ADAM SMITH, MODERN NETWORKS AND THE GROWING NEED FOR ANTITRUST RATIONALITY ON COMPETITOR COOPERATION[1]

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Abstract: *As the business world has become more global in scope and more interdependent in operations, it has generated competing pressures on the antitrust system in the United States and elsewhere–pressures to distinguish more clearly between old fashioned "conspiracies" and modern forms of "de facto partnership". First, competing businesses must increasingly cooperate in setting standards, providing network interconnections and pooling patents. Secondly, global networking creates more incentives and opportunities for competitors to engage in larger (and potentially more effective) cartels to fix prices and divide markets around the world. This article seeks to explain how antitrust law must be clear, strong, and penal if it is to effectively curb and deter the great modern cartel threat, while at the same time becoming clearer and less penal if it is to avoid becoming a significant deterrent to effective cooperation that can promote both efficiency and consumer welfare in a modern economy. We outline some potential steps that could be taken by enforcers, judges and legislators to provide greater clarity and reassurance to legitimately cooperating competitors.*

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I. AN AMBIGUOUS HISTORICAL LEGACY CONCERNING COMPETITORS

In 1776, Adam Smith, then the most famous economic thinker in the English speaking world, published his economic treatise *The Wealth of Nations*–which included a memorable, oft-repeated warning about the prevalence of cartels: "People of the same trade seldom meet, even for merriment or diversion, but the conversation ends in a conspiracy against the public or in some contrivance to raise prices."[4] One hundred and fourteen years later, the US Congress passed, virtually unanimously, a statute that could have been more appropriately dedicated to Adam Smith, rather than John Sherman. With sweeping simplicity, the law declared that any "contract, combination, or conspiracy . . . in restraint of trade" was a crime that could also be enjoined and subjected to private suits for treble damages.

Today the legacies of Adam Smith and John Sherman live on, as sources of inspiration and confusion, in an economic world that is totally different from anything that they could have even imagined. In our modern service-oriented economies, competitors frequently find themselves interconnected and interdependent in ways that could not have been imagined over a century ago, let alone two centuries ago.

Thus, the challenge for today is to remember that Adam Smith's memorable warning remains highly relevant in age of large global cartels–while allowing competing enterprises to cooperate with each other in setting technical standards, pooling blocking patents, or starting new networks, without their antitrust fears being unnecessarily magnified by Dr. Smith's rhetoric or Senator Sherman's vagueness.

Thus, without losing sight of the serious danger that genuine cartels pose for the world economy, we will try here to review some ways that antitrust uncertainties to productive competitor cooperation might be reduced. Enforcers, judges, and legislators could all play constructive roles in such efforts.

II. THE MODERN PRESSURE FOR COOPERATION AMONG THOSE WHO COULD COMPETE

There are many instances in today's modern economy where the need for cooperation among competitors is clear. Contrary to what some prior

4 Cited in: *United States v. Realty Multi-List, Inc.*, 629 F.2d 1351, 1370 (5th Cir. 1980).

antitrust rulings might suggest, cooperation among competitors is not always suspect. To the contrary, various forms of competitor cooperation can foster innovation, technological advances, and greater market efficiencies. Although we do not present this as an exhaustive list, the following are some of the clearer instances where cooperation among competitors can be advantageous not only for them but for the consuming public:

- *When standardization is needed to facilitate technical interoperability.* Industry standards are a familiar, and ever more important, aspect of the modern world. They may run the range from simple standards for fundamental interchangeability requirements (like railway gauges or electric outlets) to highly technical interfaces on specialized computer networks.
- *When competitors can effectively cooperate and assist each other with research, innovation, and/or complementary development efforts.* Modern research and development can involve very large efforts requiring numerous individuals and/or enterprises working together to try to create a new state-of-the-art product.[5] The Manhattan Project to develop the atomic bomb during World War II was the quintessential, involving at least three major chemical companies pursuing alternative innovation routes. But just developing a large new aircraft or jet engine can require a lot of cooperation among sometimes-competing partners.
- *Patent pools, including those involving blocking or complimentary intellectual property rights.* The problem of blocking patents generated by competitive innovations will often require a patent pool as a way of creating and granting clean licenses which are more useful to licensees and more profitable to the IP owners is just one example.[6] A package of complementary IP rights (such as musical copyrights) may be a lot more efficient than having creators and users engage in a large number of bilateral licenses.
- *Consortia for sharing very large risks.* Examples can be traced back as far as the voyages of discovery in the 16th Century, but the risk-sharing reality has flourished across a broad range of industries in modern economies.

5 The U.S. has enacted a special antitrust statute to encourage such efforts. National Cooperative Research and Production Act, 15 U.S.C. §§ 4301-06 (1984).

6 The competitive situation and the antitrust concerns can be quite different when a pool includes *competitive* patents, because then pooling can deprive potential licensees of competitive alternatives.

Insurance consortia are extremely common, as are joint lending and underwriting consortia among banks on very large loans and securities offerings.

- *Very large capital projects.* These can require multiple bidders/contractors just to assure that the project can be completed in a timely fashion. For a contractor, this multiple participants approach can help avoid the "all our eggs in one basket" problem that might otherwise exist.
- *Sports Leagues.* These usually involve independently owned teams cooperating in establishing a league to provide rules, schedules and referees for the contests among the teams. This cooperation is absolutely essential. However, in modern times, the sports league has frequently tried to go further and serve as a joint bargaining agent for the teams in licensing broadcast rights and trademarks–which is less essential and can sometimes raise significant antitrust problems where the league has a lot of market power[7].
- *Creating a new user-owned branded network.* In the modern service centered economies, branding can be important as a way of identifying and promoting a service or product to consumers.[8] When competing market participants perceive the opportunity to create a new network-based product or service, a joint venture often offers an effective way for participants to reassure each other that there will be sufficient network traffic to achieve efficient scale and scope. The Visa and MasterCard partners were such joint pioneers when they successfully created the now-ubiquitous credit cards in the early 1970s: they agreed to accept each others' cards, establish trademarks and necessary technical standards, and actively promote the joint product. When such a joint endeavor becomes so successful that it can achieve substantial market power, then the ongoing collective action can raise significant horizontal antitrust issues (as Visa's and MasterCard's experience clearly shows).[9]

7 See *NCAA v. Board of Regents of the University of Oklahoma*, 468 U.S. 85 (1984), and *American Needle v. NFL*, 560 U.S.,130 S. Ct. 2201 (2010).

8 This is what franchise systems (McDonald's, etc), routinely do, but most such cases the relationship between the creator of the brand (i.e., franchisor) and the franchisees is *vertical a*nd hence much less likely to generate antitrust concerns.

9 See *United States v. Visa, USA*, 344 F3.d 229 (2nd Cir. 1999). The practical solution that both Visa and MasterCard have adopted is to convert from user owned joint ventures to publicly traded corporations–a conversion that provided the original partners with handsome rewards for their efforts, while largely eliminating their Sherman Act Section 1 risks going forward.

- *Traffic Interchange Arrangement among Competitors*. These generally involve pre-existing agreements about how the parties will treat each other and/or each others' customers. Roaming agreements among wireless networks are a familiar example. Railroads have agreements on how they will deal with through traffic and how they will compensate each for use of roaming freight cars.

III. SELF-REGULATION AND SELF-SERVICE

The historic guilds that flourished in England and medieval Europe had essentially two roles – *first*, to regulate and supervise the performance of their members in order to protect the collective good will of the group for quality and fair dealing; and *secondly* to protect their members from outside competition in the area where the guild operated. Sometimes a guild was able to enlist the state, the local government, or a powerful baron to help it create legal barriers against outside competition. The result of a successful guild was that quality and reputation were generally preserved, but at the price of a lessening competition in ways that a modern antitrust enforcer might question.

Today, the tradition of the medieval guilds lives on. Local bar associations and real estate brokers' associations that have generally tried to protect their members from "cutthroat competition" within the group, while trying to assure their members' efforts are not undercut by troublesome outsiders. Indeed, Judge Posner has once argued that the legal profession, much like other medieval guilds, was built on selfish, anticompetitive restrictions to entry of the market, conduct, and pricing of the work, justified on a "quality-protection rationale (or rationalization)" performance.[10] National organizations (like the New York Stock Exchange, the National Association of Professional Engineers, and the sports leagues have done the same thing. In virtually every case, the modern guild, like its historic predecessors, has had a broad view of that its legitimate "regulatory" role should justify it in limiting competition among its members and/or erecting barriers against

10 Richard A. Posner, The Material Basis of Jurisprudence, 69 Ind. L.J. 911, esp. 917-924 (1996) ("The Medieval Cartel as a Model of the Modern Legal Profession").

outsiders.[11] It is this recurring reality that has generated the antitrust issues and cases which we will turn to next.

IV. ANTITRUST LAW AS A RECURRING CHECK ON MODERN GUILD RESTRAINTS

Modern US antitrust law still has to deal regularly with situations that echo the medieval guilds. It is still common to see groups of like minded businesses coming together in various types of collective efforts designed to enhance efficiency and/or order (including joint ventures, ad hoc consortia, trade associations, standards setting organizations, etc). Sometimes these groups have self-regulatory functions in which they are dictating rules of competitive conduct to their members and would-be members, thus echoing traditional guilds. Sometimes they enlist the government to help them regulate entry, pricing or performance. From time to time, these collective undertakings will act in a manner that is anticompetitive, by limiting competition among their members or excluding outsiders. As a result, the Sherman Act has often been invoked by both government enforcers and private parties to try to curb the actions that these collective undertakings are willing to take to foster the interests of some or all of their members.

The result is an often picturesque, but far from coherent body of law. The courts have sometimes showed these "modern day guilds" some of the deference that traditional guilds expected to receive in medieval times before the age of antitrust, but at other times antitrust courts have been very stringent in applying antitrust law.[12] Since the late 1970s at least, any collective integration with some at least plausible "efficiency" or "integration" has not been subject to a rule of per se illegality but has been examined under the far more lenient rule of reason standard that has evolved from the landmark *Standard Oil*[13] case in 1911. The resulting cases can be loosely placed in categories based on what activity the collective undertaking was restraining.

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11 *See*, William F. Baxter, *NYSE Fixed Commission Rates: A Private Cartel Goes Public*, 22 Stan L. Rev. 675 (1970) (providing that the NYSE enlisted the SEC to help maintain its monopoly).

12 *United States v. Sealey Inc.*, 338 U.S. 350 (1967) and *United States v.Topco Associates*, 405 U.S. 596 (1972) are two obvious examples of the courts applying an overly stringent per se rule to brand-creating cooperation among actual or potential competitors.

13 *Standard Oil Co. v. United States*, 221 U.S. 1 (1911).

1. Pricing

Agreements involving the setting of prices charged by horizontal competitors are clearly the most sensitive area of modern antitrust law.[14] In the last 40 years, we have seen the courts gradually shift to rule of reason treatment where there was a plausible efficiency or regulatory reason for the joint pricing arrangement.

Broadcast Music v. CBS,[15] is a landmark case because the Supreme Court accepted rule of reason treatment for joint licensing of copyrighted music produced by competitors. *Broadcast Music* was a landmark case because the Supreme Court finally recognized that some horizontal price fixing agreements do have considerable value and should be subjected to a more stringent test (as opposed to being automatically found per se illegal). Stating that "easy labels do not always supply ready answers,"[16] the Court went on to announce that it would sometimes be necessary to undertake a lengthier preliminary examination of the issue at bar to determine whether or not there are any redeeming features to the questioned conduct.

Goldfarb v. Virginia State Bar[17] is a clear example of the Supreme Court's willingness to accept rule of reason treatment (rather than per se treatment or outright exemption) because of a state regulatory interest. This was a private suit brought by consumers against the Virginia State Bar (a state sponsored guild) for having established a minimum fee schedule for real estate transactions (specifically title searches). The Supreme Court, in holding that the Virginia State Bar was not immune from antitrust liability provided that:

1) The price schedule was price fixing as "[t]he fee schedule was enforced through the prospective professional discipline from the State Bar, and the desire of attorneys to comply with announced professional norms, . . . the motivation to conform was reinforced by the assurance that other lawyers would not compete by underbidding."[18]

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14 See *United States v. Socony-Vacuum Oil Co*, 310 U.S. 150 (1940).

15 *Broadcast Music v. CBS*, 441 U.S. 1 (1977).

16 *Id.* at 8.

17 *Goldfarb v. Virginia State Bar*, 421 U.S. 773 (1975).

18 *Id.* at 781-782.

2) That the "learned professions" were not exempt from antitrust laws, and
3) The Virginia State Bar was not a state actor for "state action" doctrine purposes because of the way it operated on behalf of lawyers in Virginia. Even though the Virginia State Bar was not immune from antitrust laws and had indeed fixed prices, the Court, in a vague opinion, seemed to suggest that the action of the State Bar's minimum fee setting would be treated as a rule of re*ason case on* remand.

2. Potential Competition among Members

An important instance in which the Sherman Act has been used to limit the action of cooperating competitors was in *NCAA v. Board of Regents of the University of Oklahoma*.[19] In this case, the National Collegiate Athletics Association ("NCAA"), which regulates intercollegiate sports among its members, adopted a plan for the televising of college football games that required all NCAA members to assign their television rights to the NCAA. The plan's stated intent was to reduce the adverse effect of live television upon football game attendance, by limiting the total amount of televised college football coverage. No NCAA member team was permitted to independently negotiate their own television rights, a restriction that was successfully challenged in a private antitrust case brought by two major football schools, the Universities of Oklahoma and Georgia. The Supreme Court held that, while the actions of the NCAA in marketing the collective TV rights did constitute horizontal price fixing, it would be inappropriate to apply the per se rule because the NCAA is an industry organization where horizontal restraints on competition are essential if the product is to be available at all. Instead the Court created a new "quick look" doctrine under which a provision subject to the rule of reason could be prohibited after a very limited inquiry. Because the NCAA football program involved such a plain restriction on price and output of college football telecasts, the Court held that it could be struck down on the basis of such a limited inquiry.

Having approved this quick-look approach, first in *NCAA* and then in *FTC v. Indiana Federation of Dentists*[20] the Supreme Court then squarely rejected application of the quick look test in *California Dental Association v.*

19 *National Collegiate Athletic Association v. Board of Regents of the University of Oklahoma*, 468 U.S. 85 (1984).

20 *FTC v. Indiana Federation of Dentists*, 476 U.S. 447 (1986).

FTC.[21] The California Dental Association had rules limiting advertisements of price, particularly discounts, and of quality. The Court provided that quick look analysis is warranted only when it will be easy to ascertain whether the questioned conduct will have an anticompetitive effect on the market. Because, the Court decided, there were plausible pro-competitive and anti-competitive explanations for the rules that the association implemented it was suggested that a longer look, but shorter than "the fullest market analysis,"[22] be used in order to review the challenged restraint of trade. In effect the Court was moving to a much more flexible (and therefore unpredictable) standard for examining antitrust cases.

3. Access for Non-Members

Silver v. New York Stock Exchange[23] is another example (like *Goldfarb*) where the Supreme Court held that conduct which might have otherwise been subject to a per se boycott prohibition should be treated under the rule of reason for "regulatory" reasons. The case involved a decision by a guild-like, self-regulatory organization the New York Stock Exchange ("NYSE") to order some of its members to remove their private direct lines that had been in operation between their offices and the those of the nonmember plaintiff. The Court made clear that "removal of the wires by collective action of the Exchange and its members would, had it occurred in a context free from other federal regulation, constitute a per se violation of s 1 of the Sherman Act."[24] Having then decided Securities Exchange Act of 1934 ("the Act") does not grant NYSE members implied antitrust immunity from the Sherman Act the Court ruled that because this denial of network access should be judged by the rule of reason instead of condemning NYSE's action as a per se violation.

4. Membership Eligibility

The Fifth Circuit decision in *United States v. Realty Multi-List, Inc.*[25] involved certain membership restrictions in a local real estate multiple listing service

21 *California Dental Association v. FTC*, 526 U.S. 756 (1999).

22 *Id.* at 729.

23 *Silver v. New York Stock Exchange*, 373 U.S. 341 (1963).

24 *Id.* at 347.

25 *United States v. Realty Multi-List, Inc.*, 629 F. 2d 1351 (5th Cir. 1980).

("RML") that had been established the local realty group in an area. These restrictions on potential members went well beyond those which the state of Georgia required for one to obtain a real estate license.[26] Those excluded included part time brokers who did not operate from traditional brick-and-mortar offices during regular business hours; and the Government was able to show that those who were excluded suffered real competitive damage as a result. The Court stated in its opinion that "[g]roup boycotts are among the categories of business which the courts have declared to be per se violations of Section 1."[27] Despite that, the Court held that RML's membership criteria did not warrant per se treatment, but went on to invalidate them under a rule of reason standard, after a lengthy discussion of the pros and cons of RML's membership system.[28]

5. Intellectual Property Licensing

A number of familiar joint ventures have developed important property rights (as with the "Visa" and MasterCard" trademarks). A particularly active area of private antitrust litigation has involved sports leagues, which tend to be quite active in pooling their members' rights vis-à-vis in dealing with outsiders. One hugely important example involves licensing of TV broadcasting rights, where Congress has enacted an antitrust exemption to permit this activity to go forward.[29] Other lesser, non-exempt licensing activities have been held subject to the rule of reason. Thus, for example, the National Football League ("NFL") holds the rights to all its teams' logos and licenses them on what are no doubt monopolistic terms. In the very recent case of *American Needle, Inc. v. National Football League*,[30] the Supreme Court rejected the NFL effort to narrow even this exposure by arguing the NFL is a "single entity" (only subject Sherman Act Section 2) when it engaged in this activity. Rather, the Court found that "NFL's licensing activities constitute concerted action that

26 RML requires its members to hold a Georgia Real estate broker's license, to agree to abide by RML's bylaws, to receive the favorable recommendation of RML's membership committee after it investigated his or her application, to receive an 85% affirmative vote from RML's active members, and to purchase a share of RML stock at a price, and subject to other conditions, set by RML's Board of Directors.

27 *Realty Multi-List* at 1365.

28 *Realty Multi-List* at 1370.

29 Sports Broadcasting Act of 1961, 15 U.S.C. § 1291 (1988).

30 *American Needle, Inc. v. National Football League*, 560 U.S. ___, 130 S. Ct. 2201 (2010).

is not categorically beyond the coverage of §1. The legality of that concerted action must be judged under the Rule of Reason."[31]

As we hope we have made clear, the history of antitrust law as it pertains to joint ventures is somewhat uncertain and confused, even though the cases are now decided under the Rule of Reason. Judging all cases under the rule of reason creates a difficulty when counseling clients as to the ramifications of their joint venture dealings.

V. AN ANTI-ADAM SMITH THEME COMPLICATES THE PICTURE

For a wide variety of political reasons, the U.S. has chosen to temper its strong antitrust mandate with ad hoc exceptions that tend to foster the interests of particular producers and/or regulators at the expense of consumers. Sometimes this has been by Congress in response to lobbying by important constituencies, and sometimes it has been done by the Supreme Court or lower courts in deciding the cases before them.[32]

Federalism concerns seem to have become a significant part of the picture and thus distinguish the U.S. antitrust situation from other leading jurisdictions. Thus, the "anti-Smith" element in modern U.S. antitrust law is especially clear in *Parker v. Brown*[33] and its progeny creating the so-called "state action" doctrine exempting cartels authorized or just tenuously blessed by state and local governments. *Parker v. Brown*, involved a state-sponsored cartel arrangement in a product where California was the dominant source of the relevant product for the whole country. The plaintiff was a dissenting California producer and packer of raisins bringing suit against (i) the State Director of Agriculture and (ii) Raisin Proration Zone No.1 ("Zone 1"), among others. The findings in the District Court showed that almost one half of the raisins consumed worldwide were, at the time, produced in Zone 1. The challenged action in this case involved the California Agricultural Prorate Act[34] which authorized the establishment of state regulated, agricultural marketing programs, instigated on the basis of a vote of the

31 *Id.*

32 A particularly egregious example concerns major league baseball, where the Court found that it was not "commerce" and hence exempt, *Federal Baseball Club v. National League*, 259 U.S. 200 (1922), and has since refused to reverse this position, although it is clearly wrong in modern terms. *Flood v. Kuhns*, 407 U.S. 258 (1972).

33 *Parker v. Brown*, 317 U.S. 341.

34 *Id.* at 346.

relevant producers (in this case the Zone 1 members); the result of such a program was to restrict competition among the growers and maintain prices in the distribution of their commodities to packers. The Court concluded that, "[t]he state in adopting and enforcing the prorate program made no contract or agreement and entered into no conspiracy in restraint of trade or to establish a monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit."[35]

In the subsequent history of the state action doctrine the Supreme Court has been uneven at best. In *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*,[36] in rejecting its application, the Court explained that under the state action doctrine as announced in *Parker* there are two separate standards for antitrust immunity: (1) the challenged restrain of trade must be "one clearly articulated and affirmatively expressed as state policy," and (2) "the policy must be 'actively supervised' by the state itself."[37]

In 1984, the Court reemphasized that the challenged conduct must be undertaken "pursuant to a 'clearly articulated and affirmatively expressed state policy' to replace competition with regulation."[38] Yet the next year in *Southern Motor Carriers Rate Conference v. United States*,[39] the Court provided that "a state policy that expressly permits, but does not compel, anticompetitive conduct may be 'clearly articulated' within the meaning of *Midcal*."[40] The language from *Southern Motor Carriers* seemingly blurs the practical effect of the earlier announced standard. Sometimes a state's authorization of anticompetitive behavior will be explicit in a statute. However, when a state's intention is not explicit in the statute a state's articulation of an intent to permit anticompetitive conduct can be inferred in anticompetitive conduct foreseeably results from the regulation.[41]

35 *Id.* at 352.

36 *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc*, 445 U.S. 97 (1980).

37 *Id.* at 105.

38 *Hoover v. Ronwin*, 466 U.S. 558, 569 (1984).

39 *Southern Motor Carriers Rate Conference v. United States*, 471 U.S. 48 (1985).

40 *Id.* at 61.

41 See e.g. *Town of Hallie v. City of Eau Claire*, 471 U.S. 34 (1985) (The Supreme Court held that as anticompetitive effects logically would result from the broad governmental authority to regulate others action, state action doctrine immunity resulted).

The second prong of the test announced in *Midcal* is the active supervision requirement." The Supreme Court has made clear that there is a close relationship between the clearly articulated and active supervision requirements in that "[b]oth are directed at ensuring that particular anticompetitive mechanisms operate because of a deliberate and intended state policy."[42] There are many examples of state sponsored programs that failed to satisfy the active supervision requirement. In *324 Liquor Corp. v. Duffy*[43] the Supreme Court held that a New York statute satisfied the clearly articulated standard in that the statute affirmatively expressed a New York state policy of resale price maintenance in the liquor industry. However, the Court also found that there was no active state supervision of the process and that, because of the lack of supervision, the state action doctrine did not apply.

The Sherman Act, while seemingly embracing Adam Smith's words, has thus been prevented from being used against blatant cartels (such as the raisin growers cartel in *Parker v. Brown*) and monopolies for reasons of federal deference to the rights of the individual states of the union. This result is in stark contrast to the system that is used in the European Union. Article 86(1) of the Treaty on the Functioning of the European Union ("TFEU") provides that: "In the case of public undertakings to which Member States grant special or exclusive rights, Member States shall neither enact nor maintain in force any measure contrary to the rules contained in this Treaty, . . ."[44] The European Court of Justice has previously held that Article 86 was simply a specific application of certain general principles which are binding upon member states.[45] Thus, even if an EU Member State has authorized the questioned anticompetitive conduct it does not necessarily mean that the conduct will escape antitrust scrutiny. Moreover, the TFEU also gives the European Commission the responsibility (which is exercised by the Directorate General for Competition) to limit or prohibit so-called "state aids" – i.e., Member State subsidies to favored enterprises.[46]

42 *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 636 (1992).

43 *324 Liquor Corp. v. Duffy*, 479 U.S. 335 (1987).

44 TFEU Article 86(1).

45 Case 13/77 *INNO v. ATAB* [1977] ECR 2115, [1978] 1 CMLR 283 para. 42.

46 TFEU Article 87. About a third of the enforcement resources of DG Competition are apparently devoted to regulating state aids.

VI. SOME ANTITRUST BARRIERS TO RATIONAL COOPERATION

As we hope is clear by now, the antitrust landscape in the area of cooperative joint activities is extremely unclear. As a result of this, many competitors who would stand to benefit the public and mutually benefit each other by cooperating are often discouraged from doing so. It is this barrier to *rational* cooperation between competitors that can in fact stifle competition, exactly the opposite effect of what the U.S. antitrust laws are supposed to achieve. The following are just a few examples of these barriers:

1. Philosophic Ambiguity

As we have noted, the Sherman Act essentially established a common law system of law enforcement–with federal judges (and especially Supreme Court Justices) left with huge potential discretion on how to implement the very sparse terms of a broad statute. This has generated a body of jurisprudence in which populist ideas of "equality" and "fairness" have been mixed with some sophisticated (and not so sophisticated) economic theories to produce a smorgasbord of different resolutions of different cases over the years. Which theme(s) may be applied to any particular exercise of competitor cooperation can be hard to predict, and old precedents have become ever less reliable guides to the future.

2. Private Litigation and "bet the company risks"

With treble damages and joint and several liability without any right of contribution, private antitrust litigation can become hugely risky and dangerous for any single defendant. Thus a relatively small market participant (or even a potential competitor that entered into a market-allocation agreement to stay out of the market) can be found liable for treble damages for all the damages caused by the whole conspiracy. These risks can be substantially magnified if the defendant is part of a large class action. Judge Dennis Jacobs of the Second Circuit Court of Appeal, articulated this risk nicely in his dissenting opinion in, *In re Visa Check/MasterMoney Antitrust Litigation*.[47] He noted that in its recent *In re Sumitomo Copper Litigation* decision[48], the Second Circuit had held that class certification should be denied under Federal Rule of Civil

47 *In re Visa Check/MasterMoney Antitrust Litigation*, 280 F.3d 124 (2nd Cir. 2001).

48 *In re Sumitomo Copper Litigation*, 262 F.3d 134 (2nd Cir. 2001).

Procedure 23(f)[49] when the certification order would tend to terminate the litigation by a coercive settlement. Yet in the *Visa* case "the aggregated and trebled claims of the four million class members [was] alleged to top $100 billion . . ."[50] Judge Jacobs went on to say that in a case such as this:

> "[e]ven a defendant who is innocent may rationally choose to pay a few hundred million dollars in settlement of a class action that than 'run the risk of ruinous liability.' As the district court observed (without the slightest overstatement), the 'enormous financial risks' faced by the defendants 'are obviously increased drastically by certification of the class.'"[51]

Although this case was an extreme situation (four-million class members is definitely not the norm, even today) a class does not need to contain that vast number of plaintiffs in order for it to make sound business sense for a defendant to settle, rather than litigate.

Plaintiffs in private antitrust litigation, especially in the class action context, gain additional leverage in the settlement bargaining process because there is no right of contribution among co-defendants in antitrust cases.[52] As a result, any plaintiff will try to play each defendant off every other defendant, by accepting low offers from initial settlers and making escalating demands against those who remain. The final defendant left standing is likely to face a very large settlement demand, because at trial, it could be made liable for the total damages caused by the conspiracy, less the settlements received by the plaintiff(s).

3. Treble Damages

The use of treble damages as a penal remedy seems excessive and inappropriate in a close case brought under the rule of reason. Treble damages were originally added to the Sherman act in order to facilitate the public assisting

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49 Federal Rule of Civil Procedure 23(f)'s advisory committee notes provide that "[a]n order granting certification . . . may force a defendant to settle rather than incur the costs of defending a class action and run the risk of potentially ruinous liability. These concerns can be met at low cost by establishing in the court of appeals a discretionary power to grant interlocutory review in cases that show appeal-worthy certification issues."

50 *In re Visa Check/MasterMoney Antitrust Litigation*, 280 F.3d at 148.

51 *Id.*

52 *See Texas Industries, Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630 (1981).

in enforcement of antitrust laws, at a time when the maximum criminal fine was only $5000. However, times have moved on and it would be highly appropriate for Congress to reconsider the issue whether *mandatory* treble damages should be awarded in *every* antitrust case, however close and difficult the question before the court is. Moreover, the presence of the penal treble damage remedy may well cause judges to find an antitrust exemption or a defense when the conduct at issue has some potential justifications and has been openly engaged in for many years.[53]

4. Multiple Potential Instigators of Antitrust Processes

The multitude of different people (federal and state enforcers, customers and suppliers, free riders, competitors, joint venture members, etc.) who might bring antitrust suits further adds to the uncertainty faced by antitrust counselors in advising a client on whether a particular form of competitor cooperation is likely to be challenged or prohibited under the antitrust laws.

5. Multiple Potential Fora

If a party decides that it wants to bring an antitrust lawsuit in the U.S. it has plenty of places to do so (federal court, state court, and sometimes an administrative agency or arbitration forum) and as a result of this the outcome is often uncertain. It is this kind of legal uncertainty that can cause competitors to abandon a generally promising joint venture idea because the potential litigation risks outweigh the projected benefits of the proposed collective activity.

VII. JUSTICE BRANDEIS' UNFORTUNATE LEGACY: *CHICAGO BOARD OF TRADE*

Justice Brandeis was a highly acclaimed jurist whose decisions sometimes contained strong elements of populism. It was Brandeis' populist ideology that led him astray when deciding the *Board of Trade of the City of Chicago*[54] case. The Chicago Board of Trade was a joint venture for warehousemen, brokers, and traders and was the leading U.S. market for trading in grain for immediate delivery, contracts for future delivery, and sales of grain in transit. Immediate delivery and future sales were made on the exchange floor during

53 See *Gordon v. New York Stock Exchange*, 422 U.S. 659 (1975).

54 *Board of Trade of City of Chicago v. United States*, 264 U.S. 231 (1918)

regular hours, and to-arrive sales were made during special call sessions immediately following the regular daily sessions. The Board implemented a rule that prevented people from trading after the floor had closed at different prices from the closing price on the floor; this effectively protected the floor traders (i.e. the highest volume traders) from over night price fluctuations. The government's case challenged that rule on the grounds that it was artificially fixing the price of "to-arrive" grain for traders who may want to trade on that market overnight.

The District Court held the rule violated Section 1 of the Sherman Act but the Supreme Court reversed and ordered judgment for the defendants. Justice Brandeis famously provided:

> "[T]he legality of an agreement or regulation cannot be determined by simple a test, as whether it restrains competition. Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation or the reverse; but because knowledge of intent may help the court to interpret facts and to predict consequences."[55]

The Brandeis *Chicago Board of Trade* decision seemed to abandon whatever structure and order that have been previously found in Judge Taft's ancillary restraints doctrine from *Addyston Pipe & Steel*[56] and Chief Justice White's standard for unreasonable restraints in *Standard Oil.*[57] In *Chicago Board of Trade*, Justice Brandeis opened the door to a much less structured inquiry in which he declared many factors to be relevant, but he gave no guidance on how to weigh said factors. Furthermore, Justice Brandeis never focused on

55 *Id.* at 238.

56 *United States v. Addyston Pipe & Steel Co.,* 85 F. 271 (6th Cir. 1898).

57 *Standard Oil supra* note 1.

the market-power issue other than to say that "Chicago is the leading grain market in the world. Its Board of Trade is the commercial center through which most of the trading in grain is done."[58] If instead, *Chicago Board of Trade*, had held that a joint venture could adopt a restrictive rule (even a price-restraining rule) so long as there was a good reason for adopting the rule, then this would not be the troublesome case that it turned out to be. Instead, as Professor Bork has previously stated, the decision was an open invitation for courts practice "judicial subjectivism." Put differently, the decision allowed courts to practice unstructured decision making.

Another problem with the Brandeis opinion is the way that it has been used by courts since then. It presents a particularly difficult problem in jury trials. The ABA sample jury instructions for civil antitrust cases[59] ask the jury a few very general questions as to whether the challenged joint activity is, in the jury's eyes, "unreasonable" or "anticompetitive."[60] This has opened the door for judicial passivity which has become quite common (for example the *Sears/Visa* case).[61]

VIII. CONCLUSION: SEEKING TO MITIGATE THE PRACTICAL CONSEQUENCES OF LEGAL UNCERTAINTY, WHILE TRYING TO MAKE RULE OF REASON ANTITRUST CASES MORE MANAGEABLE

As we hope it is clear, case law in the United States presents a challenge to those seeking to counsel clients on the possible ramifications of their cooperative joint activities. While it is easy to see why there is a need for antitrust deterrence, particularly in the cartel area, there is also a very real risk of over-deterrence vis-à-vis various forms of non-secret cooperation among competitors. The problem of over-deterrence is enhanced in the antitrust area by special plaintiff-favoring rules–including mandatory treble damages, one-way litigation cost recovery, and joint and several liability with no right of contribution among participants.[62] Furthermore, given the cautious nature

58 *Chicago Bd. of Trade*, 246 U.S. at 235.

59 Antitrust Sec., Am. Bar Ass'n, Sample Jury Instructions In Civil Antitrust Cases A4 – A8 (1987).

60 *Id.*

61 *SCFC ILC, Inc. v. VISA U.S.A., Inc.*, 819 F. Supp. at 967 (D. Utah 1993), *aff'd in part rev'd in part*, 36 F. 3d 958 (10th Cir. 1994).

62 The normal American rules in tort cases allow recovery of actual damages, no litigation cost recovery against the losing party, and a right of contribution among joint tort feasors.

of the many attorneys, it is not surprising that legal advisors will often err on the side of caution when advising a client on a proposed course of action regarding a joint venture or some other form of ongoing cooperation with competitors. Negative advice that leads to client inaction is less likely to cause the lawyer to be proven wrong by future developments.

The detrimental results from legal uncertainties magnified by overly conservative legal advice are obvious. Sometimes a cooperative business effort is never undertaken. Or heightened level of antitrust caution may cause the level of cooperation to be narrower than would be optimal from a business standpoint. Either way, the end result would be lost cooperative opportunities which could have generated efficiencies and had positive competitive effects. The practical problem of legal uncertainty is the reality that antitrust litigation (and especially litigation under the rule of reason) tends to impose large costs defending a suit, and thus even a weak private case may be sufficient to derail a promising competitor cooperation project if the opponent is noisy and determined enough.

There are a number of things that could be done to mitigate this set of problems, but most of these involve the kinds of major changes that the U.S. has generally been unwilling to undertake, or even seriously consider. Thus, while most other leading antitrust jurisdictions have relatively new and/or recently amended antitrust mandates, the United States chugs along with a basic antitrust mandate enacted in 1890 and amplified in 1914. Instead antitrust policy has been created in a largely incremental, common law process which has been heavily influenced by the experience and philosophic preferences of a changing cast of Supreme Court Justices who can generate some major zigzags in antitrust jurisprudence over time.

That said, we respectfully offer a number of quite significant proposals for change, hoping that at least some of them might be considered or even adopted before another century passes:

1. *Develop a much more structured Rule of Reason.* This is probably a task for the Supreme Court, but the Court has generally denied certiorari or otherwise declined to move us decisively beyond the totally unstructured *Chicago Board of Trade* formula. The "quick look" doctrine in *NCAA v. Board of Regents* was a modest attempt toward more structure, but it did not reach the harder cases and was further blurred by its subsequent decision in *California Dental*.

2. *Eliminate by statute mandatory trebling of damages (i) in all rule of reason cases or at least (ii) for some specific categories of publicly disclosed cooperative conduct.* The treble damage remedy is plainly penal and dates back to a time (i.e., 1890) when the government remedies were minimal[63] and Congress was unsure whether the Attorney General would enforce the new statute at all. While this penal approach remains entirely appropriate for cartel violations, even though criminal penalties have been vastly strengthened in the last 40 years, it tends to over-deter in cases where parties have engaged in publicly-disclosed cooperative projects. A more limited alternative (exemplified by the Joint Research Act) would be for Congress to specify certain categories of joint ventures or cooperation that would be subject on to normal damages.
3. *Provide by statute for injunction-only antitrust relief against some publicly-disclosed categories of cooperative conduct.* Such an approach would probably be best used for specified types of cooperative activity where advance notice is being publicly provided, and hence objectors would have a chance to act in advance. Obviously, this proposal, by excluding damage claims for the specified conduct, would eliminate the perceived uncertainties of having a jury trial.
4. *Eliminate by statute or judicial reversal the prohibition on contribution among antitrust defendants.* The Supreme Court created this exception in its *Radcliff Materials*[64] decision in 1981, and it could change this rule of statutory construction; or, alternatively, Congress could change the rule. Either way, such a step would materially increase the comfort level of individual firms, particularly smaller ones, about joining a large joint venture or other cooperative project.
5. *Increase a Trial Judge's Discretion Regarding Litigation Costs.* The so-called "American rule" on litigation costs means that the defendant cannot recover any of its litigation costs, even if it decisively prevails or the plaintiff abandons the case after imposing years of cost or delay.[65] Thus, litigation, or even clear threats of a lawsuit can be a very effective way

63 A Sherman Act violation was a misdemeanor with a $5000 maximum corporate fine in 1890. The Government could only obtain injunctions but not civil penalties In civil cases.

64 *Texas Industries, Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630 (1981).

65 Section 4 of the Clayton Act (15 USC Sect. 15) provides a special plaintiff-favoring exception to the "American" rule. Under this, the prevailing antitrust plaintiff is entitled to recover its reasonable litigation costs when a final decision is rendered in its favor. However, even this one-way cost-shifting exception

for an objector with a deep pocket to derail a promising joint venture or cooperative project involving competitors.[66] This problem (which is not unique to antitrust cases) could be mitigated by strengthening by statute or rule that a trial Judge has the ability to order the party who brings an abusive case, motion or defense pay the prevailing party's costs of responding.

6. *Legislation to give the antitrust agency general power to immunize particular cooperation from liability under a specified standard.* The obvious models is Article 101(3) of the European Treaty which gives the European Commission (and since 2004 the national competition authorities) the authority to exempt otherwise illegal agreements under a broad standard.[67] This can be exercised in single cases or by granting what is called a "bloc exemption" for specified categories of agreements. The only apparent U.S. parallel is under the Newspaper Preservation Act of 1970[68], which allowed the Attorney General to exempt a joint operating agreement between competing newspapers when he found that one of them was likely to fail.
7. *Provide for more advisory opinions by antitrust enforcement agencies.* The DOJ Business Review process and the FTC Advisory Opinion process can provide useful comfort vis-à-vis potential private litigation threats for cautious potential participants in a joint venture or other cooperative project. However, these processes are often quite slow and tend to be much less used than the "no action" letters issued by the SEC. The process could probably be sped up and made more useful to applicants, if the agencies were specifically authorized to act on the basis of applicant-provided facts and thereby save staff resources.
8. *Encourage more enforcement agency guidelines.* The use of guidelines by the antitrust agencies has been a mixed bag. Guidelines have been particularly useful in areas where an agency has sufficient activity to be a relevant voice for antitrust counselors (e.g., mergers and IP licensing). By contrast, the guidelines have been least productive where the

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does not apply to anything short of final decision (e.g., if the allegedly abusive defendant abandons its challenged activity before an injunction is issued, the plaintiff cannot recover costs).

66 Robert H. Bork, The Antitrust Paradox A Policy At War With Itself (New York: Basic Books 1993) (1978).

67 TFEU Art. 101(3), previously Article 81(2) of the prior treaty.

68 15 U.S.C. § 1801.

enforcement agency has sought to justify non-enforcement and tried to narrow the law in defendants' favor (with the DOJ's Vertical Restrains Guidelines in 1984 or its 2008 Report on Section 2 of the Sherman Act).

It would also be possible to expand the power of other designated agencies to exempt certain types of cooperative conduct from antitrust liability. This approach would certainly deal with antitrust uncertainty and litigation cost threats as a deterrent to cooperative projects among competitors. However, experience tends to suggest that industry-oriented regulators (such as the Surface Transportation Board, the Comptroller of the Currency, or the Secretary of Transportation) have tended to downplay the significance of antitrust when exercising such powers of approval or exemption. Hence this type of approach would seem to be a last resort remedy suitable only to some acute, clearly defined situations.