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SUPREME COURT DECISIONS

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## HARVARD, NOT CHICAGO: WHICH ANTITRUST SCHOOL DRIVES RECENT SUPREME COURT DECISIONS?

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By Einer Elhauge<sup>1</sup>

After a long antitrust slumber, the Supreme Court has become active again in antitrust law, deciding seven cases in the last two years. Since all seven of these cases were decided against the plaintiff, one might think the Court has finally decided to implement the highly conservative Chicago school of antitrust. But so far, it shows no signs of doing so. Rather, while its opinions indicate a determination to cut back on some excesses from an earlier era of pro-plaintiff antitrust decisions, they also indicate an embrace of the moderate Harvard school approach to such issues, rather than an embrace of Chicago school principles. They further indicate a clear embrace of using sound economic analysis to resolve antitrust issues, rather than a resort to either the old formalisms that favored plaintiffs, or new formalisms that try to favor defendants.

My apologies in advance to other great universities for referring to the schools of antitrust thought as the Harvard and Chicago schools. Many notable scholars who fit these schools are at neither university. I employ the Harvard and Chicago school terminology simply because it is in such widespread usage, and has a historical significance that helps convey the gist of two antitrust philosophies.

### I. *LEEGIN* AND VERTICAL DISTRIBUTIONAL RESTRAINTS

Let's start with *Leegin*, the case that finally overruled *Dr. Miles* and the per se rule against vertical minimum price-fixing.<sup>2</sup> If anything was a topic of consensus among the Harvard and Chicago schools, it was the proposition that this rule of per se illegality was misguided. But unlike the Harvard school, Chicago school scholars generally take the next step of insisting the proper rule was one of per se *legality*.<sup>3</sup> The Supreme Court indicated no sympathy for this position in *Leegin*. To the contrary, it was only able to muster a 5-4 majority to overrule *Dr. Miles* at all, and even the majority stressed the need for "diligent" rule-of-reason scrutiny.<sup>4</sup>

Notwithstanding the sharply divided result, the Court was actually in unanimous agreement that the relevant antitrust economics indicated that vertical minimum price-fixing could have both

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<sup>1</sup> Petrie Professor of Law at Harvard University, and co-author of ELHAUGE & GERADIN, *GLOBAL ANTITRUST LAW & ECONOMICS* (Foundation Press 2007).

<sup>2</sup> *Leegin Creative Leather Products v. PSKS, Inc.*, 127 S.Ct. 2705 (2007).

<sup>3</sup> Richard A. Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 9, 23-26 (1981); ROBERT H. BORK, *THE ANTITRUST PARADOX* 288 (1978) ("every vertical restraint should be completely lawful"); Frank H. Easterbrook, *Workable Antitrust Policy*, 84 MICH. L. REV. 1696, 1700-1701 (1986) ("Chicago School ... seems to favor little other than prosecuting plain vanilla cartels and mergers to monopoly").

<sup>4</sup>127 S.Ct. at 2719.

anticompetitive effects and procompetitive efficiencies.<sup>5</sup> Given that this is the classic recipe for applying rule-of-reason review, what was the dispute about? Basically the dissent took the position that, given the mixed economic theory, the case should be resolved, not by the traditional test for deciding whether to apply per se scrutiny, but rather by the empirical evidence or by the doctrine of *stare decisis*. Neither argument was persuasive, though the strongest grounds for rebuttal were missed by the majority.

The empirical evidence stressed by the dissent was that: (1) during the period of the Fair Trade Acts, retail prices were higher in states that had passed statutes allowing vertical minimum price-fixing than in states that didn't, and (2) retail prices were lower after repeal of those acts than before.<sup>6</sup> The majority offered the true, but rather weak, response that higher prices might be procompetitive if they were coupled with more services that consumers wanted.<sup>7</sup> The more powerful response would have been that this empirical evidence addressed the wrong question, because it compared prices in states with per se illegality to prices in states with a rule of per se *legality*. A rule of per se legality is likely to allow more anticompetitive effects than a rule of reason that remains available to redress anticompetitive forms of the conduct. Thus, the price effects of switching from per se illegality to per se legality are not the same as switching from a rule of per se illegality to a rule of reason, which was the relevant issue here. These studies do, however, provide powerful empirical refutation of the Chicago School position favoring per se legality.

As for *stare decisis*, it seems rather late in the day to argue that judicial interpretations of antitrust laws should be governed by a strong rule of statutory *stare decisis*.<sup>8</sup> As the majority correctly noted, the text of the Sherman Act incorporates capacious common law language that has long been thought to effectively delegate antitrust issues to the Courts for ongoing common law resolution.<sup>9</sup> As a matter of practice, the Court in fact overrules antitrust decisions in common law fashion all the time.<sup>10</sup> Indeed, in this very area, the Court had already overruled the per se rules against vertical maximum price-fixing and vertical nonprice restraints.<sup>11</sup> The dissent tried to argue that the statute repealing the Fair Trade Acts indicated a legislative preference for bringing back the per se rule,<sup>12</sup> but the majority was right that the repeal could more plausibly be read as indicating

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<sup>5</sup> *Id.* at 2714-20; *id.* at 2727-30 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>6</sup> *Id.* at 2727-28 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>7</sup> *Id.* at 2718-19.

<sup>8</sup> See generally EINER ELHAUGE, STATUTORY DEFAULT RULES 211-224 (Harvard Univ. Press 2008) (explaining theoretical basis for a fairly strong doctrine of statutory *stare decisis*, but noting the several grounds for exceptions to this basis and doctrine)

<sup>9</sup> 127 S.Ct. at 2720-21; ELHAUGE, STATUTORY DEFAULT RULES, *supra* note 8, at 29, 215.

<sup>10</sup> See, e.g., *Illinois Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006) (overruling old doctrine that market power in a tying case could be inferred from the existence of a patent); *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984) (overruling the doctrine that a corporation could conspire with a wholly owned subsidiary); *U.S. Steel Corp. v. Fortner Enters.*, 429 U.S. 610 (1977) (holding that the per se rule against tying required independent proof of tying market power, even though prior cases had not required such proof).

<sup>11</sup> See *Continental T.V. v. GTE Sylvania*, 433 U.S. 36 (1977) (overruling per se rule against vertical nonprice restraints); *State Oil Co. v. Khan*, 522 U.S. 3 (1997) (overruling pre se rule against vertical maximum price-fixing).

<sup>12</sup> 127 S.Ct. at 2732-33 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

a preference for returning the issue to federal courts for common law resolution.<sup>13</sup>

The dissent fell back on the argument that this was too dramatic a doctrinal shift to be justifiable as gradual common law decisionmaking.<sup>14</sup> The majority responded by noting that the decisions overruling the per se rules against vertical maximum price-fixing and vertical nonprice restraints were based on reasoning that was equally applicable to the per se rule against vertical minimum price-fixing, and had left the latter a lonely outlier that did not seem to fit the surrounding doctrinal landscape.<sup>15</sup> But that argument was not totally convincing because the mix of anticompetitive effects to procompetitive ones was somewhat worse for the per se rule on vertical minimum price-fixing, and it had existed for five decades before the other vertical per se rules made their appearance.<sup>16</sup>

Once again, I think the majority missed a more powerful argument. The bigger problem of doctrinal fit was that, given recent Supreme Court precedent, the per se rule against *horizontal* price-fixing no longer applies in cases where such price-fixing allegedly advances the procompetitive purposes of a productive business relation.<sup>17</sup> Adhering to *Dr. Miles* would thus have meant having antitrust law treat vertical minimum price-fixing that allegedly advances the procompetitive purposes of a productive business relation between a supplier and distributor *worse* than the law treats horizontal price-fixing that allegedly advances the procompetitive purposes of a productive business relation. While vertical minimum price-fixing may be marginally more likely to be anticompetitive than other vertical distributional restraints, there can be no doubt that it is far less likely to be anticompetitive than horizontal price-fixing. Thus, if horizontal price-fixing gets rule-of-reason scrutiny when it is allegedly ancillary to a productive business relation, it would be perverse to give worse scrutiny to vertical price-fixing, which is always ancillary to some permissible business relation between the manufacturer and dealer.

As for the dissent claim that overruling *Dr. Miles* would create a sea change in legal practice,

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<sup>13</sup> *Id.* at 2723-24.

<sup>14</sup> *Id.* at 2737 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>15</sup> *Id.* at 2721-22.

<sup>16</sup> *Id.* at 2736-37. (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>17</sup> The current horizontal doctrine is largely the product of three cases. In *Broadcast Music, Inc. v. Columbia Broadcasting System*, 441 U.S. 1 (1979), the Court held that the per se rule does not apply if horizontal price-fixing advances the procompetitive purposes of a productive business relation. In *Arizona v. Maricopa County Medical Soc'y*, 457 U.S. 332 (1982), the Court made clear that the mere existence of some productive business relation was not sufficient to oust the per se rule. Rather, it held that the per se rule continues to apply if the price-fixing is not alleged to advance the procompetitive purposes of that relation. The fact that the price-fixing advances procompetitive justifications that are unrelated to the productive business relation does not create any exception to the per se rule. Then, in *NCAA v. Board of Regents of Univ. of Oklahoma*, 468 U.S. 85 (1984), the Court held that the per se rule does not apply if the horizontal price-fixing or output restraint is alleged to advance the procompetitive purposes of a productive business relation, although it also made clear that such an alleged connection might be rejected on possibly abbreviated rule-of-reason review. See generally ELHAUGE & GERADIN, *supra* note 1, at 190-191 (summarizing the current contours of the horizontal doctrine).

the majority responded that enforcement of *Dr. Miles* was limited by two doctrines.<sup>18</sup> First, under *Business Electronics*, ambiguous agreements (including even a vertical agreement to terminate a retailer because of price-fixing) were interpreted to constitute a vertical nonprice agreement subject to rule-of-reason scrutiny rather than per se scrutiny.<sup>19</sup> Second, under *Colgate* and *Monsanto*, if a supplier "unilaterally" demanded that its dealers adhere to minimum resale prices and those dealers acquiesced by complying with the minimum resale prices, it was not deemed a vertical agreement at all.<sup>20</sup>

All true, but once again more powerful responses were left unmentioned. The reality is that there was little real enforcement of the per se rule against vertical minimum price-fixing. The reasons are plain once one considers the possible categories of litigants. U.S. enforcement agencies rarely, if ever, brought actions against vertical minimum price fixing because they were persuaded by the economic critique of *Dr. Miles*. Rival manufacturers or retailers lack standing to bring suit against vertical minimum price-fixing rule, because they cannot show antitrust injury given that they would actually benefit if such an agreement caused other manufacturers or retailers to charge anticompetitively high prices.<sup>21</sup> Consumers do have antitrust standing, but to prove injury and damages they must prove a net anticompetitive effect, which requires satisfying an effective rule of reason that negated the practical advantage of any per se rule on liability. And in fact consumers hardly ever brought suit.

The upshot was that the per se rule against vertical minimum price-fixing was generally invoked only by dealers themselves, as in *Leegin*, either in a suit brought to challenge their termination for noncompliance or defensively to avoid enforcement of such an agreement. This didn't provide that much enforcement where dealers were willing participants. It might even have produced the anticompetitive effect of making manufacturers reluctant to replace dealers who are performing poorly for other reasons, because those dealers could bring a lawsuit claiming their termination was for noncompliance with resale price agreements, taking advantage of a per se rule that did not require them to show any actual anticompetitive effect to the market. Ending such suits hardly seems like a big change, nor an unsalutary one.

Relatedly, the dissent also stressed reliance on the old per se rule.<sup>22</sup> The majority responded by stating that: (1) reliance interests could not justify retaining an inefficient rule; (2) any reliance was fairly weak because doctrines like *Monsanto* allowed minimum prices to be fixed in other ways; (3) the fair trade laws meant per se price fixing was legal in most states until 1975, thus making the length of time not that different from the overruled doctrine on vertical maximum price-fixing, and no more than 10% of goods were covered by vertical minimum price-fixing when it was legal.<sup>23</sup>

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<sup>18</sup> 127 S.Ct. at 2721-22.

<sup>19</sup> *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988).

<sup>20</sup> *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984); *United States v. Colgate & Co.*, 250 U.S. 300 (1919).

<sup>21</sup> *Atlantic Richfield v. U.S.A Petroleum*, 495 U.S. 328 (1990).

<sup>22</sup> 127 S.Ct. at 2735-36 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>23</sup> *Id.* at 2724-25.

All these points could have been made more powerfully. The first point, the dissent noted, this was just bare assertion without reasoning.<sup>24</sup> But there is a strong theoretical basis for the majority's assertion, which it unfortunately failed to cite. Mainly, scholarship by scholars like Professor Kaplow has shown that if a legal change would be efficient, then the more efficient doctrine would require parties to bear the risk of legal change, rather than making their reliance a reason to avoid that change, because that forcing parties to bear that risk produces the optimal level of reliance.<sup>25</sup> More recent work by Professor Shavell emphasizes that reliance may nonetheless provide grounds not to change the law when reliance increases the costs or reduces the benefits of a legal change, such as when a technological investment makes a shift to new pollution controls more costly or less beneficial.<sup>26</sup> The reason is that, in such cases, the reliance can alter whether the legal change is in fact efficient. Here, there seemed to be little reason to think that any reliance on the per se rule of illegality would alter whether efficiency would be advanced better by a rule of reason.

The second point was fine as far as it went, but could have been made more forcibly given, as noted above, the lack of real enforcement even for clear vertical minimum price-fixing. The third point was also accurate, but the dissent persuasively noted that 10% today would constitute \$300 billion of trade, so is hardly chicken liver.<sup>27</sup> The stronger response would have been that the dissent offered no grounds to think that reliance meaningfully differed depending on whether the overruled doctrine was around for 96 years, as here, or for 10 or 29 years, as with the per se rules against vertical nonprice and maximum price restraints that were overruled in *GTE Sylvania* and *Khan*. One would think that any meaningful economic reliance at the time of any overruling decision would likely have been incurred within the prior ten years.

So, it seems clear that, under standard Harvard school principles, the majority was right to overrule the per se rule against vertical minimum price-fixing. The puzzle is what provoked a vigorous dissent Justice Breyer, one of the world's most sophisticated antitrust justices, who has generally been fully within the Harvard school. Part of the reason may be that the majority failed to express the stronger grounds for its conclusion that I have described above. But the fact that Breyer's dissent referred no less than six times to the *stare decisis* considerations that were cited in an abortion case made it hard to avoid the conclusion that this case had gotten mixed up with abortion politics.<sup>28</sup> One wonders sometimes whether it would not be better to have a separate Supreme Court of Abortion Law, to prevent abortion issues from mucking up the rest of Supreme Court jurisprudence and from distorting the nomination and confirmation process for justices who spend the lion's share of their time on unrelated issues.

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<sup>24</sup> *Id.* at 2735 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>25</sup> See ELHAUGE, STATUTORY DEFAULT RULES, *supra* note 8, at 306-07 (summarizing literature and its implications for reliance arguments in statutory interpretation).

<sup>26</sup> *Id.* at 307-08.

<sup>27</sup> 127 S.Ct. at 2735-36 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.)

<sup>28</sup> *Id.* at 2731, 2734-35, 2737 (Breyer, J, dissenting, joined by Stevens, Souter & Ginsburg, JJ.) (citing six times to *Federal Election Comm'n v. Wisconsin Right to Life, Inc.*, 127 S.Ct. 2652 (2007) (Scalia, J., concurring in part and concurring in judgment)).

In any event, several features of the Court opinion made clear that it was embracing only the moderate Harvard School critique of *Dr. Miles*, and not the more extreme Chicago School critique. The Chicago School critique rests largely on the notion that, because manufacturers generally want to minimize retail markups, they have optimal incentives to weigh any adverse effects on retail markups against any procompetitive efficiencies. Thus, that school argues, a rule of *per se* legality would be better because courts are unlikely to weigh the anticompetitive and procompetitive effects better than manufacturers with optimal incentives. However, the Court recognized that this was true “in general” and “usually,” but not always.<sup>29</sup> Instead, the court emphasized that manufacturers would lack optimal incentives when vertical minimum price-fixing helped facilitate a manufacturer cartel or the vertical exclusion of smaller rivals, and that vertical minimum price-fixing might reflect the incentives of retailers, which are not procompetitive.<sup>30</sup> If vertical minimum price-fixing were really *per se legal*, then those usages of it would be immunized.

Far from embracing the Chicago School position that vertical minimum price-fixing should be *per se legal*, the Court affirmatively stated that “Vertical agreements establishing minimum resale prices can have either procompetitive or anticompetitive effects...”<sup>31</sup> Nor did the Court advocate a lax version of the rule of reason that could amount to a *de facto* rule of *per se* legality. To the contrary, the Court stressed that “resale price maintenance . . . does have economic dangers,” and that in applying the rule of reason, courts “have to be diligent in eliminating their anticompetitive uses from the market.”<sup>32</sup>

The Court’s statements about how rule-of-reason review should be conducted reflected a further rejection of Chicago School principles. *Leegin* suggests various things about how to conduct rule-of-reason analysis in future vertical minimum price-fixing cases. One is to dismiss cases where “only a few manufacturers lacking market power adopt the practice,” but to use more careful scrutiny “if many competing manufacturers adopt the practice.”<sup>33</sup> This is quite similar to the long-established approach for vertical exclusionary restraints like exclusive dealing, where Supreme Court precedent dictates aggregating the shares covered by similar vertical restraints by other manufacturers on concentrated markets.<sup>34</sup> But Chicago school adherents have wrongly sought to change this well-established aggregation standard, based largely on odd formalisms.<sup>35</sup> A more balanced economic approach, going back to Harvard school exemplar Professor Areeda, shows that aggregation is instead the correct approach when the manufacturers are large players on concentrated markets.<sup>36</sup> *Leegin* indicates the Supreme Court has not only rejected the Chicago school efforts to overrule this aggregation doctrine, but has extended it to vertical minimum price-fixing.

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<sup>29</sup> 127 S.Ct. at 2718-19.

<sup>30</sup> *Id.* at 2716-17.

<sup>31</sup> *Id.* at 2717.

<sup>32</sup> *Id.* at 2719.

<sup>33</sup> *Id.*

<sup>34</sup> See ELHAUGE & GERADIN, *supra* note 1, at 516-17 (collecting sources).

<sup>35</sup> *Id.* at 516 n.20.

<sup>36</sup> *Id.* at 517-519.

What lies in the future? One nice feature of the *Leegin* is that it eliminates the need to continue drawing the confusing *Business Electronics* distinction between vertical price-fixing agreements and agreements to terminate dealers because of price-fixing, because both now get the same rule-of-reason scrutiny. Perhaps it is not too much to hope that *Leegin* might also eliminate the perhaps even more confusing *Monsanto* distinction between vertical agreements and manufacturer demands followed by dealer acquiescence. That distinction was always hard to make sense of, given that demands and acquiescence could well suffice to show a binding legal contract, and especially given that *Monsanto* itself found an agreement even though the evidence in that case showed nothing but demands followed by acquiescence.<sup>37</sup> To the extent this doctrine made any sense at all, it seemed driven by a desire to narrow a per se rule that lacked a sound economic basis and by a general sense that vertical price-fixing was less likely to be anticompetitive if initiated by the manufacturer. By overruling the per se rule, *Leegin* eliminates the motive to narrow that rule by finding nonagreements. Further, *Leegin* suggests that, rather than driving findings of nonagreement, whether the manufacturer or dealer initiated the vertical price-fixing restraint should instead be a factor considered in determining whether the restraint was likely to be anticompetitive under the rule of reason.<sup>38</sup>

Softening the legal effect of who initiated the restraint makes sense. Even if a dealer initiated the restraint, dealers have incentives to offer terms they think manufacturers will find efficient and profitable. Further, even if a manufacturer initiated the restraint, any individual manufacturer has incentives to get dealers to carry its products by offering terms it knows a powerful dealer or dealer cartel will find profitable, even if those profits come at the expense of consumer welfare. Moreover, the Court itself acknowledged that manufacturers could have their own anticompetitive incentives for imposing vertical minimum price-fixing.

## II. WEYERHAEUSER AND PREDATORY BUYING

Next consider *Weyerhaeuser*, the case that held that proving predatory buying requires evidence that the defendant overpaid so much for the inputs that the price of the predator's output was below cost.<sup>39</sup> This holding fit very well with the traditional Harvard school test, going back to Professor Areeda and Turner, which requires evidence that predatory pricing be below cost.<sup>40</sup> But it fit very poorly with the traditional Chicago school argument that predatory pricing should be per se legal.<sup>41</sup>

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<sup>37</sup> *Id.* at 794-95.

<sup>38</sup> 127 S.Ct. at 2719-20.

<sup>39</sup> *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber*, 127 S.Ct. 1069 (2007).

<sup>40</sup> Phillip Areeda & Donald F. Turner, *Predatory Pricing and Related Practices Under Section 2 of the Sherman Act*, 88 HARV. L. REV. 697 (1975); Elhauge, *Why Above-Cost Price Cuts to Drive out Entrants Do Not Signal Predation or Even Market Power – and the Implications for Defining Costs*, 112 YALE L.J. 681 (2003)

<sup>41</sup> BORK, *supra* note 3, at 154; Richard A. Posner, *The Chicago School of Antitrust Analysis*, 127 U.Pa.L.Rev. 925, 927 (1979); Frank H. Easterbrook, *Predatory Strategies and Counterstrategies*, 48 U. CHI. L. REV. 263 (1981).



One might argue that *stare decisis* made the Court reluctant to adopt a rule of per se legality. But we have seen above that the *stare decisis* doctrine usually poses little constraint in antitrust cases. Further, *stare decisis* did not apply here at all because there was no Supreme Court precedent on predatory buying, just on predatory selling. The Court had the ready ground for distinction that predatory buying is, if anything, less likely to be harmful to consumers than predatory pricing, because it may be designed to create upstream monopsony power that might not meaningfully affect the downstream prices paid by consumers. Indeed, had the Court simply held that a predatory buying claim required proof that the conduct was likely to allow recoupment through enhanced monopoly power in the downstream output market, that would have effectively eliminated any distinctive claim for predatory buying, because such a claim would require proof of the same elements that already prove predatory pricing: (1) below-cost pricing in the output market and (2) a sufficient likelihood of recoupment through enhanced monopoly power in the downstream output market.

One might also object that the lawyers did not argue that predatory buying should be per se legal, just as they did not argue that vertical minimum price-fixing should be per se legal. But lawyers make arguments that they think will succeed, so if they did not make those arguments it must reflect their assessment that the Court would be unreceptive to them.

Other features of the opinion confirmed the Supreme Court's moderate, unconservative approach, to antitrust law. First, conservatives sometimes take the view (especially in merger cases) that because monopsony power lowers prices, it should be deemed less problematic than monopoly power. The *Weyerhaeuser* Court gave us a ringing rejection of this view, explicitly holding that it regarded monopsony and monopoly power as equivalent problems.<sup>42</sup>

Second, more commonly, antitrust conservatives often take the view that antitrust law should not condemn conduct that creates anticompetitive effects upstream if that conduct could not have any anticompetitive effect downstream on the markets in which consumers buy, and thus could not harm consumer welfare. The Court squarely rejected this theory, holding that it would suffice to prove illegal predatory pricing to prove both (1) that input prices were bid up to a level that made the output below cost, and (2) that the defendant had a dangerous probability of recouping those losses with enhanced monopsony power in the upstream input market. No showing need be made that the predatory buying would impair rivals in the downstream output market enough to lead to the sort of enhanced monopoly power in that market that would lead to higher consumer prices.

For example, in *Weyerhaeuser* the input market for logs was regional, whereas the output market for finished lumber seems to have been national. The defendant, Weyerhaeuser, may not have had any monopoly power in the output market, its conduct may not have affected national output prices at all, and eliminating one small rival like Ross-Simmons may not have enabled it to recoup any lost profits in the national output market. In the regional input market for Northwestern logs, in contrast, Weyerhaeuser had a 65% buyer share and plausible monopsony power, it had

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<sup>42</sup> 127 S.Ct. at 1076.

allegedly raised prices on that input market, and driving rivals out of that regional input market might allow it to recoup lost profits by paying the regional mills a low monopsony price in the future. The Court held that proof of the latter would suffice, without any need to prove recoupment or the risk of higher prices in the downstream finished lumber market. This holding that upstream market harm suffices was fully in line with past Supreme Court precedent on buyer cartels, and with lower court cases on buyer mergers.<sup>43</sup> But it was the first Supreme Court case to confirm this notion also applied to unilateral buyer conduct.

This holding also has clear implications for a price squeeze claim. A predatory buying claim resembles a price squeeze claim in that, in both claims, the defendant allegedly inflated input prices and left too small a differential between the upstream input price and the downstream output price for rivals to survive. Further, some older lower court decisions on price squeezes utilized a vague test quite similar to the lower court test that the *Weyerhaeuser* Court rejected: whether the upstream price was higher than a fair price and made it hard for the actual rivals to compete.<sup>44</sup> The *Weyerhaeuser* decision indicates the Court is likely to embrace the position that a price squeeze claim should require evidence that the price differential between the upstream and downstream prices is lower than the incremental costs added by any downstream activities.<sup>45</sup>

### III. *TWOMBLY* AND HORIZONTAL COLLUSION

In *Twombly*, the Court made it clear that interdependent parallel conduct, or mere oligopolistic coordination, does not suffice to show an antitrust conspiracy under U.S. law.<sup>46</sup> This was widely understood before, but surprisingly never quite explicitly stated by prior Supreme Court cases.<sup>47</sup> *Twombly* further held that Sherman Act §1 complaint should be dismissed if all it alleged was parallel conduct, coupled with a bare assertion that a conspiracy existed. Some specific fact additional to parallel conduct (often called a "plus factor") must not only be ultimately proven, but alleged in the complaint. This was the widespread practice of lower courts on pleading standards for antitrust conspiracies, but arguably conflicted with some older Supreme Court caselaw that stated

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<sup>43</sup> See *Mandeville Island Farms v. American Crystal Sugar*, 334 U.S. 219 (1948) (condemning a buying cartel in a regional sugar beet market without any proof that it would have a price effect on the downstream national market in refined sugar); *U.S. v. Pennzoil*, 252 F.Supp. 962 (D.Pa. 1965) (condemning merger that created local monopsony power in Pennsylvania crude oil market even though it seemed unlikely to affect output in downstream worldwide market for refined oil); *U.S. v. Rice Growers Ass'n*, 1986-2 Trade Cas. (CCH) ¶ 67,288 (E.D. Cal.) (condemning merger that created local monopsony power in California paddy rice market even though it seemed unlikely to affect output in downstream worldwide market for milled rice); ELHAUGE & GERADIN, *supra* note 1, at 1013 ("Even without higher prices in a downstream market, the creation of monopsony power remains anticompetitive in the upstream market and harmful to sellers in it.")

<sup>44</sup> See *United States v. Aluminum Co.*, 148 F.2d 416 (2d Cir.1945); *Bonjorno v. Kaiser Aluminum & Chem. Corp.*, 752 F.2d 802, 808-11 (3d Cir.1984).

<sup>45</sup> ELHAUGE & GERADIN, *supra* note 1, at 457-458 (advocating this position and showing that other U.S. lower appellate courts, and prominent EC judgments, have adopted such a position).

<sup>46</sup> *Bell Atlantic v. Twombly*, 127 S.Ct. 1955, 1964 (2007).

<sup>47</sup> See ELHAUGE & GERADIN, *supra* note 1, at 837.

a complaint should not be dismissed unless there was no doubt the plaintiff could prove no set of facts that would support his claim.

*Twombly* offered little guidance on what the necessary plus factors might be. My own reading is that other Supreme Court caselaw indicates that the requisite additional evidence could be provided not only by direct evidence of a conspiracy, but also by evidence that indicates the parallel conduct either was implausible without an explicit agreement or followed common invitations or secret meetings.<sup>48</sup> The lower courts have sometimes gone further to suggest that the requisite plus factor could be shown by a "motivation for common action" – that is, by some indication that the firms would have a disincentive to engage in the conduct unless others did the same.<sup>49</sup> The problem is that this plus factor is true for cases of pure oligopolistic coordination, when no conspiracy is inferred. Another plus factor the lower courts have sometimes used is evidence of adverse economic performance, like excessive prices or profits. But again this is true in cases of pure oligopoly. Such plus factors thus now seem insufficient after *Twombly*.

All the above is consistent with the Harvard School, which has long concluded that oligopolistic coordination should not be covered because firms in oligopolistic markets cannot avoid knowing their prices are interdependent when they set their prices, so that it would be hard to define any prohibition in a way that tells firms how to behave.<sup>50</sup> However, it conflicts with Judge Posner's Chicago School view that supracompetitive pricing by an oligopoly should be an antitrust violation, in part because he thinks it unlikely without an actual agreement.<sup>51</sup> The opinion's continued embrace of a per se rule for horizontal price-fixing also conflicts with Judge Easterbrook's Chicago school position that such agreements should not be illegal unless the conspirators are first proven to have market power.<sup>52</sup>

Perhaps the most interesting feature of *Twombly* is that it recognizes that oligopolistic coordination need not involve coordination on price, but can involve coordination on a strategy of not moving into the areas where rivals compete.<sup>53</sup> This is important because antitrust conservatives often incorrectly assume that oligopolistic coordination and unilateral effects on a differentiated market are mutually exclusive theories. This erroneous assumption rests on the implicit premise that the only relevant coordination is coordination on price, a form of coordination that is difficult unless product offerings are homogenous, which by definition they cannot be if the market is differentiated based on geographic location or product characteristics in a way that gives the firms varying attractions to different consumers.

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<sup>48</sup> See *id.* at 801-802.

<sup>49</sup> See AREEDA, KAPLOW & EDLIN, *ANTITRUST ANALYSIS* 226–31 (6th ed. 2004).

<sup>50</sup> See Turner, *The Definition of Agreement Under the Sherman Act*, 75 HARV. L. REV. 655 (1962)

<sup>51</sup> See Richard A. Posner, *Oligopoly and the Antitrust Laws*, 21 STAN. L. REV. 1562 (1969),

<sup>52</sup> See Frank H. Easterbrook, *The Limits of Antitrust*, 63 TEXAS L. REV. 1 (1984). My own view is that, given costs and errors in adjudicating market power, a market power screen would worsen underdeterrence problems without lowering overdeterrence because naked horizontal price-fixing has no procompetitive justification. ELHAUGE & GERADIN, *supra* note 1, at 105-106.

<sup>53</sup> *Bell Atlantic v. Twombly*, 127 S.Ct. 1955, 1972 (2007).

*Twombly* acknowledges that, rather than coordinate on price, firms might coordinate on a strategy of maintaining their differentiated status. Where markets have geographic differentiation, they can coordinate on a policy of not invading the geographic areas of other firms. Where markets have product or brand differentiation, they can coordinate on a policy of not moving into the “spatial” location of the other brands (i.e., adopting similar characteristics or brand advertising and pricing). Thus, a merger on a differentiated market might be condemned on the ground that they make it easier to coordinate on maintaining product or geographic differentiation. Proof of a differentiated market thus no longer undermines a theory of oligopolistic coordination.

#### IV. *CREDIT SUISSE* AND THE SCOPE OF ANTITRUST LAW

*Credit Suisse* may be the least-heralded of this term’s Supreme Court decisions, but is probably the most important because it has implications for the scope of *all* antitrust doctrines. In this case, the Court held that federal securities law precludes antitrust law when the two are “clearly incompatible” given “(1) the existence of regulatory authority under the securities law to supervise the activities in question; (2) evidence that the responsible regulatory entities exercise that authority; ... (3) a resulting risk that the securities and antitrust laws, if both applicable, would produce conflicting guidance, requirements, duties, privileges, or standards of conduct,” and that “(4) ... the possible conflict affected practices that lie squarely within an area of financial market activity that the securities law seeks to regulate.”<sup>54</sup> The Court emphasized that the possible conflict need not be a present one: even if the federal securities agency currently prohibits precisely the same conduct that antitrust law prohibits, it suffices for an antitrust exemption that, in the future: (a) the agency could create a conflict by choosing to exercise its regulatory authority differently, or (b) the agency and antitrust courts might interpret or apply their similar prohibitions differently.<sup>55</sup>

None of this was that big a change from the implied exemption law of past cases. If generalizable beyond SEC cases, it indicates that an implied antitrust exemption applies if: (1) a federal non-antitrust agency has an exercised power to regulate the relevant conduct, and (2) current or future agency choices about how to exercise or apply that power might create a risk of a conflict with antitrust standards on conduct that is squarely within the core area covered by the non-antitrust law. Two features indicated, however, that the Court was trying to cabin this implied exemption doctrine a bit. First, the limitation of implied exemption to the core areas covered by non-antitrust laws indicated a potential narrowing of implied exemption law. Second, the Court suggested in several places that the potential-conflict exemption test might be unique to securities law.<sup>56</sup> Perhaps in the future we will talk of a “securities exemption” the way we now talk about the labor or insurance exemption, that is, as a *sui generis* exemption doctrine with its own elements that do not extend to other sorts of cases.

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<sup>54</sup> *Credit Suisse Securities v. Billing*, 127 S.Ct. 2383, 2392 (2007).

<sup>55</sup> *Id.* at 2390-91, 2394-96.

<sup>56</sup> *Id.* at 2389, 2392.

One can see why the Court was worried about applying this standard outside of securities cases. Given the extent of modern federal regulation, it may well be the case that, in most of our economy, some agency has an exercised power to regulate some conduct that might also constitute an antitrust violation. If all such conduct were exempt from antitrust scrutiny, there could well be little left to the antitrust laws. Further, usually Congress has authorized the relevant agency to regulate the conduct in some more limited way, or based on more limited standards that are unrelated to competitive concerns. It seems implausible that in such cases that Congress really meant to oust antitrust review, or that doing so would be socially desirable. Instead, Congress may well have intended to express even more concern about the relevant conduct, by indicating it was undesirable not only under competition standards, but under other normative standards as well. In any event, nothing in this opinion indicated any embrace of Chicago School principles, which if anything tends to be hostile to regulation as likely reflecting anticompetitive interest group capture.<sup>57</sup>

## V. PRIOR TERMS

One might think all this could just be an aberration of the particular cases decided this term. But the same general conclusion holds for other Supreme Court cases decided in recent terms. In 2006, the Court decided three cases. *Dagher* held that it was not per se illegal for an otherwise lawful joint venture to set the prices at which it sells its products.<sup>58</sup> This case raised no split between the Chicago and Harvard Schools, given that both schools treat joint ventures under the rule of reason, especially since setting prices for the jointly-made products was an unavoidable feature of the joint venture.<sup>59</sup> *Volvo* held that the Robinson-Patman Act prohibition on anticompetitive price discrimination does not apply unless the discrimination is between dealers selling to the same customer.<sup>60</sup> Again, the case raised no real split between the Harvard and Chicago Schools, both of which are disdainful of current Robinson-Patman Act law, which under *Morton Salt* infers an anticompetitive effect from the mere existence of secondary-line price discrimination. Although both schools treat that law as bad economics required by a misguided populist statute, the oddity is that in fact the statutory text is explicitly contrary to this conclusion in *Morton Salt*.<sup>61</sup>

The third case, *Illinois Tool Works*, held that the market power necessary to prove illegal tying must be directly proven, rather than inferred from the mere existence of a patent.<sup>62</sup> This holding was once again squarely within the Harvard School, which had long advocated the same position.<sup>63</sup> So was the Court's suggestion that procompetitive justifications might be admissible in

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<sup>57</sup> BORK, *supra* note 3, at 347-364; Frank H. Easterbrook, *The Supreme Court, 1983 Term-Foreword: The Court and the Economic System*, 98 HARV. L. REV. 4, 51-54 (1984).

<sup>58</sup> *Texaco Inc. v. Dagher*, 547 U.S. 1 (2006).

<sup>59</sup> See ELHAUGE & GERADIN, *supra* note 1, at 96-97 (noting that the price-fixing would be joint even if the joint venture set different prices for the two brands).

<sup>60</sup> *Volvo Trucks North America, Inc. v. Reeder-Simco GMC, Inc.*, 546 U.S. 164 (2006).

<sup>61</sup> See ELHAUGE & GERADIN, *supra* note 1, at 758, 772.

<sup>62</sup> *Illinois Tool Works Inc. v. Independent Ink, Inc.*, 547 U.S. 28 (2006).

<sup>63</sup> See X AREEDA, ELHAUGE & HOVENKAMP, ANTITRUST LAW ¶1737 (1996).

a tying case.<sup>64</sup> However, the opinion nowhere suggested any enthusiasm for overruling the doctrine that tying could be illegal based on market power in the tying product, without proof of substantial foreclosure in the tied product.<sup>65</sup> Even less does it indicate any inclination to adopt the Chicago position that tying should be treated as per se legal.<sup>66</sup> Which is all to the good, because modern economic analysis shows that the Chicago position that tying could not increase monopoly profits was based on very limited assumptions that seldom apply to real markets.<sup>67</sup>

2005 saw no Supreme Court antitrust cases. In 2004, there were three. *Empagran* held that the U.S. antitrust laws did not apply to a claim of anticompetitive injuries suffered in foreign nations that were independent of any U.S. effects.<sup>68</sup> *Flamingo* held that the U.S. Postal Service could not be an antitrust defendant.<sup>69</sup> Both were jurisdictional issues on which there was no Harvard-Chicago split. *Trinko* was more substantive, holding that a monopolist's duty to deal did not extend to cases where the monopolist had not voluntarily offered the relevant product on the demanded terms to either the plaintiff or anyone else in the past.<sup>70</sup> But the Court did not adopt the position of many Chicago School scholars that unilateral refusals to deal should be per se legal.<sup>71</sup> Indeed, far from overruling the *Aspen* duty to deal, it held that *Aspen* was "at or near the outer boundary" of the antitrust duty to deal, thus not only confirming its continued validity, but also indicating that such a duty might even be extended beyond *Aspen*.<sup>72</sup>

And before 2004? From 2000-2003, there were no Supreme Court antitrust decisions, and there were only four from 1994-1999, none of which raised any conflict between the Harvard and Chicago schools. In 1999, *California Dental* held that abbreviated rule-of-reason condemnation could not be applied when the defendants offered a theoretically plausible procompetitive justification for their restraint on advertising.<sup>73</sup> In 1998, *Discon* held that the per se rule against boycotts did not apply to a vertical agreement to refuse to deal with a third party.<sup>74</sup> In 1997, *Khan* overruled the per se rule against maximum price-fixing.<sup>75</sup> Finally, the 1996 *Brown* case held that the labor exemption applied to agreements between employers that were engaged in collective

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<sup>64</sup> See ELHAUGE & GERADIN, *supra* note 1, at 553 (discussing this language from *Illinois Tool*); X AREEDA, ELHAUGE & HOVENKAMP, *ANTITRUST LAW* ¶1760 (1996) (arguing that justifications should be admissible).

<sup>65</sup> See ELHAUGE & GERADIN, *supra* note 1, at 545-47, 553 (noting that this doctrine makes sense if antitrust doctrine takes the view that squeezing out consumer surplus is anticompetitive).

<sup>66</sup> See BORK, *supra* note 3, at 380-81; Posner, *The Chicago School of Antitrust Analysis*, *supra* note, at 926.

<sup>67</sup> See ELHAUGE & GERADIN, *supra* note 1, at 544-51.

<sup>68</sup> *F. Hoffmann-la Roche Ltd. v. Empagran S.A.*, 542 U.S. 155, 162-63 (2004).

<sup>69</sup> See *United States Postal Service v. Flamingo Indus. (U.S.A) Ltd.*, 540 U.S. 736 (2004).

<sup>70</sup> See *Verizon Communications v. Law Offices of Curtis v. Trinko*, 540 U.S. 398, 409 (2004).

<sup>71</sup> See RICHARD A. POSNER, *ANTITRUST LAW* 242-44 (2d ed. 2001); Easterbrook, *Workable Antitrust Policy*, *supra* note 3, at 1700-1701.

<sup>72</sup> 540 U.S. at 409.

<sup>73</sup> See *California Dental Ass'n v. F.T.C.*, 526 U.S. 756 (1999). See generally ELHAUGE & GERADIN, *supra* note 1, at 190-191 (explaining how *California Dental* fits within the doctrinal landscape of horizontal restraint cases).

<sup>74</sup> *NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128 (1998).

<sup>75</sup> *State Oil Co. v. Khan*, 522 U.S. 3 (1997).

bargaining with unions.<sup>76</sup> The Harvard School is consistent with all these positions, and I know of nowhere where the Chicago School has taken a contrary position.

#### CONCLUSION

Since 1994, every Supreme Court antitrust case has been consistent with the rule that the antitrust defendant always wins. That is a remarkable fourteen cases in a row. But none has ever sided with the Chicago School over the Harvard School on any issue in which the two are in conflict. To the contrary, to the extent the Supreme Court has picked sides in this debate, it has always sided with the Harvard School. Last year's term was no exception.

Although I have not done so here, one could extend this analysis to every Supreme Court case since the 1970s, when the Chicago-Harvard split became clear. None of this is to deny that the reasoning of Chicago school theorists has often been quite influential with the Court, and has been highly valuable in helping move the Court from some of the ill-founded anti-defendant positions from earlier formalist periods. But when it comes to actual conclusions, the Court has been much more comfortable with the moderate prescriptions of the Harvard School than with the radical revolution advocated by the Chicago School.

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<sup>76</sup> *Brown v. Pro Football, Inc.*, 518 U.S. 231 (1996).