GAVIL, KOVACIC & BAKER, *supra* note 32, at 620-25 (discussing "The Economic Debate About Predatory Pricing: A Short History"). Although *Brooke Group* comes close to endorsing the average variable cost test advocated by Areeda and Turner, *see Brooke Group*, 509 U.S. at 222 n.1, nearly 20 years after *Matsushita*, the precise measure of cost remains undetermined. *See, e.g.*, United States v. AMR Corp., 335 F.3d 1109, 1116-21 (10th Cir. 2003)(rejecting four different methodologies proffered by the government to measure cost, but embracing no alternative).

66. *Matsushita*, 475 U.S. at 588-89; *Brooke Group*, 509 U.S. at 224.

67. *Matsushita*, 475 U.S. at 589; Brooke Group, 509 U.S. at 224-26. This now standard paradigm may be inadequate, therefore, to explain pricing strategies that either do not involve significant losses, or which permit immediate or simultaneous recoupment. In such cases, the risk of loss is minimized and hence the "plausibility" of the strategy is no longer as readily

discounted. *See, e.g.*, GAVIL, KOVACIC & BAKER, *supra* note 32, at 620-25 (discussing modern recoupment theories).

68. *Matsushita*, 475 U.S. at 589.

69. *Brooke Group*, 509 U.S. at 223 ("the exclusionary effect of prices above a relevant measure of cost either reflects the lower cost structure of the alleged predator, and so represents competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting.")

70. *Matsushita*, 475 U.S. at 587.

71. *See* notes 197-210 and accompanying text, *infra*.

72. *See, e.g.*, *Matsushita*, 475 U.S. at 589 (citing various commentators and noting "consensus").

73. *See, e.g.*, ROBERT H. BORK, THE ANTITRUST PARADOX 149-55 (1978); Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975); Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263 (1981).

74. *Id.*

75. *See, e.g.*, Aaron Edlin, *Stopping Above Cost Predatory Pricing*, 111 YALE L.J. 941 (2002). For a reply to Professor Edlin, *see* Einer Elhauge, *Why Above-Cost Price Cuts to Drive Out Entrants Are Not Predatory – and the Implications for Defining Costs and Market Power*, 112 YALE L.J. 681 (2003).

76. *But see* Star Fuel Marts, LLC v. Sam's East, Inc., 362 F.3d 639 (10th Cir. 2004)(rejecting imposition of *Brooke Group*-styled recoupment requirement 2-1 and hence upholding district court's issuance of preliminary injunction against below-cost pricing in action brought under Oklahoma Unfair Sales Act).

77. As the court observed in United States v. AMR Corp., 335 F.3d 1109 (10th Cir. 2003), "[r]ecent scholarship has challenged the notion that predatory pricing schemes are implausible and irrational." *Id.* at 1114, *citing* Patrick Bolton, et al., *Predatory Pricing: Strategic Theory and Legal Policy*, 88 GEO. L. J. 2239, 2241 (2000); and Jonathan B. Baker, *Predatory Pricing After Brooke Group: An Economic Perspective*, 62 ANTITRUST L.J. 585, 590 (1994).

Indeed, even on their own terms, *Matsushita* and *Brooke Group* are subject to criticism. For example, as to *Matsushita*, it is at least debatable whether the "economic plausibility" of the alleged predatory pricing conspiracy should have been taken from the jury by the mechanism of summary judgment. *See, e.g., Matsushita*, 475 U.S. at 598, 601 (White, J., dissenting)("In

defining what respondents must show in order to recover, the Court makes assumptions that invade the factfinder's province."). Similarly, the Supreme Court's decision in *Brooke Group* can be faulted for awarding judgment as a matter of law with respect to plaintiff's theory that the defendant would be able to recoup its losses through future oligopolistic pricing, which was supported by documents discovered from the defendant's own files. *Brooke Group*, 509 U.S. at 243, 257-58 (Stevens, J., dissenting). *See also* Baker, *Predatory Pricing After Brooke Group*, 62 ANTITRUST L.J. at 598-602 (disputing Court's reasoning as to recoupment based on the evidence presented).

78. *Aspen Skiing*, 472 U.S. at 605.

See notes 93-96 and accompanying text, *infra*.

80. *NCAA*, 468 U.S. at 107 ("Congress designed the Sherman Act as a 'consumer welfare prescription.'"), *quoting Reiter v. Sonotone Corp.*, 442 U.S. 330, 343, (1979).

81. *Aspen Skiing*, 472 U.S. at 605-07.

82. *NCAA*, 468 U.S. at 107 ("Price is higher and output lower than they would otherwise be, and both are unresponsive to consumer preference.")

83. *Kodak*, 504 U.S. at 465 ("Respondents...allege...that Kodak service was of higher price and lower quality than the preferred ISO service.").

84. As Jonathan Baker has argued, *Aspen* and *Kodak* together suggest that an inference of anticompetitive harm from a monopolists' conduct can be drawn from several factors present in both cases: (1) a rival was substantially excluded by the defendant's conduct; (2) the mechanism for doing so was the disruption of a collaborative or complementary relationship that previously existed between the monopolist and the rival; and (3) the monopolist lacked a valid business justification for its actions. *See* Jonathan B. Baker, *Promoting Innovation Competition Through the Aspen/Kodak Rule*, 7 GEO. MASON L. REV. 495, 500-03 (1999). For a reply, which rejects the inference of harm based on absence of business of justification, *see* Timothy J. Muris, *The FTC and the Law of Monopolization*, 67 ANTITRUST L.J. 693, 699 (2000)(arguing that *Aspen* in fact looked at harm to consumers, and that the issue of harm was not before the Court in *Kodak*, which was decided on summary judgment). *See also* Dennis W. Carlton, A *General Analysis of Exclusionary Conduct and Refusal To Deal – Why Aspen and Kodak are Misguided*, 68 ANTITRUST L.J. 659 (2001).

85. *See, e.g., Microsoft*, 253 F.3d at 64 ("although Microsoft did not bar its rivals from all means of distribution, it did bar them from the cost-efficient ones.")

86. *See, e.g*, ANTITRUST GUIDELINES FOR COLLABORATIONS AMONG COMPETITORS § 3.36(b), at 24 (2000)(available at http://www.ftc.gov/os/2000/04/ftcdojguidelines.pdf); HORIZONTAL

MERGER GUIDELINES, §4 (rev. 1997)(available at http://www.usdoj.gov/atr/public/guidelines/hmg.htm).

87. *Aspen Skiing*, 472 U.S. at 608.

88. *Kodak*, 504 U.S. at 483-86.

89. *Aspen Skiing*, 472 U.S. at 608.

90. *See* notes 197-210 and accompanying text, *infra*.

91. *Aspen Skiing*, 472 U.S. at 611-12.

92. *See* notes 214-223 and accompanying text, *infra*.

93. *Microsoft*, 253 F.3d at 58-59 (citations omitted).

94. This was true, for example, with respect to almost all of Microsoft's license restrictions with OEMs. *Microsoft*, 253 F.3d at 58-64 ("[W]e hold that with the exception of the one restriction prohibiting automatically launched alternative interfaces, all the OEM license restrictions at issue represent uses of Microsoft's market power to protect its monopoly, *unredeemed by any legitimate justification.*" *Id.* at 64 (emphasis added)). Similarly, the court held with respect to two of the three challenged acts relating to Microsoft's integration of its Internet browser into its Windows operating system that Microsoft "proffer[ed] no justification." *Id.* at 66. The D.C. Circuit also affirmed the district court's finding of a Section 2 violation with respect to Microsoft's exclusive dealing arrangements with Internet Access Providers because Microsoft failed to offer any *procompetitive* justification. *Id.* at 71. The court also found anticompetitive effect and no justification as to Microsoft's deals with Independent Software Vendors, *id.*, its dealings with Apple, *id.* at 72-74, and its conduct directed at Sun's Java programming language. *Id.* at 74-78.

95. An example is the court's conclusion that the plaintiffs had "failed to demonstrate that Microsoft's deals with ICPs [Internet Content Providers] have a substantial effect upon competition." 253 F.3d at 71. The court came closest to actual balancing in its treatment of Microsoft's prohibition of the launching of a substitute user interface upon completion of the boot sequence, holding that "a shell that automatically prevents the Windows desktop from ever being seen by the user is a drastic alteration of Microsoft's copyrighted work, and *outweighs the marginal anticompetitive effect* of prohibiting the OEMs from substituting a different interface automatically upon completion of the initial boot process." 253 F.3d at 63. However, this is more an example of disproportionality than true "balancing," because the court found the anticompetitive effect to be "marginal," whereas the justification was substantial. The court outright reversed and remanded the government's tying and attempt to monopolize claims, making no effort to compare effects and justifications – in the case of tying, for the district

court's error in applying the per se rule, 253 F.3d at 45-55, and in the case of attempt to monopolize, for failure to prove a relevant market for Internet browsers. *Id.* at 40-44.

96. This was true with respect to one aspect of Microsoft's integration of its Internet browser into Windows, its provision for an override of the user's choice of a non-Microsoft default browser, for which it argued "valid technical reasons." 253 F.3d at 67. The court responded: "The plaintiff bears the burden not only of rebutting a proffered justification but also of demonstrating that the anticompetitive effect of the challenged action outweighs it. In the District Court, plaintiffs appear to have done neither, let alone both; in any event, upon appeal, plaintiffs offer no rebuttal whatsoever." *Id.*

97. The cases are: United States v. AMR Corp., 335 F.3d 1109 (10th Cir. 2003); LePage's Inc. v. 3M Co., 324 F.3d 141 (3rd Cir. 2003); Pepsico, Inc. v. Coca-Cola, Co., 315 F.3d 101 (2nd Cir. 2002); Conwood Co. v. U.S. Tobacco Co., 290 F.3d 768 (6th Cir. 2002); United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001); Virgin Atlantic Airways Ltd. v. British Airways PLC, 257 F.3d 256 (2nd Cir. 2001); and Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039 (8th Cir. 2000).

98. None of these cases involved challenges, therefore, to *Sylvania* style vertical intrabrand restraints, either price or non-price.

99. *See AMR*, 335 F.3d at 1112 (lower pricing, capacity shifting and yield management utilized in response to new entry by low cost carrier in airline's Dallas-Fort Worth hub); *LePage's*, 324 F.3d at 147 (bundled rebates and exclusive dealing); *Pepsico*, 315 F.3d at 104 (loyalty provisions of distribution contracts); *Conwood*, 290 F.3d at 773-80 (exclusive product display racks and misuse of category management); *Microsoft*, 253 F.3d at 59-78 (restrictive licensing, product integrations, rebates and promotions, tying, exclusive dealing, threats to withdraw cooperation, deception); *Virgin Atlantic*, 257 F.3d at 261-62 (structured incentives and discounts with travel agents and corporate customers); and *Concord Boat*, 207 F.3d at 1044-45 (market share, long-term, and volume discounts).

100. *See AMR*, 335 F.3d at 1113; *LePage's*, 324 F.3d at 145; *Pepsico*, 315 F.3d at 104; *Conwood*, 290 F.3d at 773-80; *Microsoft*, 253 F.3d at 47; *Virgin Atlantic*, 257 F.3d at 259; and *Concord Boat*, 207 F.3d at 1045-46.

101. *LePage's*, 324 F.3d at 146 ("3M concedes it possesses monopoly power in the United States transparent tape market, with a 90% market share"); *Conwood*, 290 F.3d at 783 n.2 ("USTC enjoyed 74 to 77 percent market power nationwide in the moist snuff industry...[and] neither challenges this finding nor argues that it does not possess monopoly power"); *Microsoft*, 253 F.3d at 54 (market share of 95% sufficient to support inference of market power). One arguable exception was *Concord Boat*, where the defendant's share was alleged to be 75% and the defendant still prevailed. But that share actually dropped after the challenged conduct began to a low of 50%. *See* 207 F.3d at 1044-45.

102. *See, e.g.*, *Pepsico*, 315 F.3d at 109 (64% market share insufficient to infer monopoly power, especially where market definition was rejected and there was no direct evidence that defendant had ability to control prices or exclude competition); *Virgin Atlantic*, 257 F.3d at 271 (60% market share insufficient because based on routes that covered only 17% of capacity).

103. In *Conwood*, for example, the destruction of Conwood's display racks by UST cost Conwood in excess of $100,000 per month plus substantial policing and administrative time. *Conwood*, 290 F.3d at 778. *Microsoft* is another obvious example. *See Microsoft*, 253 F.3d at 64 ("although Microsoft did not bar its rivals from all means of distribution, it did bar them from the cost-efficient ones."). *See also* Steven C. Salop & R. Craig Romaine, *Preserving Monopoly: Economic Analysis, Legal Standards, and Microsoft*, 7 GEO. MASON L. REV. 617, 626-42 (1999)(discussing economics of exclusion in the context of Microsoft's use of input foreclosure, customer foreclosure, and use of credible predatory threats). As Professor Edlin has observed, loyalty rebates may also raise rivals' costs, serving as a subterfuge for exclusivity. Edlin, *supra* note 75, at 698 n.53. *See also* Tom, et al., *supra* note 34, at 617, 627-30 (discussing effects of raising rivals' costs in exclusivity and how discounts and incentives can lead to partial or total exclusivity that is anticompetitive.); Thomas G. Krattenmaker & Stephen C. Salop, Anticompetitive Exclusion: Raising Rivals' Costs To Achieve Power over Price, 96 Yale L.J. 209 (1986) (describing how foreclosure can raise rivals' costs and facilitate exercise of market power).

104. Like raising rivals' costs, reducing rivals' revenues may be an effect of exclusivity in a variety of contexts. Conduct such as the bundled rebates in *LePage's* and the capacity shifting and yield management in *AMR*, however, are examples of exclusionary strategies that specifically reduce rivals' revenues, perhaps to the point where they fall below the minimum scale required to compete effectively. UST's destruction of Conwood's display racks, which raised its costs, also directly resulted in lost sales and profits, reducing its revenues. *Conwood*, 290 F.3d at 778-79.

105. Microsoft's threat to withdraw support for Microsoft Office unless Apple agreed to abandon its use of Netscape's Internet browser, *Microsoft*, 253 F.3d at 72-74, its deception of Java developers, *Id.* at 76-77, and its threat to abandon distribution of Intel technologies unless Intel abandoned its development of a Java-cross-platform compatible virtual machine, *Id.* at 77-78, all appear to have been relatively costless examples of exclusionary conduct. The destruction of competitors' display racks in *Conwood* also appears to be an example of relatively costless exclusionary conduct. *Conwood*, 290 F.3d at 778-80.

106. The most obvious examples of strategies involving sacrifice appear to be those that involve reduced prices, discounts or rebates, such as *LePage's*, *Pepsico*, *Concord Boat*, and *American Airlines*. However, if the discount or rebate is only offered to some customers and not to others, the "sacrifice" can be minimized or even eliminated. In other words, there may be a mechanism for immediately recouping any losses, which diminishes the "sacrifice" required to achieve the exclusionary result. *See, e.g.*, Edlin, *supra* note 75, at 956-60 (discussing various price-lowering schemes that may not involve sacrifice).

There may also be costs involved in the purchase of more traditional exclusionary rights, such as through simple exclusive dealing. Such costs, however, may also likely take the form of some kind of payment, discount or rebate. *See, e.g.*, *LePage's*, 324 F.3d at 157 ("LePage's claims that 3M made payments to many of the larger customers that were designed to achieve sole source status."). *See also* Krattenmaker & Salop, *supra* note 103, at 227-28 (discussing nature of "exclusionary rights."). In these cases, the dominant firm is securing exclusionary rights by sharing part of the gains it receives from the exercise of market power that they facilitate.

107. Microsoft's product integration, for example may have benefitted consumers in the short run. Consumers may also have benefitted in the short run from 3M's bundled rebates, although that is not necessarily the case. And consumers probably benefitted in the short run from American Airlines's shift of capacity and reduction in fares in its Dallas-Ft. Worth hub.

108. It is difficult to see how consumers could have benefitted at all from UST's challenged conduct in *Conwood*, and many aspects of Microsoft's behavior likely had either no benefit for consumers or harmed them. For example, although product integration may have been beneficial for consumers, lack of interoperability, which is not necessary to achieve integration, clearly renders the market less responsive to consumer choice, and hence is not. Neither does it appear that Microsoft's various licensing restrictions and efforts to secure exclusivity benefitted consumers in any way. Not surprisingly, therefore, as noted *supra*, Microsoft proffered no procompetitive justification for much of its conduct. Finally, if loyalty and bundled product rebates result in higher prices to those not meeting the rebate conditions, they may not involve net benefits to consumers.

109. *See LePage's*, 324 F.3d at 162 ("3M's exclusionary conduct not only impeded LePage's ability to compete, but also harmed competition itself"); *Conwood*, 290 F.3d at 789-90 ("there was evidence showing that USTC's actions caused higher prices and reduced consumer choice" and that it also restricted the growth of rivals' market share); *Microsoft*, 253 F.3d at 59-80 (extensive discussion of impact of specific Microsoft conduct on both rivals and consumers).

110. The sole exception might be *Microsoft*, where the defendant secured a complete reversal of the attempt to monopolize claims, 253 F.3d at 80-84, and some of the more minor monopolization claims, *see* notes 95-96, *supra*, and secured a reversal and remand of the tying claims. *Id.* at 84-95. The government prevailed, however, on the core of its monopolization case. *Id.* at 50-80.

111. *See LePage's*, 324 F.3d at 146 (monopoly power conceded); *Conwood*, 290 F.3d at 782 (monopoly power conceded); *Microsoft*, 253 F.3d at 51-58 (finding of monopoly power affirmed "in its entirety" based on combination of circumstantial and direct evidence).

112. *See* note 109, *supra*.

