Worse than the Tower of Babel? Remedying Antitrust’s False Dichotomy Through De Novo Appellate Review

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ABSTRACT

Modern antitrust analysis rests on a strange perch. Its paradigmatic method—pretentiously entitled the Rule of Reason—appears (but only appears) to be a dichotomous analytic. At the first stage, a court supposedly defines the relevant market and determines, as a matter of fact, whether marketplace forces constrain the defendant from profitably raising price above the level that would prevail in a competitive market. Only when market forces are inadequate to protect consumers, that is, the defendant has market power, does the court proceed to stage two, at which it assesses, as a matter of law, whether the defendant used its power improperly.

Nothing approaching this dichotomous analytic paradigm is true. The ostensibly separate inquiries into market power and competitive effects are really a unitary assessment of the industry’s best competitive makeup, that is the allocation of business realms into those requiring rivalry and those in which cooperation or foreclosure are permitted. For example, rivalry is usually required in the realm of short-run price competition. But in some cases, such as when a firm holds a valuable patent, courts permit foreclosure in that short-term realm in order to foster competition to innovate new products over the longer term.

Although the “competitive makeup” term of art is foreign to the antitrust vocabulary, it captures actual antitrust practice in the courts. Everybody knows that pure competition is a fiction; all industries involve an amalgam of

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competitive, cooperative, and foreclosed realms. And antitrust law requires competition only where it serves consumer interests.

Although many experts question whether federal judges can effectively assess business conduct as the competitive makeup approach requires, Austrian economics provides a theoretical justification for concluding that thoughtful judges can do a better job of resolving antitrust cases than would mindless, automaton courts applying necessarily over- and under-inclusive bright-line prophylactic rules. Most importantly, the Supreme Court has to date, including its most recent 2013 decision, demanded that federal judges engage theory and make thoughtful antitrust decisions.

Although much of this Article is interpretive, attempting to explain what courts actually do when they say they are applying the antitrust dichotomy, it recognizes a significant problem that requires a remedy. Trial judges have the power to dictate the level of scrutiny that appellate courts will apply to their decisions. The false dichotomy can be manipulated so that most decisions can be framed as either issues of market definition, reviewed under the clearly erroneous standard, or competitive effect, reviewed de novo. Given the complexity and social import of many antitrust cases, a single federal judge should not have this power.

Appellate courts should thus abandon the clearly erroneous standard of review for market definition. The Supreme Court requires independent appellate scrutiny of fact-findings controlling important issues of public policy that are indistinguishable from the antitrust laws. It would thus be a small, but important, step to impose a de novo review standard for all antitrust issues.
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INTRODUCTION

*There’s something happening and you don’t know what it is, do you, Mr. Jones?*

—**BOB DYLAN,** Ballad of a Thin Man

*Everybody knows that the dice are loaded, everybody rolls with their fingers crossed ... that’s how it goes, and everybody knows.*

—**LEONARD COHEN,** Everybody Knows

Modern antitrust analysis rests on a strange perch. Its paradigmatic method—pretentiously entitled the “Rule of Reason”—appears (but only appears) to be a dichotomous analytic. At the first stage of the analysis, a court supposedly defines the relevant market and determines, as a matter of fact, whether market forces constrain the defendant from profitably raising price above the level that would prevail in a competitive market. Only when market forces are inadequate to protect consumers—that is, the defendant has market power—does the court proceed to stage two where it assesses, as a matter of law, whether the defendant used its power improperly.

In a 2011 article, Harvard Law School Professor Louis Kaplow described this paradigm as “worse than ... the Tower of Babel.” Workers constructing the tower, he wrote, were “[a]t least ... aware that their utterances were mutually incomprehensible.” When it comes to antitrust, “everyone

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1 BOB DYLAN, *Ballad of a Thin Man,* on *HIGHWAY 61 REVISITED* (Columbia Records 1965).
3 In a small group of cases involving naked horizontal agreements not to compete, antitrust liability is imposed without reference to market power. See infra Part IV.F.4.a.
4 See, e.g., NCAA v. Bd. of Regents of Univ. of Okla., 468 U.S. 85, 109 n.38 (1984) (noting that “[m]arket power is the ability to raise prices above those that would be charged in a competitive market”).
5 Although, in generic discussion, competitive effects are often expressed in terms of objective price increases, in actual cases these effects take a variety of different forms. For example, neither of the two significant antitrust trials of the late 1990s focused on price increases. Instead, both focused on the effects of practices designed to undermine potential or existing competitors. See generally Microsoft v. United States, 253 F.3d 34, 50 (D.C. Cir. 2001); United States v. Visa U.S.A., Inc., 163 F. Supp. 2d 322, 340–42 (S.D.N.Y. 2001).
7 Id.
seems to write and speak as if others have a common understanding.”8 But, according to Kaplow, they do not: the judges’ and lawyers’ unarticulated intuitions and assumptions are as vital to their decisions as they are inaccessible to each other.9 Kaplow effectively concluded that “[s]omething is happening” in antitrust cases, but the participants, like Bob Dylan’s thin man, “don’t know what it is.”10

Kaplow’s critique is both dead on and largely irrelevant. He correctly portrays the rhetoric at stage one of the antitrust dichotomy as hollow and inadequate for its intended purpose of assessing whether the defendant possesses market power.11 But the “Tower of Babel” analogy is wrong; no one uses that rhetoric in the literal fashion that Kaplow criticizes. It serves as a framework through which lawyers and judges assess the consumer impact of challenged conduct after taking into account all of the available information. “That’s how it goes,” in Leonard Cohen’s words, and “everybody knows.”12 While the process would likely improve if everyone spoke openly about their reasoning processes, current practice is hardly babble; and uprooting it, at least too quickly, could wreak unnecessary havoc.13

8 Id.

9 Louis Kaplow, Why (Ever) Define Markets?, 124 HARV. L. REV. 437, 465–66 (2010). Kaplow contends: [I]t is remarkable that the criterion by which one market definition is deemed superior to another has received little direct attention and analysis. That is, there is no canonical operational statement of the standard for determining what constitutes a relevant market and, a fortiori, no developed underlying rationalization for whatever the principle might be. Id. Kaplow was not the first to criticize market definition. See Richard S. Markovits, The Limits to Simplifying Antitrust: A Reply to Professor Easterbrook, 63 TEX. L. REV. 41, 58 (1984).

10 DYLAN, supra note 1.

11 Kaplow, supra note 9, at 440 (arguing that “the market definition process should be abandoned” because “the entire rationale for [it] is to enable an inference about market power” but “there does not exist any coherent way to choose a relevant market without first formulating one’s best assessment of market power”).

12 COHEN, supra note 2 (“Everybody knows that the dice are loaded / Everybody rolls with their fingers crossed ... / That’s how it goes, everybody knows”).

13 The traditional market definition process may provide an essential framework for determining whether particular conduct has an anticompetitive effect. In developing the 1982 merger guidelines, the then-Assistant Attorney General for the Antitrust Division, and respected antitrust commentator, William Baxter explained in the text of the guidelines that they intentionally divided and simplified the inquiry. Department of Justice Antitrust Division, Symposium, 1982 Merger Guidelines, 71 CALIF. L. REV. 649, 650 (1982). “[I]n theory,” he wrote, “all the demand and supply forces relevant to the evaluation of a merger could be incorporated in the definition of a market.” Id.

But Baxter recognized that despite its theoretic purity, an all-encompassing concept of the market would be difficult to apply. Thirty years later, long-time Antitrust Division economist, Greg Werden, defended Baxter’s reasoning in response to Kaplow’s critique.
The gulf between rhetoric and reality, however, is far from innocuous. The antitrust dichotomy between market power and competitive effects is descriptively false. The Supreme Court has required trial judges to assess antitrust defendants’ entrepreneurial decision-making to determine whether it comports with the competitive norms set by the antitrust laws. The ostensibly separate inquiries into market power and competitive effects are really a unitary process through which the court determines an industry’s best competitive makeup. Every industry is made up of realms in which firms could compete, including the realms of pricing, quality, geographic scope, innovation, interaction with competitors, suppliers or dealers, and product choice. Although antitrust generally requires competition to regulate market behavior, the Court has long recognized that the law permits cooperation or even foreclosure in some realms in order to enable rivalry to better serve consumer interests in others. An industry’s optimal competitive makeup requires rivalry between firms only when it efficiently serves consumer interests.

The critical question for an antitrust court is thus: should rivalry be required within the realm in which the defendant restrained competition? In answering this question, the existing false rhetoric of dichotomy permits a trial judge to choose, pretty much willy-nilly, the level of scrutiny that an appellate court will apply to its decision. The district court has this power because the unitary nature of the court’s true analysis can usually be manipulated to rest on either stage of the false dichotomy. And therein lies the rub. If the court chooses to decide the case based on market power, it is reviewed

“The presentation of an antitrust case,” Werden wrote, “is a narrative about actual or likely competitive effects consisting of the actors, the scene, and the action—i.e., competition and the challenged conduct. Decades of experience suggests that market delineation often adds clarity and power to the narrative” of many (although certainly not all) antitrust cases. Gregory J. Werden, *Why (Ever) Define Markets? An Answer to Professor Kaplow*, 78 ANTITRUST L.J. 729, 740 (2013). He also recognized that “the tools of modern economics do not always provide a satisfactory means for assessing the likely competitive effects of a merger without resort to market delineation.” *Id*. When they do not, the relevant market remains important to the substantive analysis. Even Kaplow recognized that talking about markets can assist a trial judge. Louis Kaplow, *Market Definition and The Merger Guidelines*, R. INDUS. ORG., Aug. 2011, at 107, 110 n.9 (acknowledging that “a market metaphor might not sometimes be helpful”).

14 The Supreme Court’s case law recognizes that antitrust does not compel competition in all realms. *See infra* Part IV.F.

15 Although prior work has strongly criticized market definition, this is the first article to show it is inseparable from the consideration of competitive effects.


17 *See infra* note 18 and accompanying text.
under the deferential clearly erroneous standard. But if the trial judge decides to analyze competitive effects, the appellate court will review the decision de novo.

Antitrust analysis in the federal district courts is not the wasteland Kaplow makes it out to be. Most judges do excellent work, but the complexity of many antitrust cases ensures that errors are inevitable, and the cases’ widespread economic impact counsels against tolerating those mistakes. As the second Justice Harlan wrote in another context, labeling a matter of significant public importance a fact-finding subject to deferential review “obscure[s] the peculiar responsibilities resting on state and federal courts ... and encourage[s] them to rely on easy labeling and jury verdicts as a substitute for facing up to the tough individual problems ... involved in every ... case.”

This very real problem with antitrust analysis can be cured with a single doctrinal change. Appellate courts should scrutinize all antitrust liability questions de novo regardless of whether the district court bases its decision on market power or competitive effects. Following Justice Harlan’s advice, the federal appellate courts aggressively review many fact-intensive questions involving complex and socially important issues. Antitrust cases fit well within this framework and should be subject to similar scrutiny.

Part I reviews the traditional dichotomy in antitrust analysis between market structure and competitive effects. Part II explains that the most recent merger guidelines promulgated jointly by the federal antitrust enforcement agencies have begun to question this dichotomy. Part III distinguishes Kaplow’s polemic against market definition from the critique offered here. Kaplow accepts the traditional two-step paradigm, rejecting

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18 Under the clearly erroneous standard, the reviewing court will not disturb a district court’s decision unless after reviewing all of the evidence the reviewing court “is left with the definite and firm conviction that a mistake has been committed.” United States v. Gypsum Co., 333 U.S. 364, 395 (1948); see, e.g., Behrend v. Comcast Corp., 655 F.3d 182, 193 (3d Cir. 2011) (applying clearly erroneous standard), rev’d, 133 S. Ct. 1426 (2013); Microsoft v. United States, 253 F.3d 34, 50 (D.C. Cir. 2001); United States v. Engelhard Corp., 126 F.3d 1302, 1305 (11th Cir. 1997) (explaining that “[t]he definition of the relevant market is essentially a factual question,” and “[a]s long as the district court’s findings are plausible, we may not reverse the district court even if we would have decided the case differently”); Graphic Prods. Distribrs., Inc. v. ITEK Corp., 717 F.2d 1560, 1569 (11th Cir. 1983) (explaining that the “relevant product and geographic market is a question of fact, and findings concerning the market should be overturned on appeal only if clearly erroneous or where there is no evidence to support the finding”).

19 Microsoft, 253 F.3d at 50.


21 See infra Part VI.B.
only the process that courts ostensibly use at stage one. Part IV shows the dichotomy is false at its core and presents the descriptive thesis that traditional antitrust inquiries into market power and competitive effects are inseparable. A court determines the ideal competitive makeup of the industry and punishes firms that thwart competition in realms where it would serve consumer interests. Part V responds to anticipated criticism, showing that structure and effects are logically intertwined and that lower courts appearing to follow the antitrust dichotomy are tacitly determining the industry’s best competitive makeup. Part VI articulates and justifies the prescriptive thesis that appellate courts should review all antitrust decisions de novo. It shows courts have long applied probing scrutiny to similarly fact-intensive issues under constitutional and statutory regimes that resemble the antitrust laws in all meaningful ways.

I. ANTITRUST’S FALSE DICHOTOMY

A. The Modern Market Power-Competitive Effects Dichotomy

The paradigm of modern antitrust analysis is a two-stage analytic dichotomy. At the first stage, the court ostensibly determines if the defendant has the ability to overcome the marketplace forces that stimulate competition and typically protect consumer interests, an ability commonly known as market power. After completing its first inquiry, the court is said to move to the second stage, at which it examines competitive effects, that is the impact of the defendant’s conduct on consumers.

1. Stage One—Market Power

At stage one, a court supposedly identifies the competing products that satisfy consumer demand in order to define the market, calculate the competitors’ shares, and estimate the likelihood of competitive entry and supply substitution. A relevant market is an observable cluster of economic activity—a set of reasonable substitute products or services from which...

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22 Kaplow, supra note 9, at 441.
23 See infra notes 25–43 and accompanying text.
24 Id.
25 “Competitive entry” is a term reserved for entirely new participants in the market, and supply substitution refers to the ability of companies already making related products to shift their production to compete with the product in question. For example, in the standard-52-card-deck playing-card market, a competitive entrant would have no prior experience making cards, while supply substitution would occur if the manufacturer of Old Maid cards switched to 52-card decks.
consumers choose. The inquiry is simple in theory, asking whether consumers substitute one product for another, thereby reciprocally incentivizing each producer to strive to make its own good more valuable. Also, it is presumed that a court can answer this question simply by finding facts about the market.

The firm’s market share is thought to be a vital predictor of whether it has market power, that is, the ability to raise price profitably to the detriment of consumers. If the defendants’ shares are large, the court may infer power. Other evidence, such as the likelihood of competitive entry or supply substitution, may undermine that inference. Within the paradigm, the market-defining trial judge is thought to work much like a medical technician reading an x-ray, examining the parameters of a market for imperfections. The defect

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27 Microsoft v. United States, 253 F.3d 34, 81 (D.C. Cir. 2001) (explaining that “the determination of a relevant market is a factual question to be resolved by the District Court”). In the Du Pont case, for example, the Supreme Court held it could not overturn a lower court’s relevant market finding unless the lower court applied “erroneous legal tests ... to essential findings of fact or that the findings themselves were ‘clearly erroneous’” under Federal Rule of Civil Procedure 52(a). United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 381 (1956) (“We do not try the facts of cases de novo.”).
This approach was formalized in William M. Landes & Richard A. Posner, Market Power in Antitrust Cases, 94 Harv. L. Rev. 937, 939 (1981) (explaining that “[t]he concept of market power as the setting of price in excess of marginal cost is formalized in the ‘Lerner index,’ which measures the proportional deviation of price at the firm’s profit-maximizing output from the firm’s marginal cost at that output”).
28 See Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 17 (1984) (tying case); United States v. Grinnell Corp., 384 U.S. 563, 571 (1966) (monopolization case); Times-Picayune Publ’g Co. v. United States, 345 U.S. 594, 611–13 (1953) (tying case); Microsoft, 253 F.3d at 50 (monopolization and tying); Herbert Hovenkamp, Federal Antitrust Policy: The Law of Competition and Its Practice § 3.1, at 79 (3d ed. 2005) (defining market power as the defendant’s ability to “make more money by selling its output at a higher-than-competitive price”). For ease of exposition, market power is normally expressed in terms of profitably raising price. However, it can include any sort of conduct that burdens consumers at the expense of the defendant firm as compared to the situation that would prevail in a competitive market. Hovenkamp, supra at 79 & 79 n.2. For example, market power could be exercised through lower quality, reduced choice, or delayed innovation in addition to higher prices.
29 Herbert Hovenkamp has argued that in predatory pricing and foreclosure cases the defendant’s market share may be directly at issue and not merely relevant because of its correlation to market power. Hovenkamp, supra note 28 § 3.1c, at 82–83.
30 Lawrence A. Sullivan & Warren S. Grimes, The Law of Antitrust: An Integrated Handbook ¶ 2.6b, at 68–70 (2006) (explaining that after calculating market shares a court must assess barriers to entry because “[i]f firms outside the market could easily enter the market, a high market share may not reflect a great deal of market power”).
is either there or not, as a matter of fact, and appellate review is limited to de-
termining whether the lower court’s findings are clearly erroneous.\textsuperscript{31}

2. Stage Two—Consumer Harm

The objective, structural analysis of stage one is thought to be analyti-
cally distinct from the second stage of the dichotomy during which the
court determines whether the defendant’s conduct harmed consumers.\textsuperscript{32} At
this stage, the court becomes a policy analyst, sifting through subtle and
contestable economic considerations. Most market conduct has both pro-
and anti-competitive effects; certain aspects can further the interests of
consumers, other aspects may make them worse off. These competing
effects may arise in different time frames. Immediate consumer harm may
result, for example, from higher prices, but additional revenue gained
through higher prices may fuel long-run competition to innovate new
products that benefit consumers. The impact of these competing factors
cannot be calculated precisely. A court must exercise considerable subjec-
tive judgment to determine, as a matter of law, whether a business practice
violates antitrust law. These decisions are reviewed on appeal de novo.

B. Applying the Dichotomous Analytic

The D.C. Circuit’s 2001 decision in \textit{United States v. Microsoft}\textsuperscript{33} may be the
clearest illustration of the paradigmatic antitrust dichotomy. The government
alleged that Microsoft abused its market power in the operating systems mar-
ket to restrain competition in the Internet browser market.\textsuperscript{34}

1. Stage One—Market Power

The court required the plaintiff to establish the defendant’s market power
as a “necessary element” before considering whether anticompetitive effects
flowed from the defendant’s conduct.\textsuperscript{35} The D.C. Circuit’s \textit{Microsoft} opinion
illustrated the deferential nature of stage-one review. The trial court found
that the relevant market excluded Apple computers, leaving Microsoft’s share
extremely large.\textsuperscript{36} On appeal, Microsoft argued that such a narrow market

\textsuperscript{31} \textit{Microsoft}, 253 F.3d at 50–51.
\textsuperscript{32} \textit{Id.} at 50.
\textsuperscript{33} \textit{Id.} at 50–57.
\textsuperscript{34} \textit{Id.} at 50.
\textsuperscript{35} \textit{Id.} at 51; \textit{HOVENKAMP}, \textit{supra} note 28 § 1.7, at 45 (describing market structure as a
prerequisite that must be supplemented with proof of anticompetitive conduct).
\textsuperscript{36} \textit{Microsoft}, 253 F.3d at 52.
was illogical because Mac had “competed with Windows for years” and should not constitute a separate market “simply because the Mac OS runs on a different microprocessor.”\textsuperscript{37} The appellate court rejected Microsoft’s argument without independent analysis, holding that it fell “far short of what is required to challenge findings as clearly erroneous.”\textsuperscript{38}

Considering Microsoft’s large market share and barriers to entry, the trial court determined that it possessed market power.\textsuperscript{39} In rejecting Microsoft’s appellate argument that despite its share it lacked the ability to raise price profitably above the competitive level, the D.C. Circuit again cited the factual nature of the inquiry, stressing that Microsoft could not prevail “because the company does not challenge [the relevant] findings” of fact.\textsuperscript{40}

2. \textit{Stage Two—Consumer Harm}

When addressing Microsoft’s appellate challenges to the trial court’s stage-two analysis, the opinion took on an entirely different tone. It carefully reexamined whether the facts supported the trial court’s conclusion that Microsoft’s conduct, on balance, harmed consumers.\textsuperscript{41} The court’s willingness to reexamine the facts when analyzing the competitive effects of the defendant’s conduct is even more apparent in the sections of the opinion overturning the district court’s holdings that Microsoft engaged in unlawful attempted monopolization\textsuperscript{42} and tying.\textsuperscript{43}

C. \textit{The Origins of the Paradigm}

Although some claim a longer lineage,\textsuperscript{44} the modern antitrust dichotomy crystallized with the publication of two early 1980s law review articles:

\textsuperscript{37} Id.

\textsuperscript{38} Id.

\textsuperscript{39} Id. at 54–57. In \textit{Microsoft}, the D.C. Circuit applied section 2 of the Sherman Act and often referred to “monopoly power” rather than “market power.” Id. The section 2 test requires two elements that duplicate the rule-of-reason analysis: “(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.” \textit{Id.} at 50 (quoting United States v. Grinnell Corp., 384 U.S. 563, 570–71 (1966)). Citing section 1 agreement cases interchangeably with monopolization cases, the court made clear that the dichotomous approach is the same under both sections of the act. \textit{Id.} at 51.

\textsuperscript{40} Id. at 57.

\textsuperscript{41} Id. at 58–80.

\textsuperscript{42} Id. at 80–84.

\textsuperscript{43} Id. at 84–97.

\textsuperscript{44} Gregory J. Werden, \textit{Assigning Market Shares}, 70 ANTITRUST L.J. 67, 68–72 (2002). The author is a long-serving economist at the Antitrust Division.
William Landes and Richard Posner’s *Market Power in Antitrust Cases* \(^{45}\) and Frank Easterbrook’s *The Limits of Antitrust*. \(^{46}\) The former articulated an economic connection between market shares and market power, \(^{47}\) and the latter questioned the courts’ ability to assess competitive effects, arguing that market power should be a threshold requirement. \(^{48}\) Although the courts have not adopted the reasoning in either article in total, both have been enormously influential. \(^{49}\) Their theses are summarized below.

1. **Market Shares and Market Power**

   Landes and Posner used the Lerner Index, which articulates a relationship between price and market share, \(^{50}\) to thrust market power to the threshold of antitrust analysis. Market concentration is relevant, they argued, because a firm with a larger share, all else being equal, can raise price profitably to a higher level than a firm with a smaller share. \(^{51}\)

   This conclusion rests on two intuitive economic principles. First, a firm with a smaller market share must reduce its own output by a greater percentage in order to increase the market price. \(^{52}\) For example, a firm with a fifty percent market share, assuming rival sales are fixed, must reduce its own output by two percent in order to decrease industry-wide supply by one percent. \(^{53}\) If the firm had a seventy-five percent share, however, it could reduce its own sales by a smaller percentage and have the same impact. \(^{54}\) A larger share thus makes market power—the ability to raise price profitably—more likely.

   Second, if rivals can increase capacity in response to a price increase, the smaller the rivals’ current shares, the less significant any percentage


\(^{49}\) Fred S. McChesney, *Talking ‘Bout My Antitrust Generation: Competition For And In The Field of Competition Law*, 52 EMORY L.J. 1401, 1424 (2003) (concluding that “Easterbrook’s filters ... have exerted an important influence in antitrust thinking ... and deservedly so”).

\(^{50}\) Landes & Posner, *supra* note 27, at 938.

\(^{51}\) *Id.* at 939–42.

\(^{52}\) Kaplow, *supra* note 9, at 451.

\(^{53}\) *Id.* (explaining that reducing total supply while demand remains constant increases the price).

\(^{54}\) *Id.*
increase in their sales will be on overall market supply.\textsuperscript{55} Thus the dominant firm that increases its prices will retain more sales at the higher price.\textsuperscript{56} Again, a larger market share correlates with a greater likelihood of market power.

Market share alone, however, cannot reveal whether a firm has market power. To reach a definitive conclusion, the Lerner Index requires a market observer to know both (1) the elasticity of demand for the defendant’s product and (2) the capacity of the firm’s competitors to expand their output.\textsuperscript{57} Although these variables might be difficult to measure, each was thought to turn on specific observable economic behavior. If enough information could be gathered, market power could be calculated precisely. This fact-based inquiry could take place separate from any assessment of the actual effects of the business practice challenged.

Importantly, Landes and Posner acknowledged the creative, prescriptive nature of their project.\textsuperscript{58} The then-current case law and enforcement agency guidelines did not directly support their analysis.\textsuperscript{59} Under the Lerner Index, much larger market shares would be needed to support a finding of market power than the Court\textsuperscript{60} and the then-applicable merger guidelines required.\textsuperscript{61} As the authors forthrightly recognized, antitrust courts applying their analysis would have “to think far more systematically about market power than they [were then] accustomed to do[ing].”\textsuperscript{62}

\textsuperscript{55} Id. at 452.
\textsuperscript{56} Id.
\textsuperscript{57} Landes & Posner, supra note 27, at 940–41.
\textsuperscript{58} Id. at 938–39.
\textsuperscript{59} Landes and Posner nevertheless argued that their analysis is consistent with the case law. But it is hard to take them seriously because they appear to pick and choose the passages they like while dismissing others as “puzzling.” Id. at 977. For example, they describe Judge Hand’s Alcoa opinion, United States v. Aluminum Co. of America, 148 F.2d 416, 426 (2d Cir. 1945), as “in the spirit of [their] analysis” when he recognizes foreign aluminum effects the U.S. market, but criticize it for failing to include that production in the relevant market. Landes & Posner, supra note 27, at 978–79.
\textsuperscript{60} United States v. Von’s Grocery Co., 384 U.S. 270, 272 (1966) (prohibiting a merger where the post-merger firm would possess 7.5 percent of the relevant market).
\textsuperscript{61} The 1968 guidelines used the share of the top four firms in the market as part of the decision whether to challenge a merger. When the four-firm share exceeded seventy-five percent, it would challenge the merger if the two firms each had at least a four percent share or if a single firm of at least a fifteen percent share sought to merge with a firm of a one percent share or more. In less concentrated markets, the Division would challenge mergers between firms with at least a five percent share or a single firm of at least a twenty-five percent share that sought to acquire a firm with a one percent share or more. See U.S. Dep’t of Justice, Horizontal Merger Guidelines (1968), http://www.justice.gov/atr/hmerger/11247.pdf.
\textsuperscript{62} Landes & Posner, supra note 27, at 956.
2. The Market Power Screen

In The Limits of Antitrust, Frank Easterbrook argued that judges were incapable of analyzing the complex economic factors driving business decisions. He thus proposed that courts adopt a series of filters that would have to be satisfied before considering anticompetitive effects. The first and most important filter was market power as evidenced by market share. Easterbrook recommended using market power as a threshold requirement in every case, because, without it, firms “cannot injure competition no matter how hard they try.” The market, he maintained, “is better than the judicial process in discriminating the beneficial from the detrimental.”

Like Landes and Posner, Easterbrook did not purport to describe existing law. He openly sought to stop judges from evaluating the impact of a business practice on consumers until after determining that the defendant crossed the market power threshold.

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63 Easterbrook, supra note 16, at 11–12. Easterbrook explained that “it is fantastic to suppose that judges and juries could” fully evaluate the economic impact of a business practice. In addition, Easterbrook stated:

The welfare implications of most forms of business conduct are beyond our ken. If we assembled twelve economists and gave them all the available data about a business practice, plus an unlimited computer budget, we would not get agreement about whether the practice promoted consumers’ welfare or economic efficiency more broadly defined.

Id.

64 Id. at 16–39.

65 Id. at 17–23.

66 Id. at 20; see Mark A. Lemley & Mark P. McKenna, Is Pepsi Really a Substitute for Coke? Market Definition in Antitrust and IP, 100 GEO. L.J. 2055, 2077 (2012) (explaining the paradigmatic view as follows: “Mergers, joint ventures, and some agreements among competitors are harmless in competitive markets but can impose serious competitive threats in highly concentrated markets. Before those agreements can be characterized as unlawful, the fact finder must establish either the existence of market power or the likelihood that the conduct at issue will create such power or facilitate its exercise.”).

67 Easterbrook, supra note 16, at 21; Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451, 503 (1992) (Scalia, J., dissenting) (stating that “the inter-brand market functions as an infinitely more efficient and more precise corrective to [potentially anticompetitive] behavior [by firms lacking market power than antitrust liability], rewarding the seller whose intrabrand restraints enhance consumer welfare while punishing the seller whose control of the aftermarket is viewed unfavorably by interbrand consumers.”).

68 Id. at 9 (prescribing that “[t]he judge should employ some presumptions and filters that will help to separate pro- and anti-competitive explanations. These filters would be the alternative to the inhospitality tradition, the solution to the limits of antitrust.”).

69 Id. at 11.
D. 1982 Merger Guidelines

When the Reagan Administration took office in 1981, the president appointed the law professor William Baxter as Deputy Assistant Attorney General responsible for the Antitrust Division. A kindred spirit of Landes, Posner, and Easterbrook, Baxter immediately took up the task of rewriting the antitrust enforcement agencies’ merger guidelines. The effort was revolutionary. For the first time, the guidelines defined a market to include the products that the merging firms’ customers saw as reasonable substitutes at prevailing prices and “additional products ... if a significant percentage of the buyers of products already included would be likely to shift to those other products in response to a small but significant and non-transitory increase in price.” This mode of analysis, known as the “SSNIP test,” has been used ever since.

Like the prior guidelines, the 1982 version relied on market share, but the thresholds set to trigger an investigation were increased significantly. The required market shares were thus more consistent with the

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71 Id. at 131–32. The merger guidelines were originally promulgated in 1968 to provide guidance on when the Division would challenge a merger. The guidelines were substantially revised in 1982, 1992, and 2010. They do not have the force of law, but are relevant to the law in two ways. First, enforcement policy must be based on the law, because the agencies do not have the power to block a merger. They must convince a court that the merger violates the law. Second, as experts, the agencies’ guidelines often influence courts interpreting the law. See generally United States v. Gen. Dynamics, 415 U.S. 486 (1974) (allowing the consummation of a merger despite high market shares).
72 Id. (explaining that “the 1982 [merger guidelines were] so different in conceptual structure from its predecessor that few participants or commentators seriously thought of it as a ‘revision,’ instead, we all considered it to be a new document with a new approach”).
75 HORIZONTAL MERGER GUIDELINES (1982), supra note 73. The 1982 guidelines changed the focus from the total shares of the top four firms to a market-wide concentration measure, the Herfindahl-Hirschman Index (HHI), that summed the squares of each firm’s market share. Id. In this way, the distribution and size of all competitors would be considered with greater weight apportioned to larger firms, “which probably accords with their relative importance in any collusive interaction.” Id.
76 Id.
Landes-Posner-Easterbrook notion that the agencies would only challenge a merger when the new entity would likely have market power.  

E. 1992 Merger Guidelines

Ten years later, the enforcement agencies revised their guidelines and solidified market power’s status as a threshold requirement. The drafters emphasized that the agencies ordinarily would undertake “no further analysis” when a proposed merger is unlikely to “significantly increase” the market shares of the merging firms.

F. The Perceived Importance of the Paradigm

This two-stage approach to antitrust analysis is so well engrained that no commentator seriously questions it. Antitrust lawyers and economists believe courts resolve many cases at stage one without considering competitive effects. “[T]he outcome of more cases,” according to antitrust economist and law professor Jonathan Baker, “has surely turned on market definition than on any other substantive issue.” Former Federal Trade Commission Chairman Robert Pitofsky has thus observed that

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77 Id.
79 Id. Hovenkamp describes the role of market definition under modern generally accepted antitrust principals “as a prerequisite to anticompetitive performance.” HOVENKAMP, supra note 28 § 1.7, at 45 (emphasis added) (asserting that “[s]tructure has become a necessary but not a sufficient cause”).

Some lower courts ostensibly adopted this approach as law. See, e.g., FTC v. Freeman Hosp., 69 F.3d 260, 268 (8th Cir. 1995) (asserting that “[t]he determination of the relevant market is a ‘necessary predicate’ to a finding of a Clayton Act violation”); Graphic Prods. Distribs., Inc. v. ITEK Corp., 717 F.2d 1560, 1571 (11th Cir. 1983) (describing proving market power as “[h]aving crossed this threshold…”).

80 Herbert Hovenkamp may come closest to seeing the dichotomy’s falsity. Herbert Hovenkamp, Response: Markets in IP and Antitrust, 100 GEO. L.J. 2133, 2136 (2012) (explaining that antitrust analysis “has either developed or borrowed technical conceptions of market concentration, market power, market share, entry barriers, and economies of scale and scope, all of which can go into an antitrust assessment of competitive effects”). Other commentators have argued antitrust analysis should include non-economic factors. See, e.g., Maurice E. Stucke, Reconsidering Antitrust’s Goals, 53 B.C. L. REV. 551, 595 (2012) (asserting that antitrust should take account of a broader area of goals than the improper exercise of market power).

“[k]nowledgeable antitrust practitioners have long known that the most important single issue in most enforcement actions—because so much depends on it—is market definition.”

II. THE 2010 MERGER GUIDELINES: UNDERMINING THE FALSE DICHOTOMY?

In 2006, the United States Department of Justice, Antitrust Division (the Division) and the Federal Trade Commission (FTC or the Commission) began to question the paradigmatic dichotomy. Division attorneys and economists stressed that “[t]he market definition process is not isolated from the other analytic components,” and the agencies thus do not always “define a market before proceeding to address other issues.” Rather, the agencies use an “integrated process by which the[y] ... reach an understanding of the merger’s likely effect on competition.” Baker, who was then the FTC’s Bureau of Economics Director, reported the Commission’s view that defining a market is not a critical step in assessing the competitive impact of a merger when the combination “can be shown to harm competition directly.” Adopting a res ipsa loquitur-like approach, he reasoned that if consumer harm is apparent, it must exist within a relevant market and “there is little need to specify the market’s precise boundaries.”

The 2010 revision to the 1992 guidelines formalized this view. Although it retained the Baxter-inspired market definition methodology, the new drafters prefaced that section with the caveat that “[t]he measurement of market shares and market concentration is not an end in itself, but is useful to the extent it illuminates the merger’s likely competitive effects” and that the analysis “need not start with market definition” as it had in each prior iteration.

To emphasize flexibility, the new guidelines began with a list of types of evidence that could indicate adverse competitive effects. Market concentration was listed as the third factor after (1) observed anticompetitive

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82 Robert Pitofsky, New Definitions of Relevant Market and the Assault on Antitrust, 90 COLUM. L. REV. 1805, 1807 (1990); see also Lemley & McKenna, supra note 66, at 2077–78 (defining market definition as an essential aspect of antitrust analysis).
84 Id. at 5.
85 Id.
87 Id.
88 2010 MERGER GUIDELINES, supra note 74, at 7.
89 Id. at 3–4.
effects in consummated mergers and (2) direct comparison based on experience. The drafters also increased the thresholds through which market share alone would trigger greater scrutiny, effectively increasing the cases in which the enforcement agencies would have to use other means of assessing a merger.

The 2010 guidelines are subject to varying interpretations. Perhaps the drafters intended only to explore different avenues to determine market power within the existing dichotomy, believing evidence of anticompetitive effects could also be used to predict the merged firm’s power if particularly good evidence were available. Alternatively, however, the new guidelines can be read to recognize that market power is but one consideration in a broader analysis that invariably requires a unitary assessment of the optimal competitive makeup of a particular industry.

III. LOUIS KAPLOW’S CRITIQUE OF MARKET DEFINITION

Perhaps inspired by the new guidelines, Kaplow launched what he described as “a wholesale assault on the core logic of the [market definition] methodology,” arguing convincingly that the process hinders a court’s ability to determine whether a defendant has market power. Taking the paradigmatic

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90 Id. at 3.
91 Id. at 19.
92 See Kaplow, supra note 13, at 2, 19. Kaplow states:
[T]he new Guidelines’ modest statements launch the evolution of merger review (further) down a slippery slope and therefore are dangerous, threatening to throw the process and court scrutiny into disarray. From this perspective, what matters less are the words themselves; reading between the lines, a more momentous shift may be underway.
Id. at 16.

93 2010 MERGER GUIDELINES, supra note 74, at 2 (“The Agencies consider any reasonably available and reliable evidence to address the central question of whether a merger may substantially lessen competition.”).
94 Kaplow, supra note 9, at 440. Kaplow’s critique spans three law review articles that were published in 2010 and 2011. See supra notes 6, 9 & 13.
rhetoric seriously, Kaplow concluded that antitrust judges are irrationally employing a counterproductive tool.\textsuperscript{95} He never considers, however, the possibility that courts may not be following the antitrust dichotomy.\textsuperscript{96} This section summarizes Kaplow’s argument and then compares it to a similar misunderstanding of the judicial role in another area of law.

A. Understanding Kaplow’s Critique

Kaplow contends that the practice of defining markets by calculating shares to draw inferences of market power is incoherent.\textsuperscript{97} Markets cannot be defined in a rational way and even if they could, he shows, market shares would not convey useful information.\textsuperscript{98}

Kaplow first demonstrated that the process of examining cross elasticity between products—the heart of traditional market definition—illogically requires courts to search for irrelevant information.\textsuperscript{99} Knowing what products, if any, a firm’s customers would adopt if price increased is useless information.\textsuperscript{100} The market elasticity of a firm’s products is the only relevant issue. “All [a firm] cares about,” in deciding whether to increase price, Kaplow explained, “is the rate at which [its customers would] reduce their purchases of its own product as the price rises.”\textsuperscript{101} The court thus has no need to determine the products to which consumers might switch in order to assess market power.

Even worse, Kaplow contended, the market definition process requires a court to disregard known, relevant information.\textsuperscript{102} With respect to virtually any potential substitute, a court will know that (1) it has some impact on the defendant’s pricing decisions, but (2) less than a perfect substitute would have.\textsuperscript{103} Paradigmatic market definition, however, is binary. It only permits the court to either include the partial substitute in the market as if

\textsuperscript{95} Kaplow, supra note 9, at 515.
\textsuperscript{96} Although rejecting market definition, Kaplow does not question the bifurcated market power-competitive effects dichotomy. See Kaplow, supra note 6, at 276 (asserting that market power is critical issue); Kaplow, supra note 13, at 4 (asserting that “[f]or economists the message is to continue or accelerate work on other ways of determining market power”); Kaplow, supra note 9, at 502 (recognizing need to find the best way to measure market power in various industries).
\textsuperscript{97} Kaplow, supra note 9, at 516.
\textsuperscript{98} Id. at 515.
\textsuperscript{99} Id. at 449, 481–85.
\textsuperscript{100} Kaplow, supra note 13, at 5 (“[T]he formula properly depicts market power regardless of the particulars of demand substitution.”).
\textsuperscript{101} Kaplow, supra note 9, at 449.
\textsuperscript{102} Id. at 516.
\textsuperscript{103} Id. at 515.
it were perfect, overstating its impact on price, or leave it out and understate its impact.\textsuperscript{104} Either way, the court would ignore what it knows to be true—that the partial substitute has a limited impact on the defendant’s pricing decisions.\textsuperscript{105}

Kaplow thus rejected the traditional market definition process entirely and argued for using the best available evidence to estimate market power.\textsuperscript{106} To illustrate his point, Kaplow posited a hypothetical merger between orange juice companies. Under the standard paradigm, one would ask whether to include, say, grapefruit juice, in the relevant market.\textsuperscript{107} To make that decision, however, the court would need to have a sense of whether a non-orange juice limited the ability of the merging firms to raise price.\textsuperscript{108} “But,” Kaplow reasoned, “if we have already reached the conclusion that orange juice drinkers would switch to another juice, we are done.”\textsuperscript{109} The merging orange juice producers obviously lack market power. There is no value, according to Kaplow, in the standard exercise of deciding whether grapefruit juice is within the relevant market and calculating shares based on that decision.\textsuperscript{110} We can just rely on whatever evidence convinced us that OJ drinkers would switch to grapefruit juice.

Second, Kaplow argued that even if there were a logical method to define the market and determine accurate shares, that data point would be virtually useless.\textsuperscript{111} Within the existing paradigm, the search for market power is intended to determine whether the defendant can harm consumers. But market shares, Kaplow showed, provide virtually no information about either (1) how much market power a defendant possessed or (2) how much would be necessary to enable the defendant to injure its customers.\textsuperscript{112} The answer to both questions logically requires reference to the

\textsuperscript{104} Id. at 472.
\textsuperscript{105} Id. at 487; accord Lemley & McKenna, supra note 66, at 2098 (explaining that “[t]he current approach to market definition draws an arbitrary line when what we need is a continuum that reflects the partial differentiation of products and differences in the cost and convenience of those products”).

Kaplow further argues that the hypothetical monopolist test in the merger guidelines does not help define rational markets and often produces worse results. Kaplow, supra note 13, at 10–15; Kaplow, supra note 9, at 480.

\textsuperscript{106} Kaplow, supra note 6, at 275.
\textsuperscript{107} Kaplow, supra note 6, at 505–06.
\textsuperscript{108} Id.
\textsuperscript{109} Id. at 506.
\textsuperscript{110} Id. at 480 (traditional market definition more likely to mask than elucidate).
\textsuperscript{111} Kaplow, supra note 6, at 275.
\textsuperscript{112} Id. at 255 (“[T]he market share (even in a properly defined market) does not allow even a rough approximation of the extent of market power.”); id. at 257 (“[T]he resulting
defendant’s ability to raise price, and any answer expressed in terms of market share “fails to address either question directly and does not appear capable of providing a meaningful indirect answer.”

Kaplow acknowledged the economic correlation between market share and market power as demonstrated by the Lerner Index. But he argued that expressing power in terms of share is “a category mistake.” A car’s top speed, he analogized, cannot be expressed in terms of its engine displacement, even though that measure is “an important factor bearing on” a car’s potential speed. In both cases, the unit of measurement is not powerful enough to serve as the sole criterion for answering the question asked. Too many other relevant factors come into play. As Kaplow put it, the data point is “blatantly not in the terms (units) put by the question.”

Kaplow’s attack is powerful and his logic compelling. If judges have been following the two-stage paradigm—(1) using market shares as a proxy for market power and (2) ignoring competitive effects unless market shares are big enough—then those judges have been horrifically misguided.

B. An Illustrative Analogy Revealing Kaplow’s Error

Kaplow concludes that courts act irrationally when they define markets, but there is another possibility. Judges may be approaching the problem in a way that is very different from what the antitrust dichotomy predicts.

A helpful analogy can be found in Bruce Ackerman’s *Property and the Constitution*, which analyzed a similar divergence between the paradigmatic theory of regulatory takings and apparently out-of-sync case law. Ackerman attributed the disconnect to the commentators’ use of an alluring analytic method that differed from the approach that the courts actually used. He called this method “scientific policymaking,” describing it as developing a comprehensive view of the law’s goal and a special technical language designed to pursue it.

answers for a given market share vary too much for market share to be used even as a crude approximation” of market power.

113 *Id.* at 257.
114 *Id.* at 253.
115 *Id.*
116 *Id.*
117 *Id.* at 275.
119 *Id.* at 168.
120 *Id.* at 23–24.
121 *Id.* at 10–11.
A legal analyst of the scientific-policy-making type, Ackerman explained, “manipulates technical legal concepts so as to illuminate ... the relationship between disputed legal rules and the Comprehensive View he understands to govern the legal system.” For example, Jeremy Bentham was a scientific policymaker whose comprehensive view was that legal rules should be set to best maximize utility.

Commentators like Landes, Posner, Easterbrook, and Kaplow advance the comprehensive view that antitrust law should limit the ability of firms to raise price profitably above the competitive level. Also, they use the technical language of economics—the Lerner Index, elasticity, demand, and supply substitution—to pursue that goal. This approach fits comfortably within the scientific policymaking framework.

Ackerman argued that scientific policymaking can create “the basis for a body of ... law that is both powerful and deeply grounded.” In takings cases, it “seem[ed] familiar[] and ... sensible.” Yet, the results it predicted bore “very little relationship to the [existing legal] rules.”

The same problem infects antitrust law. As Kaplow demonstrated, the existing legal rules of market definition bear little relation to those that a court would pursue were it truly interested in assessing the defendant’s market power as a threshold issue. In such a case, as Ackerman put it, there are two possibilities: “either ... the judges have been strikingly inept or ... they have been thinking about [the] law in a way that is strikingly different from that characteristic of the Scientific Policymaker.” In the takings area, Ackerman concluded that courts were using ordinary observers’ subjective understanding of the scope of property rights rather than the criteria advanced by the scientific policy-makers.

Antitrust courts have similarly pursued a “strikingly different” path from the comprehensive view that market power is a threshold requirement that must be proven before a court may consider the effect of a defendant’s conduct on consumers. The following section explains that

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122 Id. at 15.
123 Id. at 11.
124 Id. at 24 (addressing government compensation for reducing property value through regulation).
125 Id.
126 Id.
127 Kaplow, supra note 6, at 275.
128 ACKERMAN, supra note 118, at 24–25.
129 Id. at 168.
130 Tellingly, in discussing the Lerner Index and market power, Herbert Hovenkamp’s leading treatise fails to cite a single Supreme Court case and includes no source at all prior to Landes’s and Posner’s 1981 article. HOVENKAMP, supra note 28 § 3.1, at 79 n.2.
this alternative requires the court to determine the best competitive makeup of an industry. Once that question is answered, the result is straightforward. If the defendant restrains competition in a realm that should be subjected to rivalry, it violates the antitrust laws; otherwise, it does not.

IV. Determining Competitive Makeup: What Courts Do When They Say They Are Defining Markets

The competitive makeup of an industry is a roadmap to the realms of business behavior in which antitrust law requires rivalry and those in which it does not. For example, rivalry is generally required in the realm of short-run price setting.\(^{131}\) A firm with a patent on a superior technology, however, may block competition to provide its patented product and charge supra-competitive prices without running afoul of antitrust law.\(^{132}\) Rivalry thus does not regulate the short-run unilateral pricing realm when a superior patented technology drives the market.\(^{133}\) This is true despite the patent holder’s market power. The antitrust dichotomy cannot explain why this type of market power does not count. Under the competitive makeup approach, however, the answer is simple—the best makeup of an industry driven by a superior patented technology permits foreclosure in the realm of short-run pricing of the patented product. Despite some consumer harm,

If courts were actually searching for market power in this way, one would expect a longer trail. In a recent article, Hovenkamp argued that with respect to innovation, “market power assessment will probably never do a good job ... because innovation is so badly behaved, often producing completely unanticipated results.” Hovenkamp, supra note 80, at 2135. Hovenkamp notes:

[A] problem with traditional market definition approaches to power is that they tend to lump [distinguishable products] into the same market, ignoring the differences between them. By contrast, a problem with direct measurements based on observed customer behavior is that, although they account more fully for current product differences, they do not take innovation mobility into account.

Id. at 2148.

\(^{131}\) See Palmer v. BRG of Ga., Inc., 498 U.S. 46, 48 (1990) (quoting United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 223 (1940)) (explaining that “‘under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing the price of a commodity in interstate or foreign commerce is illegal per se’”).

\(^{132}\) FTC v. Actavis, Inc., 133 S. Ct. 2223, 2231 (2013) (explaining that a “patent owner [may be able] to charge a higher-than-competitive price for the patented product” without violating the antitrust laws); see United States v. Gen. Elec. Co., 272 U.S. 476, 490 (1926) (permitting a patent holder on a single product to impose resale price maintenance when those agreements were per se illegal on unpatented products).

\(^{133}\) Actavis, 133 S. Ct. at 2231; Gen. Elec. Co., 272 U.S. at 490.
foreclosure in this realm stimulates innovation in the future that benefits consumers more than the short-run high prices hurt them.

The singular relevant question for an antitrust court is whether the defendant thwarted competitive forces in a realm in which rivalry efficiently regulates market conduct. An industry’s best competitive makeup is the one in which rivalry is compelled in those realms that antitrust can regulate efficiently, but no others.134

Knowing whether a defendant has market power may be relevant to an industry’s competitive makeup. But power alone does not convey much information. Firms are often permitted to exercise power—a monopolist for example can profitably charge prices above the competitive level with no antitrust repercussions—and a lack of market power does not necessarily insulate a defendant from liability when a plausible theory points to consumer harm.135 Competitive makeup is thus a superior tool to the paradigmatic dichotomy.

This section flushes out the competitive makeup concept and then shows, perhaps surprisingly, that the Supreme Court—albeit without using the term competitive makeup—has instructed the lower courts to apply a method of analysis that looks just like it.136

A. Distinguishing Competitive from Non-Competitive Realms

The notion that antitrust law does not require rivalry in all realms of business behavior is not new. As Easterbrook explained, “[p]art of the difficulty in antitrust comes from ambiguity in what we mean by competition.”137 In each industry, firms conduct business in a unique mix of rivalrous, cooperative, and potentially foreclosable realms.138 The non-competitive realms are efficient despite competitive restraints because they enable rivalry to serve consumer interests in other realms.

To illustrate the point, Easterbrook explained that “[t]he Chicago Board of Trade perhaps the closest of modern markets to the textbook ideal [of a market governed by rivalry], has a sheaf of rules and cooperative

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134 Easterbrook, supra note 16, at 1.
135 See infra Part IV.F.4.a (discussing the per se rule); Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451, 470–79 (1992) (holding that copy machine manufacturer lacking market power in the copier market may nonetheless violate the antitrust laws for limiting the sale of spare parts for its machines).
136 See infra Part IV.F.
138 Id. at 1 (explaining that “[e]very market entails substantial cooperation over some domain in order to facilitate competition elsewhere”).
arrangements that reduce the cost of competition.” 139 If an antitrust court simply tried to move each industry closer to the textbook model, “it is sure to be wrong a great deal of the time.” 140

B. Neoclassical v. Austrian Economics

Easterbrook’s solution was a market power filter that would block courts from intervening in markets unless the defendants controlled a large share. 141 Using market power to limit antitrust analysis is consistent with neoclassical economics. Prices are viewed as an objectively determinable function of production costs, and the optimal price is generally thought to be the marginal cost of production. 142 If the market structure indicated the defendant could price above that cost-based measure, a firm had power and would violate the antitrust laws if it used that power to harm consumers. But when a firm had a small share, a judge could rule for the defendant without assessing the impact of the defendant’s conduct on consumers. Although the structural factors necessary to predict market power may not be obvious, a court has a better chance of determining them based on objective information than it has of predicting whether particular business practices would harm consumers. Also, within a neoclassical economic worldview, without market power the firm simply could not inflict enough harm on consumers to justify the cost of antitrust intervention. 143 So, the court has no need to go further.

139 Id.
142 FTC v. Ind. Fed’n of Dentists, 476 U.S. 447, 459 (1986) (describing the role of the market as “advanc[ing] social welfare by ensuring the provision of desired goods and services to consumers at a price approximating the marginal cost of providing them”).
143 As Deven Desai and Spencer Waller explain, “[t]he rise of the Chicago School as the prevailing economic discourse for antitrust reinforced the focus on price theory to the exclusion of most other factors. It relegated business discourse to the fringes of the profession of antitrust, whether practiced by the liberal or conservative wings of the discipline.”
Although Kaplow called for taking account of all available information to determine market power, he did not question the neoclassical economic underpinnings of the antitrust dichotomy. Courts could continue to use price theory to predict a market power threshold so long as they discarded the fiction that market share analysis was a useful way to answer that threshold question. But Kaplow ignored the fact that a firm’s ability to raise price profitably—no less than a firm’s market share—provides insufficient information to enable a court to draw a reasonable inference about whether the defendant harmed consumers in a way that should violate the antitrust laws.

The U.S. Supreme Court has not rested its antitrust decisions on either Easterbrook’s or Kaplow’s dichotomies. Instead, the Court’s analysis reflects an aspect of the Austrian school of economics that rejects both the idea that prices can be derived from costs and that a firm’s ability to raise price profitably is inherently suspect. Austrian economics posits that prices arise out of a dynamic process of individual entrepreneurial decisions. An analyst thus cannot focus objectively on costs and price. The legitimacy of business conduct must be assessed subjectively given the preference of antitrust law to use rivalry to advance consumer interests. As circumstances evolve and change, entrepreneurial actors seek profit opportunities. One cannot assume a given product should be sold at its marginal cost or even the price that would prevail if multiple sellers were offering identical versions of that product within a defined geographic area. Prices exceeding marginal cost often benefit consumers and do not violate the antitrust laws. Entrepreneurial actions should contravene

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144 See generally Kaplow, *supra* note 6.

145 United States v. Gen. Dynamics Corp., 415 U.S. 486, 498 (1974) (quoting Brown Shoe Co. v. United States, 370 U.S. 294, 322 n.38 (1961)) (“[S]tatistics concerning market share and concentration, while of great significance, were not conclusive indicators of anticompetitive effects ... ‘only a further examination of the particular market—its structure, history and probable future—can provide the appropriate setting for judging the probable anticompetitive effect of the merger.’”).


149 Lemley & McKenna, *supra* note 66, at 2097 (explaining that the notion of marginal cost makes little sense in multi-product industries where the successful products must cover
antitrust only if a firm’s dynamic decisions blunt competition in realms in which rivalry would best serve consumer interests.\textsuperscript{150}

The Supreme Court appears to recognize, like the Austrians, that judges can comprehend basic entrepreneurial instincts to: (1) seek out profit opportunities; (2) avoid competition that would undermine profit; and (3) use opportunities for profit to drive competition.\textsuperscript{151} The Court’s reliance on a “rudimentary understanding of economics”\textsuperscript{152} that is widely accessible links directly to the Austrian insight. Intuitive knowledge, although rudimentary in some sense, can enable a judge to assess subjectively whether a given competitive restraint promotes consumer welfare or detracts from it.

\textbf{C. Judicial Competence}

Easterbrook recognized the importance of an industry’s competitive makeup.\textsuperscript{153} He favored the antitrust dichotomy, however, because he believed that courts were incapable of assessing whether competition should govern in a particular realm.\textsuperscript{154} “[I]t is fantastic to suppose,” he contended, “that judges and juries could ... evaluat[e a business practice]. The welfare implications of most forms of business conduct are beyond our ken.”\textsuperscript{155} Even businesspersons, he thought, generally cannot explain how the market operates.\textsuperscript{156} A judge who tried to evaluate the extent to which a business practice harmed consumers, Easterbrook concluded, would be “at sea.”\textsuperscript{157}

the costs of unsuccessful ones); Hovenkamp, \textit{supra} note 80, at 2140 (“[I]n many IP-rich markets, the ratio of fixed to variable costs is extremely high, and marginal cost measures only variable cost,” creating an “illusion of market power” based on standard analytical tools.). Even the notion that prices always tend to move toward marginal cost appears to be wrong. Mark Kelman, \textit{Trashing}, 36 STAN. L. REV. 293, 315–18 (1984) (showing that even in many seller markets prices do not invariably tend toward marginal cost).

\textsuperscript{150} \textsc{Jesús Huerta de Soto}, \textit{The Austrian School: Market Order and Entrepreneurial Creativity} 85–86 (2008).

\textsuperscript{151} \textit{See infra} IV.F.

\textsuperscript{152} \textit{Cal. Dental}, 526 U.S. at 757.

\textsuperscript{153} \textit{See} Easterbrook, \textit{supra} note 16.

\textsuperscript{154} \textit{Id.} at 10–13.

\textsuperscript{155} \textit{Id.} at 10.

\textsuperscript{156} \textit{Id.} at 5 (arguing that “sometimes no one knows” why a business practice succeeds). \textit{But see id.} at 11 (recognizing that economists could reasonably assess market practices by “resort[ing] to clues and shortcuts [and] us[ing] their economic knowledge of other markets to draw inferences about this one,” but concluding that judges could not apply these techniques in the context of the then-existing law).

\textsuperscript{157} \textit{Id.} at 2. Although this Part explains that the Supreme Court has generally expressed more confidence in the courts’ abilities than Easterbrook, there was a period in the mid-Twentieth Century when the Court appeared to agree. For example, in \textit{United States v. Topco Associates, Inc.}, 405 U.S. 596 (1972), ironically a case with which
The Austrian School, by contrast, believes that the judiciary can meaningfully assess competition’s value within particular market realms. Economic reasoning, the Austrians recognized, is universal and unspecialized. Everyone participating in an economy as a producer or consumer has the ability to make and assess entrepreneurial decisions. A non-expert’s “inner reflection ... is made possible,” Austrian economist Jesús Huerta de Soto has explained, “by the fact that in economics (like no other science) the researcher enjoys the privilege of having the same nature as those observed, a situation which provides them with extremely valuable first-hand knowledge.”

To illustrate the distinction between a neoclassical and an Austrian approach, imagine a drug market consisting of two brand name drugs and generic competitors. Assuming all of the market shares were relatively small, neoclassical economics would rule out antitrust intervention on the ground that if any drug company attempted to price its drug above the competitive level for an extended period, it would reduce its profits and thus be forced to reverse course. If brand-name drug owners consistently charged higher prices, Easterbrook would urge the law to ignore the issue as beyond the ken of antitrust judges. Kaplow would require detailed economic analysis. The Austrian School would recognize that a judge is

Easterbrook disagreed, see Easterbrook, supra note 16, at 22, the Court rejected the argument that competition should not govern in a particular realm of the grocery industry because Congress must make the decision ... to sacrifice competition in one portion of the economy for greater competition in another portion.... [C]ourts are ill-equipped and ill-situated for such decisionmaking. To analyze, interpret, and evaluate the myriad of competing interests and the endless data that would surely be brought to bear on such decisions, and to make the delicate judgment on the relative values to society of competitive areas of the economy, the judgment of the elected representatives of the people is required.

Topco, 405 U.S. at 611–12.

The Austrian School’s seminal work is CARL MENGES, PRINCIPLES OF ECONOMICS 191–225 (James Dingwall & Bert F. Hoselitz trans., 1871), available at http://mises.org/Books/Mengerprinciples.pdf (addressing a theory of price in chapter five). For an accessible summary of Menger’s ideas as well as more recent work by Austrian economists, see JESÚS HUERTA DE SOTO, supra note 150, at 85–86 (comparing the Austrian School with the Neoclassical School).

HUERTA DE SOTO, supra note 150, at 16–17, 73.

Id. at 16–17.

Id. at 42.

Kaplow claims that regardless of a judge’s economic acumen, market power determinations cannot be made intuitively because nothing about “the analysis is sensory; ‘markets’ as the term is used in this context are pure abstractions.” Kaplow, supra note 9, at 507. “[N]othing one can view (that is, other than data, reports of consumer behavior, and so
capable of (1) understanding the phenomenon that leads some drug users to pay more for a branded drug that is otherwise identical to a generic and (2) using antitrust appropriately to address potential consumer harm. The following sections show the courts adhere more closely to the Austrian approach than to any version of the antitrust dichotomy.

D. The Terms Used to Define Competitive Makeup

The term competitive makeup has been chosen to contrast with the more common phrase competitive structure. The latter term suggests an objective, fixed underpinning like the skeleton of a body or the girders in a building. The term makeup is intended to suggest a more malleable subjective concept that, whether selected intentionally or developed organically, is not fixed but can be readily changed more or less without structural alterations. The competitive makeup of an industry is to its competitive structure what the psychic makeup is to the skeletal structure in a human body, and the process of determining an industry’s best competitive makeup differs from simply observing market behavior as drawing differs from tracing. A court must take account of the dimensions on which firms optimally should compete and those on which they should be permitted to cooperate or foreclose competition. A critical question will always be whether immediate short-run competition (typically on price) or longer-run competition (generally aimed at innovation) would best serve antitrust’s goal of advancing consumer welfare through competition in a particular industry at a particular time. Secondarily, questions
may arise about whether industry participants should compete on packages of goods or services, \(^{167}\) quality, \(^{168}\) or the choices provided to consumers. \(^{169}\)

Within this alternate framework, defining the competitive market is a creative, subjective process as opposed to an observational, objective one. A finding that consumers substitute one product for another or that a defendant can profitably raise price is relevant but hardly definitive. \(^{170}\) A firm’s conduct also communicates its expectation that what it does will have substantial market effect. Also, competitors and consumers will inform the judge’s understanding of how the market works. \(^{171}\) Judges meld this information with their own intuitive understanding of how entrepreneurs seek profit in order to determine an industry’s best competitive makeup.

\textit{E. An Illustrative Example}

Before examining the case law, this section presents an example illustrating the tradeoff between short and longer-term benefits that courts must make in determining an industry’s best competitive makeup. Understanding the nature

\(^{167}\) See, \textit{e.g.}, FTC v. Ind. Fed’n of Dentists, 476 U.S. 447, 459–60 (1986) (holding that in the dental industry a “refusal to compete with respect to the package of services ... no less than a refusal to compete with respect to the price term of an agreement, impairs the ability of the market to advance social welfare ...”).

\(^{168}\) See, \textit{e.g.}, \textit{Aspen Skiing}, 472 U.S. at 605–07, 610 (noting harm from the unavailability of all-Aspen ticket, that deprived consumers of the ability to “make their own choice on these matters of quality”).

\(^{169}\) See, \textit{e.g.}, NCAA v. Bd. of Regents of Univ. of Okla., 468 U.S. 85, 102 (1984) (finding that athletic association’s actions “can be viewed as procompetitive” because they “widen consumer choice ...”).

\(^{170}\) Lemley and McKenna capture the flavor of the competitive makeup inquiry in their description of how a court should approach market definition in a case involving a defendant’s intellectual property rights.

The general point is that the competitive costs of IP rights vary with the extent to which they enable the owners of those rights to exclude close substitutes, and courts should therefore conceive of competition in the IP space in terms of the quality of available substitutes .... Indeed, there may be multiple dimensions to the differentiation, including price, quality, and (for IP goods) brand association.

Lemley & McKenna, \textit{supra} note 66, at 2102.

\(^{171}\) \textit{Cf.} FTC v. Actavis, Inc., 133 S. Ct. 2223, 2236 (2013) (using evidence that patent owner agreed to pay alleged infringer large sum to drop its challenge to patent indicates that patent holder has the ability to charge supra-competitive prices); Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 218 n.4 (D.C. Cir. 1986) (quoting \textit{Brown Shoe v. United States}, 370 U.S. 294, 325 (1962)) (explaining that “[t]he ‘industry or public recognition of the submarket as a separate economic’ unit matters because we assume that economic actors usually have accurate perceptions of economic realities”).
of this critical tradeoff helps reveal the competitive makeup assessment that is often masked in the case law by the rhetoric of dichotomy.

Pursuant to the regulatory statutes governing the provision of Internet access, the Federal Communications Commission (FCC) determined whether Internet Service Providers (ISPs) that already had access to residential property—legacy telephony and cable TV companies—should be compelled to allow competitive ISPs to use the physical connections to individual homes in order to compete.\footnote{47 U.S.C.A. § 251 (West 2014).} Although the FCC’s decisions are opaque and may turn, in part, on non-economic concerns, the differing competitive makeup of the two industries can rationalize the Commission’s differing conclusions.

On the telephony side, the FCC enabled short-run price competition by requiring legacy telephone service providers to permit competitive ISPs to use their telephone wires.\footnote{In re Deployment of Wireline Servs. Offering Advanced Telecomms. Capability, 13 FCC Rcd. 24,012, 24,030–31 (1998) (classifying DSL service as a telecommunications service); In re Amendment of Sections 64.702 of the Comm’n’s Rules & Regulations (Third Computer Inquiry), 104 F.C.C.2d 958, 964 (1986).} The Commission likely concluded that innovation in telephony markets would be adequate without the additional profits that could be garnered if legacy providers were permitted to foreclose competitive ISPs. Competition, the FCC concluded, could productively regulate this realm, and the best competitive makeup of the traditional telephone industry thus included rivalry between the legacy provider and competitive ISPs to provide Internet access over telephone wires.\footnote{See H.R. REP. NO. 104-458 (1996) (stating that the purpose of the Telecommunications Act of 1996 is to “provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans”).}

In contrast, the FCC favored innovation rivalry over short-run price competition in the cable industry, allowing cable companies to foreclose competition by denying ISPs access to their cable lines.\footnote{In re Inquiry Concerning High-Speed Access to the Internet Over Cable & Other Facilities, 17 FCC Rcd. 4798, 4826 (2002).} As the Supreme Court put it, the Commission found that “changed market conditions”—namely that Internet access was already provided competitively when the cable companies sought to enter the market—“warrant[ed] different treatment” of telephone and cable companies.\footnote{Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs., 545 U.S. 967, 1001 (2005).} Presumably, the Commission compared the benefit from (1) spurring the cable companies to innovate by allowing them to avoid competition, on the one hand, and (2) the price competition that would result if ISPs were allowed to use the cable lines,
on the other. This calculation may have been accurate for two reasons. First, as the Court recognized, by the time cable companies sought to enter the ISP market, telephony access provided existing competition. The telephone companies initially had no ISP competitors. Second, the cable companies needed to exert greater innovative effort to perfect Internet access over their lines. The best competitive makeup of the cable industry thus did not require rivalry to provide Internet access over cable wires. Rather a cooperative arrangement between the cable companies and selective ISP competitors, or one in which cable companies foreclosed all competition over their lines, constituted better competitive makeups of the cable industry than one that compelled rivalry over those lines.

F. Case Law Support

Case after case reveals that antitrust courts, as the competitive makeup approach requires, trade off the benefits of short and longer-run competition to determine the realms in which rivalry should be required. From the earliest cases, the courts have recognized that competitive restraints were not all bad. Although consumers benefit immediately from the lower-priced and higher-quality goods and services that result from rivalry in the marketplace, consumers also benefit when protecting firms from competition in one realm enables them to compete efficiently in another realm.

Because blunting short-run price competition can spur innovation, the courts have permitted firms with market power to engage in anti-consumer conduct. A monopolist, for example, may charge a price exceeding the

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177 See, e.g., id. at 1000–02 (discussing why initially regulating DSL providers as common carriers promoted competition, while doing the same for cable modem service providers would do the opposite); High-Speed Access, 17 FCC Rcd. at 4826.


179 Polk Bros v. Forest City, Inc., 776 F.2d 185, 188 (7th Cir. 1985) (“Antitrust law is designed to ensure an appropriate blend of cooperation and competition, not to require all economic actors to compete full tilt at every moment.”); United States v. Addyston Pipe & Steel Co., 85 F. 271, 281 (6th Cir. 1898) (“Contracts for the partial restraint of trade are upheld, not because they are advantageous to the individual with whom the contract is made, ... but because it is for the benefit of the public at large that they should be enforced.”).

180 See, e.g., Verizon Comm’ns, Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 407 (2004) (“The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly prices—at least for a short period—is what attracts ‘business acumen’ in the first place; it induces risk taking that produces innovation and economic growth. To safeguard the incentive to innovate, the
competitive level without violating the antitrust laws, no matter how con-
clusive the evidence that the supra-competitive price harms consumers. 181
Similarly, some non-pricing practices that foreclose competition do not
violate the antitrust laws even when the defendant has market power. As
the Supreme Court explained in the early Board of Trade of Chicago deci-
sion, restraints on competition in one realm may regulate and therefore
enhance competition in another realm. 182 The Board surely had market
power, and its rule limiting certain trades unquestionably harmed those
who sought to make the prohibited trades. 183 Yet, the Court ruled in favor
of the defendant. 184 As Justice Brandeis put it, “[t]he 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.” 185

The antitrust dichotomy cannot explain the results in cases such as
Board of Trade of Chicago that permit defendants with market power to
harm consumers. But the competitive makeup approach can. Monopolists
may set high prices or foreclose certain forms of competition because
short-run harm to consumers incentivizes consumer-friendly innovation
and competitive entry in the longer run.

Just as proof of market power, no matter how extreme, and harm to
consumers does not invariably lead to antitrust liability, the absence
of market power or consumer harm does not always insulate a firm from
liability. 186 The Supreme Court has made this point repeatedly through the
per se doctrine. 187 A naked agreement to fix prices is thus per se illegal
regardless of whether the plaintiff can prove that the defendants have
market power or that consumers have been harmed. 188

Again, the antitrust dichotomy cannot explain the per se decisions. But
the competitive makeup approach can. The best competitive makeup of

181 Id. The Court has also favorably cited Mitchel v. Reynolds, 24 Eng. Rep. 347
(Q.B. 1711), which applies a similar balance to a restraint in the sale of a non-intellectual,
property-based business. See Nat’l Soc’y of Prof’l Eng’rs v. United States, 435 U.S. 679,
688–89 (1978); accord Addyston Pipe, 85 F. at 280–81.
182 Bd. of Trade of Chi., 246 U.S. at 237.
183 In particular, the Court mentions the “four or five warehouseman in Chicago” that
together had a monopoly on the trade before the restrictions were put in place. Id. at 237.
184 Id. at 241.
185 Id. at 238.
186 See infra Part IV.F.4.a.
187 See infra Part IV.F.
188 See infra Part IV.F.
most industries requires each firm to make its own decisions about output, prices, and the markets in which it will compete. Antitrust law permits cooperative behavior only when firms sufficiently integrate their operations. Even though there may be no market power or short-run competitive injury, naked horizontal agreements create the risk of undermining consumer welfare in the longer run.

The following sub-sections review the case law in some detail to show that these situations are not mere exceptions to the antitrust dichotomy. On the contrary, courts tradeoff shorter- and longer-run gains and losses, albeit sometimes tacitly, in every case to determine an industry’s best competitive makeup. Only after analyzing these tradeoffs can a court meaningfully determine whether the defendant’s conduct restrained competition that should have existed given that industry’s best competitive makeup.

1. Early Case Law

This subsection compares three early cases and demonstrates how the competitive makeup approach explains the results, but the antitrust dichotomy does not.

a. Mitchel v. Reynolds

The early English restraint-of-trade decision in Mitchel v. Reynolds, cited favorably by the U.S. Supreme Court, typifies the competitive makeup approach. In Mitchel, the court upheld an agreement prohibiting a baker from competing in a particular geographic area for five years after the sale of an ongoing business. Although restraints of trade were prohibited under English law, the court explained that when a restraint is part of a pro-competitive contract, “the particular circumstances” must be reviewed carefully before assessing the restraint’s lawfulness.

The Mitchel court upheld the restraint because it was limited to a specific “neighbourhood” where only one bakery was likely to operate. When the only question is who that operator would be, “the concern of the public is equal

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189 See Frank H. Easterbrook, The Limits of Antitrust, 63 Tex. L. Rev. 1, 13 (1984) (explaining that the patent example is “a special application of the cooperation-competition balance” and that there is always “a tradeoff between optimal incentives ex ante and optimal use of existing knowledge”).
193 Id.
194 Id. at 349.
on both sides,”\textsuperscript{195} the court explained, and the “the restraint [wa]s exactly proportioned to the consideration, viz. the term of five years.”\textsuperscript{196}

Market power was apparently irrelevant to the court’s decision. The bakery unquestionably had the power to raise price profitably and surely planned to use it. But the court never mentioned it. What mattered was that business owners should have the ability to enter reasonably limited non-compete agreements to ensure adequate incentives to build successful businesses in the first place.\textsuperscript{197} In the terms used here, the ideal competitive makeup of the baking industry permitted the defendant to foreclose competition for a period sufficient to enable the profitable sale of a business, which in turn incentivized the development of new businesses that over time would benefit consumers than short-run price rivalry would have.

\textit{b. Board of Trade of Chicago}

The same pattern can be seen again and again in U.S. Supreme Court decisions. In \textit{Board of Trade of Chicago}, an early case interpreting the Sherman Act, the government attacked the “call rule” that effectively fixed the price for grain in transit to Chicago until the market re-opened at the last price before the market close.\textsuperscript{198} In overturning a decision striking down the rule, the Court explained that any harm caused by restricting short-term price competition was outweighed by the longer-term benefits from the cost-savings, information access, and market expansion provided by the Board of Trade.\textsuperscript{199} As in \textit{Mitchel}, the best competitive makeup of the commodity trading industry did not include the sort of competition that the Board restrained. As a result, the defendant was permitted to foreclose competition in that realm.\textsuperscript{200}

\textit{c. Addyston Pipe}

In another seminal Sherman Act case, \textit{Addyston Pipe}, the government argued that a price-fixing agreement among firms selling more than half of

\textsuperscript{195} \textit{Id.} at 352.
\textsuperscript{196} \textit{Id.} Of course, if the market could really only support one bakery, there would have been no need for the covenant not to compete.
\textsuperscript{198} Bd. of Trade of Chi. v. United States, 246 U.S. 231, 237 (1918).
\textsuperscript{199} \textit{Id.} at 240–41 (explaining that these include expanded the market participants and their knowledge of the market, enabling them to operate on smaller margins and thus lower prices).
\textsuperscript{200} \textit{Id.} at 241.
the cast iron pipe in a certain geographic area violated the Sherman Act. Then-Judge Taft quoted Mitchell, explaining that “whether this is or not a reasonable restraint of trade” must turn on whether it merely “afford[ed] a fair protection to the interests of the party in favor of whom it is given,” or went further and “interfere[d] with the interests of the public.” That is, whether the restraint was in a realm best governed by rivalry.

In contrast to the restraint in Mitchell—which was upheld because it heightened the incentives to build successful businesses—the combination of price-fixing and geographic concentration in Addyston Pipe tended to “discourage industry and enterprise, and diminish the products of ingenuity and skill.” In such a case, there was little to balance against the harm resulting from a lack of price competition. No specific fact enabled the court to conclude this restraint had a deleterious effect on innovation. It certainly did not rely exclusively on market share. Instead, it subjectively assessed the industry to conclude that the form of competition restrained fell within a realm that should be competitive and thus was part of the best competitive makeup of the pipe industry.

d. Understanding the Early Cases

In Mitchell and Board of Trade of Chicago, the courts concluded that, in the industries at issue, the best competitive makeup would not compel competition among bakers immediately upon the sale of a bakery business or among commodity agents (and their buyers) during hours when a commodity exchange market was closed. Although the defendants likely had monopoly power, these forms of foreclosure and cooperation produced significant public benefits over the longer term that outweighed the short-run benefit that rivalry would have produced. In Addyston Pipe, the defendants likely had less power than the defendants in Mitchell and Board of Trade of Chicago given that they did not possess a complete monopoly and entry was likely easier. Nevertheless, the best competitive makeup of that market required pipe manufacturers to compete on short-run prices. Longer-run benefits of coordination were not wholly absent. For example,

201 Addyston Pipe, 85 F. at 291–92.
202 Id. at 282 (quoting Horner v. Graves, 7 Bing. 735, 131 Eng. Rep. 284 (C.P. 1831)); id. at 282–83 (explaining that the law permits a restraint that is “necessary to the protection of either party”).
203 Id. at 280 (quoting Alger v. Thacher, 1837 WL 3220 (Mass. 1837)).
204 Id. at 302.
205 See id.
the potential for greater profit would draw competitive entry into the pipe industry. The critical difference was that the longer-term consumer benefits from the pipe manufacturers’ restraint were unlikely to outweigh the short-run loss of competition.

2. Dominant Firm Regulation

Section 2 of the Sherman Act\(^\text{207}\) governs the unilateral activity of dominant firms.\(^\text{208}\) Just as the early agreement cases discussed above employed the competitive makeup approach rather than the paradigmatic dichotomy, the dominant firm cases do so as well.

\(a\). Alcoa

In 1945, Judge Learned Hand’s opinion in *Alcoa* articulated a theoretical basis for attacking concentrated economic power that would drive merger enforcement policy, in addition to dominant firm regulation, for two decades.\(^\text{209}\) Importantly, he stressed that if one focused exclusively on “economic considerations,” then concentrated producing power, even if not “used extortionately,” could raise serious antitrust concern.\(^\text{210}\) “[U]nchallenged economic power,” he explained may “deaden[] initiative, discourage[] thrift and depress[] energy.”\(^\text{211}\) Where competition spurs innovation, a dominant position can be a “narcotic,” deadening the competitive drive.\(^\text{212}\) “[T]he spur of constant stress is necessary,” he wrote, “to counteract an inevitable disposition to let well enough alone.”\(^\text{213}\) Although economists recognized even a monopolist must be concerned about satisfying its


\(^{208}\) United States v. Aluminum Co. of Am. (*Alcoa*), 148 F.2d 416 (2d Cir. 1945). Although *Alcoa* was a lower court decision, the Supreme Court soon clarified that it constituted binding nationwide precedent. Am. Tobacco Co. v. United States, 328 U.S. 781, 811–12 (1946) (explaining that *Alcoa* “was decided ... under unique circumstances which add to its weight as a precedent... That court sat in that case under a new statute authorizing it to render a decision ‘in lieu of a decision by the Supreme Court’ and providing that such decision ‘shall be final and there shall be no review of such decision by appeal or certiorari or otherwise.”’).


\(^{210}\) *Alcoa*, 148 F.2d at 427.

\(^{211}\) *Id.*

\(^{212}\) *Id.*

\(^{213}\) *Id.*
customers. Hand stressed “competitors, versed in the craft as no consumer can be, will be quick to detect opportunities for saving and new shifts in production, and be eager to profit by them.” Despite his famous references to market share, none of these conclusions flowed from them. Hand subjectively assessed the value of competition in the aluminum industry, taking a page from the Austrian economists’ book.

Hand has been accused of ascribing to an antiquated notion of antitrust that saw big as, invariably, bad. But he was actually quite careful not to fall into that trap. Although he certainly took market share into account, he acknowledged “size does not determine guilt; … there must be some ‘exclusion’ of competitors; … growth must be something else than ‘natural’ or ‘normal’; that there must be a ‘wrongful intent,’ or some other specific intent; or that some ‘unduly’ coercive means must be used.” As he famously put it, “[t]he successful competitor, having been urged to compete, must not be turned upon when he wins.”

Important for the purposes of this Article, Hand’s focus was decidedly not on the ability of a firm to raise price profitably. The potential benefits of competition, rather than the negative consequences of its absence drove his analysis. This point is illustrated by his decision to exclude recycled aluminum from the market. In counting only virgin aluminum, Hand effectively decided the best competitive makeup of the aluminum industry would stimulate the market for recycling longer term—rather than maximize short-run price.

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214 Id. at 426–27.
215 Id. The U.S. Supreme Court explicitly adopted this reasoning in Am. Tobacco Co. v. United States, 328 U.S. 781, 813–15 (1946).
216 Alcoa, 148 F.2d at 427 (explaining that while a share “over ninety ... is enough to constitute a monopoly; it is doubtful whether sixty or sixty-four percent would be enough; and certainly thirty-three per cent is not”).
217 See id.; infra Part IV.B.
218 Eugene V. Rostow, The New Sherman Act: A Positive Instrument of Progress, 14 U. CHI. L. REV. 567, 577 (1947) (commenting that “[i]n the Aluminum case Judge Hand finally interred and reversed the old dictum that size is not an offense under the Sherman Act. Size, he concluded, was not only evidence of violation, or a potential offense, ... it was the essence of the offense”).
219 Alcoa, 148 F.2d at 429.
220 Id. at 430.
221 See id. at 427 (mentioning existence of social and moral benefits resulting from having many competitors in an industry, rather than a few).
222 Id. at 425 (referring to recycled aluminum as “secondary”).
223 Id. Similarly, in discussing imported aluminum, Judge Hand made the judgment that the antitrust market should be narrow enough to preclude Alcoa’s exploiting “the limits afforded by the tariff and the cost of transportation.” Id. at 426.
used his ability to subjectively assess the value of competition in the industry before him to determine the best competitive makeup of the aluminum industry.

b. Grinnell and Griffith

By the 1960s, United States v. Grinnell Corp. established that section 2 case required a plaintiff to demonstrate that the defendant “willful[ly] acqui[red] or maint[ained] ... [monopoly] power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.”224 The use of a dominant position to gain a competitive advantage, however, was suspect. In United States v. Griffith,225 for example, the Court explained that a firm with a dominant position in fire alarm systems in some geographic markets could not use that position “to gain a competitive advantage”226 elsewhere even if “no competitors were driven out of business, or acquired by appellees, or impeded in their business by threats or coercion ....”227 Again, the focus on competitive advantage embodied a subjective assessment about the value of competition in a particular realm, rather than an objective calculation of the defendant’s ability to properly raise price.228

The Second Circuit’s analysis of the price squeeze—the spread between Alcoa’s wholesale and retail price—similarly constructed a competitive makeup in which Alcoa had to enable meaningful retail competition. Id. at 436–38. That conclusion about the aluminum industry differs from the Supreme Court’s recent assessment of a price squeeze in the telecommunications market. Pac. Bell Tel. Co. v. Linkline Commc’ns, Inc., 555 U.S. 438 (2009). But that difference is precisely the point—courts do not simply observe market behavior; they construct appropriate competitive makeups for the industry in question. The appropriate makeup of the unregulated aluminum industry in the 1940s surely differed from the best makeup of the regulated telephony industry in the early twenty-first century.

225 334 U.S. 100 (1948).
226 Id. at 107.
227 Id. at 109.
228 Even Du Pont can be interpreted as divining the best competitive makeup of the industry. Although it is generally interpreted as resolving the case at the first stage of a dichotomous analytic by finding that Du Pont lacked market power, it may have actually held that the best competitive makeup of the flexible wrapping industry does not require competition within individual types of wrapping. Given that the government alleged that Du Pont had monopolized the “cellophane market,” the Court may have ruled against the government not because Du Pont lacked market power, but because there was no cellophane market to monopolize. See United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377 (1956).
c. Modern Dominant Firm Doctrine

In the past decade, the Court has seemingly contradicted Alcoa’s approach,\(^{229}\) holding that even where statutory law compels cooperation,\(^{230}\) the antitrust laws do not.\(^{231}\) A monopolist telecommunications carrier is thus free, as far as the antitrust laws are concerned, to gain a competitive advantage from its dominant position by refusing to deal with competitors, delaying a competitor’s entry,\(^{232}\) or charging a price for wholesale services that is too high to permit viable retail competition.\(^{233}\)

Alcoa’s monopolization standard has thus evolved, but not toward one that focuses on the ability to raise price profitably as the singular threshold issue. Rather, the Court has continued to search for an industry’s ideal competitive makeup. Judge Hand was faced with determining the makeup for a mid-century, unregulated, relatively stable aluminum industry in which new entrants faced significant barriers to entry. He concluded the best competitive makeup of such an industry—the one that would best serve consumer interests—required a successful enterprise to avoid a sustained dominant position by dealing with competitors on reasonable terms.\(^{234}\)

For the modern Court, the best competitive makeup in the dynamic, twenty-first century, regulated telecommunications industry, not surprisingly, did not include similar duties to foster short-run competition.\(^{235}\) Barriers to new entry were lower and supported by specific statutory requirements designed to

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\(^{229}\) Pac. Bell Tel. Co. v. Linkline Commc’ns, Inc., 555 U.S. 438, 452 n.3 (2009) (signaling the Court’s change in view by responding to an argument based on Alcoa by stating that “[g]iven developments in economic theory and antitrust jurisprudence since Alcoa, we find our recent decisions ... more pertinent to the question before us”).

\(^{230}\) See generally Steven Semeraro, The Efficiency and Fairness of Enforced Sharing: An Examination of the Essence of Antitrust, 52 U. KAN. L. REV. 57 (2003) (analyzing the Supreme Court’s refusal to find an antitrust violation when a monopolist violated a statutorily imposed duty to cooperate).

\(^{231}\) Pac. Bell, 555 U.S. at 448 n.2 (2009) (holding that duties imposed by telecommunications regulations do not impose antitrust duties).


\(^{233}\) Pac. Bell, 555 U.S. at 450–51.

\(^{234}\) Alcoa, 148 F.2d 416, 430 (2d Cir. 1945) (noting Alcoa’s practices and dealings with potential competitors prevented them from ever entering market).

\(^{235}\) The Court made quite clear that the regulated nature of the telecommunications industry was relevant to its decision. Verizon, 540 U.S. at 411–12 (“One factor of particular importance is the existence of a regulatory structure designed to deter and remedy anti-competitive harm. Where such a structure exists, the additional benefit to competition provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny.”).
channel competition. In that context, the Court concluded, the tradeoff between short-run high prices and longer-run entry and innovation weighed in favor of using rivalry to regulate the longer-run realm.

Justice Scalia made this point quite explicitly for the Court in *Verizon*, emphasizing that antitrust law’s longer-run goal is “[t]o safeguard the incentive to innovate.” The ability to raise price profitably was a positive development for consumer welfare in this industry. Scalia explained:

> The mere possession of monopoly power, and the concomitant charging of monopoly prices is not only not unlawful, it is an important element of the free-market system. The opportunity to charge monopoly prices—at least for a short period—is what attracts ‘business acumen’ in the first place; it induces risk taking that produces innovation and economic growth.

The Court determined that the best competitive makeup of the telecommunications industry did not require the short-run competition that the plaintiff sought because longer-run competition better served consumer interests.

d. Dominance Through Intellectual Property Rights

In many cases, intellectual property rights may convey a degree of market power on an antitrust defendant. Like any dominant firm, an intellectual property holder may use this power to form cooperative relationships through licensing, or it may attempt to foreclose competition altogether by prohibiting competitors from using its property. Under the antitrust dichotomy, when an intellectual property holder has market power, increasing short-run prices would appear to violate the law. After all, the defendant has power and is foreclosing competition and charging prices above the competitive level.

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239 Id.; see Hovenkamp, supra note 80, at 2148 (“The inducement for creating [intellectual property] is the prospect of the ... returns” it generates.).

240 Verizon, 540 U.S. at 407–08.

241 See United States v. Gen. Elec. Co., 272 U.S. 476, 489 (1926) (permitting patentee to license a patented technology that controlled the resale price of a patented article at a time when resale price maintenance was treated as per se illegal); Easterbrook, supra note 16, at 13 (“[I]t is now understood that the grant of patent rights, though creating a restriction of output during the patent’s life, is important to give people incentives to invent.”).
The competitive makeup approach, however, explains why intellectual property holders may sometimes, but only sometimes, violate the antitrust laws. Longer-run innovative competition is often more valuable in intellectual property intensive industries, and when that is true, antitrust does not require rivalry with respect to either prices or short-run quality improvements.

Some antitrust cases in the lower courts suggest that property rights entirely exempt a defendant from antitrust scrutiny. The Supreme Court, however, has repeatedly rejected that approach. To be sure, industries in which intellectual property rights are important have different competitive makeups than industries without significant intellectual property rights. But those differences do not immunize intellectual property holders from antitrust liability. Recognizing that creative entrepreneurs will discover ways to use their intellectual property to stifle rivalry in realms where it would benefit consumers, the Court has imposed antitrust liability on intellectual property owners of every sort. The Court also developed the concept of misuse—including the first-sale rule, the patent fraud doctrine, and the prohibition of sham litigation—to

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243 See Actavis, 133 S. Ct. 2223, 2232 (2013).

244 See id. (holding that settlement of a drug patent case may violate the antitrust laws even if the patent is valid); United States v. Loew’s, Inc., 371 U.S. 38, 49–50 (1962) (holding the same for a copyright holder); United States v. U.S. Gypsum Co., 333 U.S. 364, 390–91 (1948) (holding that courts must “balance the privileges of [the patent holder] and its licensees under the patent grants with the prohibitions of the Sherman Act against combinations and attempts to monopolize.”); United States v. Line Material Co., 333 U.S. 287, 310 (1948) (holding that a cross licensing agreement that included resale price maintenance of patented products set by agreement among the patent holders constituted “the improper use of [a patent] monopoly” violating the antitrust laws).

Similar considerations also drive whether a patent should even be available. See Mayo Collaborative Servs. v. Prometheus Labs., Inc., 132 S. Ct. 1289, 1305 (2012).

245 See, e.g., Brulotte v. Thys Co., 379 U.S. 29, 30 (1964) (holding that attempting to charge licensing royalties beyond expiration of a patent constitutes misuse).

246 See, e.g., Quanta Computer, Inc. v. LG Elecs., Inc., 553 U.S. 617, 621 (2008) (holding that patent may not be used to restrain competition after first sale).


248 Prof’l Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc., 508 U.S. 49, 60–61 (1993) (adopting standards for showing when sham efforts to enforce a patent may violate the antitrust laws).
identify when a realm should be rivalrous despite a significant intellectual property right.\textsuperscript{249}

The functionality doctrine in trademark law further illustrates the approach courts take in intellectual property cases.\textsuperscript{250} The doctrine prohibits a firm from using a functional aspect of its product as a trademark because doing so would “inhibit[] legitimate competition by allowing a producer to control a useful product feature.”\textsuperscript{251} In most situations, competition to use a particular mark is not required because consumers receive greater long-run benefits by relying on marks to identify the source of products. For example, in \textit{Brandir International, Inc. v. Cascade Pacific Lumber Co.},\textsuperscript{252} the trademark owner was able to prevent a competitor from using a mark embodying a feature of the product. The Second Circuit held that the one-piece undulating feature of a bicycle rack was not functional because other forms of bicycle racks could be made that would compete with the trademark holder’s rack.\textsuperscript{253} This conclusion was not self-evident. The court had to consider the nature of

\textsuperscript{249} \textit{Mayo}, 132 S. Ct. 1289, 1293 (2012) (“The grant of a patent might tend to impede innovation more than it would tend to promote it … [and] too broad an interpretation of this exclusionary principle could eviscerate patent law.”). The Court further explained that: Patent protection is, after all, a two-edged sword. On the one hand, the promise of exclusive rights provides monetary incentives that lead to creation, invention, and discovery. On the other hand, that very exclusivity can impede the flow of information that might permit, indeed spur, invention, by, for example, raising the price of using the patented ideas once created, requiring potential users to conduct costly and time-consuming searches of existing patents and pending patent applications, and requiring the negotiation of complex licensing arrangements. At the same time, patent law’s general rules must govern inventive activity in many different fields of human endeavor, with the result that the practical effects of rules that reflect a general effort to balance these considerations may differ from one field to another.

\textit{Id.} at 1305; \textit{see} Semeraro, \textit{supra} note 230, at 76–79 (reviewing case law requiring firms to share property to facilitate competition).


\textsuperscript{251} \textit{Id.}

\textsuperscript{252} \textit{Brandir Int’l Inc. v. Cascade Pac. Lumber Co.}, 834 F.2d 1142, 1148 (2d Cir. 1987); \textit{see also} \textit{Topps Co. v. Gerrit J. Verburg Co.}, 96 Civ. 7302 (RWS), 1996 U.S. Dist. LEXIS 18556, at *22–26, *28–29 (S.D.N.Y. Dec. 13, 1996) (holding that an infringer cannot circumvent trade dress protection by asserting a defense of functionality on the theory the prior user’s design constitutes a narrow product line, with which the infringer can only compete by copying the prior user’s design elements); \textit{Warner Bros. Inc. v. Gay Toys, Inc.}, 724 F.2d 327, 330, 334 (2d Cir. 1983) (defining product line as toy cars rather than “Dukes of Hazzard” toy cars); \textit{In re DC Comics, Inc.}, 689 F.2d 1042, 1045 (C.C.P.A. 1982) (defining product line as toy dolls rather than superhero dolls).

\textsuperscript{253} \textit{Brandir Int’l}, 834 F.2d at 1148.
competition in bicycle rack markets to determine that the industry’s best competitive makeup favored longer-run competition to innovate new types of bicycle racks over short-run price competition of those with Brandir’s one-piece undulaters.

When a court concludes a mark contains a functional element, the tradeoff flips in favor of short-run competition. For example, in Dippin’ Dots, Inc. v. Frosty Bites Distribution, the court held that a trademark on the shape of frozen ice cream was functional. Of course, ice cream has long been sold in a variety of other forms, and thus competition could have continued even if the plaintiff were prohibited from using a particular shape. The court had to subjectively assess the industry’s competitive makeup to conclude that in the ice cream industry short-run competition with respect to a particular shape would best serve consumer interests.

Again, the antitrust dichotomy cannot explain the results in these cases. Firms with strong brands often have market power, and limiting the use of their trademarks by competitors will harm consumers through higher prices. The power-or-effect dichotomy has no ready means to explain why trademark holders can exploit this market power only if their marks do not include functional elements of their product.

The competitive makeup approach provides a workable system to decide these cases. By taking account of the relative value of short- and longer-term consumer interests within a particular industry, a court determining the best competitive makeup can reasonably evaluate the value of rivalry with respect to a trademarked element.

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254 Dippin’ Dots, Inc. v. Frosty Bites Distribution, LLC, 369 F.3d 1197, 1202 (11th Cir. 2004).
255 Id. at 1206.
256 See generally Desai & Waller, supra note 143, at 1450–84 (discussing the relationship among brands, trademarks, and competition).
257 In line with the 2010 merger guidelines and Kaplow’s critique, Lemley and McKenna argue that antitrust law needs to use evidence of anticompetitive effects, rather than purely structural evidence, to determine market power. Lemley & McKenna, supra note 66, at 2059. “The problems with market definition also mean that antitrust law must pay more attention to actual competitive effects and less attention to nice numerical formulas in evaluating mergers and anticompetitive conduct.” Id. at 2101. An enhanced focus on effects, however, cannot bring coherence to the antitrust dichotomy because it does not provide a means to determine if particular effects are justified. Lemley and McKenna correctly recognized that courts need to determine “how much competition we want in this space” and that “they might well make different policy judgments in different circumstances.” Id. at 2102–03.
3. Merger Cases

In the 1950s and 1960s, the Supreme Court precluded mergers that increased concentration even when the merged firm’s share was not large enough to suggest market power. In these cases, the Court did not focus on the post-merger firm’s immediate ability to raise prices profitably. But it did recognize that its task was more complicated than simply calculating market shares. In *Philadelphia National Bank*, for example, Justice Brennan wrote that assessing the competitive impact of a merger required “a workable compromise” that “delineat[ed]” the market in a “fair” way. There, the Court recognized that it could have legitimately viewed the banking market in different ways. In these merger cases, the Court appears to have appreciated that it needed to determine the best competitive makeup of the industry, rather than merely calculating market shares to determine market power. Its process appears to have favored the long-run goal of encouraging internal expansion rather than growth through merger.

The Court’s most recent substantive merger case, *United States v. General Dynamics*, is often read as a change of course from its earlier cases. Rather than block a merger despite relatively low market shares, the Court permitted a merger despite relatively high shares. Again, however, the apparent change can also be explained by the Court’s following the competitive makeup approach rather than the antitrust dichotomy.

In *General Dynamics*, the government presented evidence based on historic sales of an increasingly concentrated coal market. Based on the standard paradigm, the merger certainly appeared problematic given the large market shares. But the trial court was not fooled, recognizing that the competitive makeup of the coal industry did not support the government’s proposed market or the inference of market power from historic

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259 See, e.g., United States v. Aluminum Co. of Am., 377 U.S. 271, 281 (1964) (explaining that the acquired company “seems to us the prototype of the small independent that Congress aimed to preserve”); United States v. Phila. Nat’l Bank, 374 U.S. 321, 365 n.42 (1963) (“[I]f concentration is already great, the importance of preventing even slight increases in concentration and so preserving the possibility of eventual deconcentration is correspondingly great.”).
261 *Id.* at 360–61.
263 *Id.* at 503.
264 *Id.* at 494–96.
265 See *id.* at 496 (recognizing that the Court had blocked mergers based on the type of statistical showing that the government offered).
sales.\textsuperscript{266} In upholding the trial court, Justice Stewart explained the competitive makeup of industries such as beer and groceries—where the Court had blocked mergers despite small shares—\textsuperscript{267} included an assumption that historic market shares would likely persist.\textsuperscript{267} The coal industry had a different competitive makeup because uncommitted reserves constituted a better measure of future competitive significance.\textsuperscript{268}

Since the 1970s, the Supreme Court has not played a significant role in merger enforcement.\textsuperscript{269} But the leading lower court cases, including \textit{FTC v. Staples}\textsuperscript{270} and \textit{FTC v. Whole Foods Market},\textsuperscript{271} have turned on competitive makeup rather than inferences of market power drawn from market shares. In \textit{Staples}, the court looked past the many sources of office supplies and the small shares of individual providers, focusing on the meaningful competition that existed between office superstores.\textsuperscript{272} Although the Court acknowledged “a broad market encompassing the sale of consumable office supplies by all sellers of such supplies” and that all these sellers “at some level, compete with one another,” it ultimately used market definition as a tool to reveal a competitive makeup for the office supply industry that required superstores to compete.\textsuperscript{273}

In \textit{Whole Foods}, the lower court concluded that all grocery stores were in the relevant market and, thus, the best competitive makeup did not require competing stores specializing in organic products.\textsuperscript{274} The appellate court disagreed, not because the lower court drew the wrong inference from the observable facts, but because the appellate court recognized a possibility for beneficial competition in organic products.\textsuperscript{275} That is, the best competitive makeup of the grocery industry would include a rivalrous realm in the sale of organic products.

\begin{footnotesize}
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\item \textsuperscript{266} \textit{Id.} at 491–94.
\item \textsuperscript{267} \textit{Id.} at 501.
\item \textsuperscript{268} \textit{Id.} at 501–02.
\item \textsuperscript{269} Thomas E. Kauper, \textit{Merger Control in the United States and The European Union: Some Observations}, 74 ST. JOHN’S L. REV. 305, 315 (2000) (explaining that “[t]he Supreme Court has not decided a merger case on the merits since 1974”).
\item \textsuperscript{271} FTC v. Whole Foods Mkt., Inc., 548 F.3d 1028 (D.C. Cir. 2008).
\item \textsuperscript{272} \textit{Staples}, 970 F. Supp. at 1080.
\item \textsuperscript{273} \textit{Id.} at 1075.
\item \textsuperscript{274} \textit{Whole Foods}, 548 F.3d at 1033 (citing district court opinion).
\item \textsuperscript{275} See \textit{id.} at 1040–41 (recognizing that core customers would pay more for some organic products); \textit{id.} at 1046–47 (Tatel, J., concurring) (following \textit{Staples} holding evidence of higher prices in markets where the merging parties did not compete suggests they are in separate markets).
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In each case, the decision turned on an assessment about how competition should operate in the industry, not strictly on an observation of how it did operate. To be sure, the courts relied on statistics about how certain types of competition affected certain types of prices. But the decision was not dictated by statistics. As the disagreement among the judges on the appellate panel in *Whole Foods* demonstrated, the decision about whether competition in a particular realm was required had to be constructed from a conception of the proper makeup of the market.

4. *Modern Non-merger Horizontal Agreement* Cases

Under section 1 of the Sherman Act, the competitive makeup approach again explains the case law more readily than the paradigmatic dichotomy. The following sections review the per se doctrine, which imposes liability without proof of market power. It then compares and contrasts two pairs of similar rule-of-reason cases, and finally, it reviews the Court’s most recent rule-of-reason case, which renewed the long-standing position that intellectual property rights do not insulate an agreement from antitrust scrutiny.

4a. *Per Se* Cases

The *per se* doctrine provides the clearest example of the use of the competitive makeup approach. It holds that naked horizontal agreements that restrain trade are illegal without requiring the plaintiff to prove that the defendant had market power or that consumers were harmed. Per se illegal practices are often said to include price-fixing, market division, bid rigging, customer allocation, and certain group boycotts.
actual practice, however, the Supreme Court has not imposed bright-line rules. Instead, courts decide whether a per se rule applies by determining the best competitive makeup of the industry.

The competitive makeup inquiry in per se cases is implemented through what the courts have called the naked agreement requirement. A business practice that would be per se illegal may not be if it is an integrated part of a potentially pro-competitive agreement. For example, a group boycott is per se illegal if it functions solely to restrain immediate price competition in a market where innovation is not important. In contrast, a boycott may be lawful when used to enforce rules governing a pro-competitive group purchasing agreement. Even agreements fixing price may be permissible when sufficiently integrated into a pro-competitive scheme.

These decisions about whether an agreement is naked or integrated are inquiries into the competitive makeup of the industry. Some integration is not enough, and no universal rule draws a bright line. Rather, the per se cases are best understood to condemn an agreement when a court determines that competition in a particular industry should govern the realm in to compete on credit terms); United States v. Topco Assocs., Inc., 405 U.S. 596, 608 (1972) (agreement to divide territories); Klor’s, Inc. v. Broadway-Hale Stores, Inc., 359 U.S. 207, 211–13 (1959) (group boycott); Int’l Salt Co. v. United States, 332 U.S. 392, 395–96 (1947) (tying); Fashion Originators’ Guild of Am., Inc. v. FTC, 312 U.S. 457, 466–67 (1941) (group boycott); United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 223 (1940) (agreement to stabilize price); United States v. Addyston Pipe & Steel Co., 85 F. 271 (6th Cir. 1899), modified, 175 U.S. 211 (1899) (territorial division).

See supra notes 281–82.

BMI, 441 U.S. at 20 (explaining that the agreement before the Court was “not a ‘naked restrain[t] of trade with no purpose except stifling of competition,’ ... but rather [it] accompanie[d] the integration of sales, monitoring, and enforcement”); compare Texaco Inc. v. Dagher, 547 U.S. 1, 5–7 (2006) (refusing to apply per se rule to an integrated joint venture agreement that included a jointly set price term), with White Motor Co. v. United States, 372 U.S. 253, 263 (1963) (explaining that per se rule applies to “naked restraints of trade with no purpose except stifling of competition ...”).

See Texaco, 547 U.S. at 5–6.


See BMI, 441 U.S. at 20.

Arizona v. Maricopa Cnty. Med. Soc’y, 457 U.S. 332, 342, 348 (1982) (applying the per se rule even though an agreement to set maximum prices was part of an integrated agreement to provide insurance coverage).
which the agreement restrained rivalry. By concluding that an agreement is sufficiently integrated, however, the court effectively finds the competitive makeup of the industry is such that competition should not govern the realm in which the agreement restrained rivalry.\footnote{See \textit{Texaco}, 547 U.S. at 5–6, (refusing to apply the per se rule to integrated agreement). In rejecting the per se rule, a court would not be holding definitively that the best competitive makeup of the industry has been achieved. It would signal only that further analysis would be required. \textit{BMI}, 441 U.S. at 24–25 (rejecting application of the per se rule but remanding with instructions to consider the practice under the rule of reason).}

In both \textit{BMI} and \textit{Catalano}, the parties made plausible arguments that their agreements were integrated.\footnote{\textit{BMI}, 441 U.S. at 7.} In the former, the Court concurred because blanket song-copyright licenses significantly reduced the transaction costs that individual negotiation and monitoring would entail.\footnote{\textit{BMI}, 441 U.S. at 20–21.} By contrast, the Court rejected the Ninth Circuit’s finding that an agreement prohibiting the sale of beer on credit was part of an integrated scheme to (1) open the distribution market to new competitors and (2) spur competition by increasing pricing visibility.\footnote{\textit{Catalano}, 446 U.S. at 645–46.} No objective standard of integration dictated these results. Rather, the Court determined that the best competitive makeup of the beer delivery industry required immediate competition on credit terms while the best competitive makeup of song-copyright licensing did not necessarily compel individual copyright owners to compete on price.\footnote{\textit{Id. at 643–44; BMI, 441 U.S. at 20–22.}}

\textit{b. Professional Engineers and California Dental Association}

In 1978’s \textit{National Society of Professional Engineers}, the Antitrust Division challenged a rule prohibiting engineers from including a price in their initial project proposal.\footnote{Nat’l Soc’y of Prof’l Eng’rs v. United States, 435 U.S. 679, 681(1978).} In 1999’s \textit{California Dental Association}, the FTC challenged a rule prohibiting dentists from including discounting information in advertisements.\footnote{Cal. Dental Ass’n v. FTC, 526 U.S. 756, 762 (1999).} In both cases, the organizations sought to justify their rules on ethical grounds,\footnote{\textit{Id. at 760–61; Prof’l Eng’rs, 435 U.S. at 681.}} and both associations had market power. The Court struck down the engineers’ rule but not the dentists’.\footnote{\textit{Cal. Dental, 526 U.S. at 781; Prof’l Eng’rs, 435 U.S. at 694–96.}}

The difference in the outcomes can be explained by the contrasting competitive makeups of the two industries. In bidding markets with sophisticated buyers, as with most engineering projects, if firms include prices in their
bids, the ensuing competition would stimulate more efficient engineering. The engineers countered that the tradeoff for short-run price competition would be a longer-run trend toward unethical bidding and compromises on safety and quality.

In favoring short-run price competition in the engineering industry, the Court did not discuss the defendant’s market power. Instead, it contrasted the facts before it with those of Mitchell v. Reynolds. In that case, Justice Stevens explained, the English court had held that “[t]he long-run benefit of enhancing the marketability of the business itself—and thereby providing incentives to develop such an enterprise—outweighed the temporary and limited loss of competition.” No similar long-run competitive concern in the engineering market outweighed the benefit of short-run competition. As a result, the best competitive makeup of the engineering industry included price competition in engineers’ initial bids.

In California Dental, by contrast, the Court recognized that retail dental markets are “characterized by striking disparities between the information available to the professional and the patient,” a mass market of unsophisticated customers. Even competitors, Justice Souter recognized, faced “significant challenges to informed decisionmaking.” In overturning the lower court’s use of a truncated rule-of-reason analysis, the majority focused on the tradeoff between short-run price competition that discount advertising would generate and longer-run competition made possible by preserving a market in which relatively uninformed customers had accurate information. On remand, the lower court chose a competitive makeup that permitted advertising restraints to ensure more accurate information.

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299 Prof’l Eng’rs, 435 U.S. at 695 (“The assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain-quality, service, safety, and durability—and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers.”).
300 Prof’l Eng’rs, 435 U.S. at 693–94.
301 See id.
302 See supra Part IV.F.1.a; Prof’l Eng’rs, 435 U.S. at 688–89.
303 Prof’l Eng’rs, 435 U.S. at 689.
304 Id. at 696.
305 Id.
307 Id. at 773.
308 Id. at 763–65.
309 See id. at 774–75 (“[E]ven if across-the-board discount advertisements were more effective in drawing customers in the short run, the recurrence of some measure of intentional or accidental misstatement due to the breadth of their claims might leak out over time to make potential patients skeptical of any such across-the-board advertising, so undercutting the method’s effectiveness.”).
310 Cal. Dental Ass’n v. FTC, 224 F.3d 942, 957 (9th Cir. 2000).
Justice Souter’s opinion in *California Dental* went further than *Professional Engineers* in highlighting the subjective component of antitrust analysis. First, he explained that in the Supreme Court cases in which antitrust liability had been upheld, “an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets.” As Justice Souter emphasized, reaching that conclusion required courts to consult “theory” and consider the impact of a restraint within a particular industry. Merely observing market facts was not enough.

Second, although the available facts about how the market operates are relevant, identifying the industry’s best competitive makeup is the judge’s ultimate task. Without mentioning market power, Justice Souter’s majority opinion explained that “there must be some indication that the court making the decision has properly identified the theoretical basis for the anticompetitive effects and considered whether the effects actually are anticompetitive.” He also “emphasized the necessity, particularly great in the quasi-common law realm of antitrust, that courts explain the logic of their conclusions,” where mechanically applying a formula would not suffice. “[T]here is generally no categorical line to be drawn,” he explained, between types of restraints. “What is required ... is an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint. The object is to ... [make] a confident conclusion about the principal tendency of a restriction ... .”

c. NCAA and BMI

In the *NCAA v. Board of Regents of University of Oklahoma* football case and the *Broadcast Music, Inc. v. CBS* copyright case, the

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311 *Cal. Dental*, 526 U.S. at 770.
312 See id. at 771.
313 See id. at 773 (emphasizing that an anticompetitive practice in one industry “could have different effects from those ‘normally’ found in the commercial world” in another industry, perhaps even pro-competitive effects).
314 See id. at 779 (holding that the “Court of Appeals’s [sic] conclusion at least required a more extended examination of the possible factual underpinnings”).
315 Even the dissent only “assume[d]” that market power would be a relevant issue. *Id.* at 788 (Breyer, J., dissenting).
316 *Id.* at 775 n.12 (emphasis added).
317 *Id.* at 780.
318 *Id.*
319 *Id.* at 781.
Court dealt with licensing arrangements between the defendants and television networks. The Court in *NCAA* held that universities had to engage in short-run price competition to license college football telecasts.\(^\text{322}\) In *BMI*, however, the Court found reasons to favor a different competitive makeup in the music copyright licensing industry. The benefits of coordination in licensing thousands of available songs—such as one-stop shopping and centralized monitoring—created long-run competitive benefits that outweigh the short-run benefits that would flow from copyright-to-copyright price competition.\(^\text{323}\) No similar long-run benefit applied to the televising of college football games, and thus the Court determined that the competitive makeup of the college football television market required short-run competition.\(^\text{324}\)

d. *Actavis*

In its most recent antitrust case, *FTC v. Actavis, Inc.*,\(^\text{325}\) the Court held that a patent holder could violate the antitrust laws by paying an alleged infringer to withhold its product from the market until the patent expired.\(^\text{326}\) Lower courts had held that as long as the agreement limited competition during the life of the patent, the settlement would fall within the patent’s scope and could not violate the antitrust laws.\(^\text{327}\) The Court rejected that reasoning.\(^\text{328}\) A court must, Justice Breyer wrote for the majority, “seek to accommodate patent and antitrust policies.”\(^\text{329}\) This process involves more than the search for market power and competitive effects. After all, the patent holder obviously had market power and the agreement ensured that consumers would pay much more for the drug than they would have in a competitive market. Under the antitrust dichotomy, the defendant’s payment would always violate the antitrust laws.

The Court might have recognized a bright-line exception for patent holders, but it did not. Trial courts, the *Actavis* majority explained, must consider all aspects bearing on the anticompetitive effect of a business

\(^\text{322}\) *NCAA*, 468 U.S. at 113.


\(^\text{324}\) *NCAA*, 468 U.S. at 113.

\(^\text{325}\) 133 S. Ct. 2223 (2013).

\(^\text{326}\) Id. at 2227.

\(^\text{327}\) Id. at 2230.

\(^\text{328}\) See id. at 2227.

\(^\text{329}\) Id. at 2233.
practice to determine whether a patent holder violated the antitrust laws. Courts must vary the depth of their inquiry “with the circumstances” and “avoid, on the one hand, the use of antitrust theories too abbreviated to permit proper analysis, and, on the other, consideration of every possible fact or theory irrespective of the minimal light it may shed on the basic question—that of the presence of significant unjustified anticompetitive consequences.” In other words, the court must determine the best competitive makeup of the industry in order to assess whether the defendant restrained rivalry in a realm efficiently governed by competition.

V. RESPONDING TO THE LIKELY CRITIQUE

Critics of the competitive makeup approach will likely contend that Part IV reads too much into Supreme Court dicta and places too little weight on lower court cases that time and again dismiss antitrust claims based solely—so they say—on the defendants’ lack of market power. In per se cases, the critic will likely argue that the Court simply presumes that market power exists. The intellectual property cases are exceptions in which market power is tolerated, and in the dominant firm, merger, and rule-of-reason and agreement cases, the Court was either (1) discussing market power without saying so explicitly or (2) discussing effects in cases where market power was obvious.

This Part distinguishes the antitrust dichotomy and the competitive makeup approaches and then shows that courts do not apply the dichotomy even when they say that they are.

A. Distinguishing the Antitrust Dichotomy from the Competitive Makeup Approach

How one views antitrust analysis depends on how one frames the concept of market power. Everyone knows the market share needed to establish power under the standard dichotomy varies by industry and depends on entry barriers, excess capacity, and other factors. Similarly, the competitive makeup takes account of a defendant’s ability to impact the market in determining

330 See id. at 2238.
331 Id.
332 Id. at 2237 (stressing that “[t]he existence and degree of any anticompetitive consequence may also vary ... among industries”).
333 See, e.g., Bathke v. Casey’s Gen. Stores, Inc., 64 F.3d 340, 345 (8th Cir. 1995) (“Antitrust claims often rise or fall on the definition of the relevant market.”).
334 See, e.g., Continental T.V., Inc., v. GTE Sylvania, Inc., 433 U.S. 36 (1977) (holding that a location restriction should be analyzed under the rule of reason); United States v. Waste Mgmt., Inc., 743 F.2d 976 (2d Cir. 1984) (holding that low barriers to entry rendered the resulting high market share of a merger inapposite).
which realms should be governed competitively. No one would dispute that rivalry is not always required and that the value of competition varies across industries and time.\footnote{E.g., Polk Bros. v. Forest City, Inc., 776 F.2d 185, 188 (7th Cir. 1985) ("Antitrust law is designed to ensure an appropriate blend of cooperation and competition, not to require all economic actors to compete full tilt at every moment."); United States v. Addyston Pipe & Steel Co., 85 F. 271, 281 (6th Cir. 1898) ("Contracts for the partial restraint of trade are upheld, not because they are advantageous to the individual with whom the contract is made, ... but because it is for the benefit of the public at large that they should be enforced.").}

The real point of disagreement is whether market power is capable of playing the gatekeeper role Easterbrook envisioned for it.\footnote{See Easterbrook, supra note 16.} If all a critic of the competitive makeup approach means by a “market power threshold inquiry” is that courts impose antitrust liability only when the defendants are capable of harming consumers, then there is no real disagreement.\footnote{See, e.g., Easterbrook, supra note 16, at 2, 5–11.} It is always possible at the end of the analysis to conclude that if rivalry should prevail in a particular market realm, then the defendants’ conduct is not innocuous.

Concluding post-hoc that the defendant may cause harm, however, is not what the antitrust dichotomy holds. As crystallized by Landes, Posner, and Easterbrook (and as accepted by virtually all modern antitrust commentators), the dichotomy maintains that a court can meaningfully determine whether a defendant has the ability to harm consumers without examining what the defendant has actually done or theorizing about what it might do.\footnote{See Landes & Posner, supra note 27; Easterbrook, supra note 16.} Indeed, the main point of the market power threshold, according to Easterbrook, was to free courts from the need to assess conduct and effect by allowing them to focus exclusively on market structure.\footnote{Easterbrook, supra note 16, at 39.}

This Article contends that market power cannot meaningfully play this role. To assess a potential threat to consumer interests, a court must determine whether competition should govern the realm in which the defendant is accused of acting anti-competitively, and that decision will invariably involve a tradeoff between short-run and longer-term consumer benefits. Sometimes market power will be important, but not always. It simply cannot play a threshold role. Apparently recognizing this reality, courts analyze antitrust cases using the competitive makeup approach both because the Supreme Court has told them to and because it is the only logical way to do it.\footnote{See supra Part I.}
B. Revealing Competitive Impact Analysis Within a Rhetoric of Dichotomy

Courts recite the rhetoric of dichotomy.\(^{341}\) When a judge imposes antitrust liability, the defendants will typically have large market shares, but when a court holds that the defendants did not violate the law, their shares will often be small. Courts understandably rely on these small shares to dismiss the case and truncate appellate review without articulating why competition was not required in the realm in which the defendant’s conduct was attacked. Whether the court really relied on a market power threshold or determined the best competitive makeup of the industry, but failed to articulate its reasoning, is impossible to determine. Indeed, given the obviousness of the result, the presiding judge may not have thought all that deeply about it.

To gain insight into the analytical framework courts actually apply, one needs to examine the difficult cases: (1) those in which signs of market power exist, yet the court does not impose liability and, (2) those cases where power appears to be lacking, yet the courts impose it. To be sure, courts typically recite the rhetoric of dichotomy in these cases as well.\(^{342}\) A closer read, however, reveals their focus is on competitive makeup.\(^{343}\)

1. Market Power in Per Se Cases

In per se cases, courts impose liability without market power, clearly relying on a competitive makeup analysis.\(^{344}\) When the agreement is naked, the value of short-run competition predominates and, thus rivalry must govern that realm.\(^{345}\) Integrated agreements, however, have longer-run benefits that may outweigh the value of short-run rivalry.\(^{346}\) Cases involving integrated agreements are thus inappropriate for per se treatment.

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\(^{341}\) Id.

\(^{342}\) See, e.g., supra Part I.

\(^{343}\) Infra Part V.B.1–2.


\(^{345}\) See, e.g., United States v. Addyston Pipe & Steel Co., 85 F. 271 (1898); United States v. Topco Assocs., Inc., 405 U.S. 596, 608 (1972) (“It is only after considerable experience with certain business relationships that courts classify them as per se violations of the Sherman Act.”)

\(^{346}\) See, e.g., Bus. Elec. Corp. v. Sharp Elec. Corp., 485 U.S. 717, 735 (1988) (“Economic analysis supports the view, and no precedent opposes it, that a vertical restraint is not illegal per se unless it includes some agreement on price or price levels.”).
because the court must carefully balance the short- and longer-run benefits to determine the value of rivalry in each realm.

Within the antitrust dichotomy, per se cases can only be explained as a curious exception in which harm supposedly occurs even though the market power threshold is never crossed. The critic would presumably explain the per se rule as an administrative cost-saving device that courts use in cases where the defendant’s power is obvious.\textsuperscript{347} Easterbrook, however, did not believe that market power would be present in all per se cases. He thus urged courts to apply the market power screen to them.\textsuperscript{348} Also, scholars have recognized that in certain circumstances price fixing and other per se conduct can benefit consumers.\textsuperscript{349}

Even if market power was always present, the dichotomy could not explain why the identified pro-consumer benefits should be ignored in per se cases. Moreover, if the defendant’s possession of market power in these cases were obvious, the administrative costs of applying the rule of reason would be small, undermining the supposed administrative benefit.\textsuperscript{350} This is particularly true given that per se cases can be quite complex when defendants plausibly assert that their agreement was integrated in a way that benefitted consumers.\textsuperscript{351}

\textsuperscript{347} Robert Bork, \textit{The Antitrust Paradox} 269 (1978) (explaining that if defendants in per se cases “were allowed to prove lack of market power,” they could “introduc[e] … the enormous complexities of market definition into every price-fixing case”); see Donald L. Beschle, ‘What, Never? Well, Hardly Ever’: Strict Antitrust Scrutiny as an Alternative to Per Se Antitrust Illegality, 38 Hastings L.J. 471, 475 (1987) (“Judicial administration, it is argued, is much simpler under a per se rule, and businessmen may plan their activity with much greater certainty.”).

\textsuperscript{348} Easterbrook, supra note 16, at 16–17, 39.


\textsuperscript{350} Beschle, supra note 347, at 475–76 (“Arguing that types of activity can be identified as invariably anticompetitive is futile; counterexamples can almost always be put forward. Consequently, defenders of per se categorization are reduced to one of two unattractive alternatives. First, they can concede that per se categories may in some instances prohibit procompetitive activity, but argue that the overall benefits of per se categorization justify the result. Such an argument is unsatisfying because it explicitly sacrifices particular blameless defendants in order to search for an increase in general welfare. Second, per se defenders can narrow their categories to eliminate procompetitive counterexamples. This strategy, however, threatens to destroy those categories entirely. And if most of the once-condemned activity is returned to the realm of the rule of reason, the insight that certain types of behavior are particularly dangerous is lost.”).

\textsuperscript{351} See, e.g., Arizona v. Maricopa Cnty. Med. Soc’y, 457 U.S. 332, 348, 337–38 (1982) (explaining that each of the three judges on the appellate panel drew a different conclusion as to whether the per se rule should apply and the U.S. Supreme Court split 6–3).
In any event, the Supreme Court has squarely rejected the notion that the per se rule condemns restraints based on a presumption of market power.\textsuperscript{352} In \textit{FTC v. Superior Court Trial Lawyers Association},\textsuperscript{353} the D.C. Circuit applied the rule of reason to an agreement among criminal defense attorneys not to take appointments unless the city increased its fees.\textsuperscript{354} Although naked boycotts of this type had been held illegal per se,\textsuperscript{355} the lower court believed that because this one involved petitioning the government, the FTC was required “[t]o prove, and not merely presume, that the boycotters ha[d] market power.”\textsuperscript{356}

In overturning the D.C. Circuit’s decision and applying the per se rule, the Supreme Court rejected the notion “that the categorical prohibitions against price fixing and boycotts are merely rules of ‘administrative convenience’ that do not serve any substantial governmental interest unless the price-fixing competitors actually possess market power.”\textsuperscript{357} The Court held that restraints are illegal per se because they “pose[] some threat to the free market” and may “inflict real injury upon particular consumers or competitors” despite the defendants’ lack of market power.\textsuperscript{358} Liability is thus imposed without a market power threshold because the defendants restrained competition in a realm best governed by short-run rivalry.

\textbf{2. Market Power in Non-Per Se Cases}

The following cases illustrate the courts’ use of the competitive makeup approach in a variety of situations in which the courts recited the rhetoric of dichotomy.

\textsuperscript{352} To be sure, the Court has held that “[t]he rationale for per se rules in part is to avoid a burdensome inquiry into actual market conditions in situations where the likelihood of anticompetitive conduct is so great as to render unjustified the costs of determining whether the particular case at bar involves anticompetitive conduct.” \textit{Jefferson Parish Hosp. Dist. No. 2 v. Hyde}, 466 U.S. 2, 15–16, 15 n.25 (1984). In a later case, however, the Court noted the import of the phrase “in part,” stressing the rule has a substantive component. \textit{FTC v. Super. Ct. Trial Lawyers Ass’n}, 493 U.S. 411, 432 n.15 (1990).


\textsuperscript{354} \textit{Id.} at 428–36.

\textsuperscript{355} See \textit{Fashion Originators’ Guild of Am., Inc. v. FTC}, 312 U.S. 457 (1941).


\textsuperscript{357} \textit{Id.} at 430, 432 n.15.

\textsuperscript{358} \textit{Id.} at 434–35; \textit{United States v. Socony-Vacuum Oil Co.}, 310 U.S. 150, 224–26 n.59 (1940) (“[T]he fact that the group [fixing prices] cannot control the market prices does not necessarily mean that the agreement ... has no utility to the members of the combination. The effectiveness of price-fixing agreements is dependent on many factors, such as competitive tactics, position in the industry, the formula underlying pricing policies.”).
This case counters the critic’s argument that the Court must have concluded market power exists whenever it recognizes potential liability. An independent service organization sued Kodak, alleging that the copier manufacturer (1) unlawfully tied the purchase of spare parts for its copiers to the labor required for the repair and (2) attempted to monopolize the provision of service for its machines. The plaintiff did not dispute Kodak’s lack of power in the copier market, but argued that Kodak had power in the parts market. Kodak responded that even if it were the sole producer of parts for its own copiers, it could not raise the price profitably because competitors in the copier market would exploit Kodak’s high prices on parts and service to win copier sales. Any extra profit Kodak might earn on the service side would be lost on the copier side.

The trial court agreed, granting summary judgment after “truncated discovery,” but the Supreme Court saw the case differently. The holding had little to do with Kodak’s share of any market, barriers to entry, excess supply, or any other structural factor typically associated with the first stage of the antitrust dichotomy. Rather, the Court relied on two theories about the appropriate role of competition in the copier industry, holding that the plaintiff had a right to discovery into whether rivalry would best govern the realm of parts and service.

Writing for the Court, Justice Blackmun cited the possibility that consumers would be harmed because they may (1) not have known the full extent of copier service costs when they bought the machine, and (2) have been locked into paying supra-competitive parts and service prices because doing so was more economical than purchasing a new copier. In addition, the Court reasoned that while innovative marketing strategies—such as a low upfront price with additional payments depending on the customer’s need for service—can be pro-competitive, one that

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360 Id. at 466 n.10.
361 Id. at 464.
362 Id. at 465–66.
363 Id. at 474 n.21.
364 Id. at 465–67.
365 Id. at 456.
366 Id. at 453.
367 Id. at 451.
368 See id. at 503–04.
369 Id. at 472–77.
involved limiting customer choice on parts and service in the copier industry might not be.\textsuperscript{370}

This analysis is a competitive makeup assessment. The Court instructed the district court to go beyond the structural arguments typically associated with market power and determine whether the best competitive makeup in the copier industry would include competition in the aftermarket for parts and service.\textsuperscript{371} Although the Court recited the paradigmatic rhetoric,\textsuperscript{372} using the term market power in the context of a theoretical assessment of the value of rivalry in particular realms strips the concept of its traditional meaning. Market power cannot block the court from considering how competition operates in an industry, as Easterbrook envisioned it would, if a court can only understand whether the defendant has power by determining whether competition in a particular realm best serves consumer interests, as the Supreme Court required the lower court to do in \textit{Kodak}.\textsuperscript{373}

Both the Department of Justice’s amicus brief\textsuperscript{374} and a dissenting opinion joined by three Justices made this point.\textsuperscript{375} The Court, they explained, had essentially held that “every maker of unique parts for its own product ... [has] market power no matter how unimportant its product might be in the market.”\textsuperscript{376} Concluding that a firm concededly lacking “power” in its product’s market, somehow has “power” in a sub-market for spare parts,\textsuperscript{377} is to recognize, in Justice Scalia’s words, “a curious form of market power”\textsuperscript{378} that extends the concept beyond where the “reasoning ... [justifying it] leaves off.”\textsuperscript{379}

\textsuperscript{370} \textit{Id.} at 478–79.
\textsuperscript{371} \textit{Id.} at 470 (“Even if Kodak could not raise the price of service and parts one cent without losing equipment sales, that fact would not disprove market power in the aftermarket.”).
\textsuperscript{372} \textit{Id.} at 477 (holding that “Kodak has failed to demonstrate that respondents’ inference of market power in the service and parts markets is unreasonable”).
\textsuperscript{373} See \textit{id.} at 467–70.
\textsuperscript{374} \textit{Id.} at 470 n.16 (quoting the government’s argument in its amicus brief, “[t]he ISOs’ claims are implausible because Kodak lacks market power in the markets for its copier and micrographic equipment. Buyers of such equipment regard an increase in the price of parts or service as an increase in the price of the equipment, and sellers recognize that the revenues from sales of parts and service are attributable to sales of the equipment. In such circumstances, it is not apparent how an equipment manufacturer such as Kodak could exercise power in the aftermarkets for parts and service”).
\textsuperscript{375} \textit{Id.} at 487–91 (Scalia, J., dissenting).
\textsuperscript{376} \textit{Id.} at 493.
\textsuperscript{377} \textit{Id.} at 489.
\textsuperscript{378} \textit{Id.} at 493.
\textsuperscript{379} \textit{Id.} at 489. Critics may claim \textit{Kodak} has been undermined by the Court’s more recent decision in \textit{Verizon}. There, Justice Scalia wrote for the majority that “the possession of monopoly power will not be found unlawful unless it is accompanied by an
Whether the Court’s Kodak decision was correct or not, it followed a competitive makeup approach rather than the paradigmatic dichotomy.

b. Rothery Storage

In Rothery Storage & Van Co. v. Atlas Van Lines, Inc., the plaintiffs alleged that Atlas Van Lines, a moving company, and its network of small movers agreed to exclude from the network any mover that competed with Atlas. In a famous opinion for a D.C. Circuit panel, Judge Bork began by concluding “the rule of reason [could not have been] offended since Atlas’ market share is far too small for the restraint to threaten competition.” At that point, the case looked to be a straightforward application of the paradigm, dismissed at stage one of the dichotomy because the defendant lacked market power.

Judge Bork, however, revealed the dichotomy’s falsity by what he wrote next. Embedded within the court’s initial conclusion that Atlas was too small to do harm, he recognized, was an implicit assumption about the realms of the moving industry that should be governed by competition. He acknowledged what courts often leave unstated—that the best competitive makeup of the moving industry permitted networks to foreclose short-run competition from their members. Outside competition by affiliated carriers was not part of the best competitive makeup, Judge Bork explained, because “restraints [on outside competition could] only be intended to enhance efficiency.”

That language appears to signal a two-stage inquiry into power and then conduct. A closer look at the case, however, reveals something more is going on. The defendant in Verizon engaged in many acts that hindered the ability of competitors to compete in the short run and likely increased consumer prices. Id. at 404–05 (recognizing that respondent alleged that Verizon “filled rivals’ orders on a discriminatory basis as part of an anticompetitive scheme to discourage customers from becoming or remaining customers of competitive LECs, thus impeding the competitive LECs’ ability to enter and compete in the market for local telephone service”). Nothing in the standard dichotomy explains why those practices should have been permitted. To conclude that the challenged conduct was not “anticompetitive,” the Court had to determine the best competitive makeup of the telecom industry did not require rivalry in the realms that the defendant foreclosed.

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380 792 F.2d 210, 213 (D.C. Cir. 1986).
381 Id. at 214. “Analysis might begin and end with the observation that Atlas and its agents command between 5.1 and 6% of the relevant market, which is the interstate carriage of used household goods.” Id. at 217.
382 Id. at 214.
383 See id. at 223–27.
384 Id. at 229 n.11.
could not “have been intended to” harm consumers.\footnote{Id. at 214.} By ultimately conflating the inquiry into consumer harm with the court’s market power analysis, Judge Bork effectively recognized that the two are part of a unitary competitive makeup inquiry.\footnote{Id. at 230 n.11 (stating that “[a]ntitrust adjudication has always proceeded through inferences about market power drawn from market shares” without citing a single Supreme Court case in support).}

c. Staples–Office Depot Merger

In \textit{FTC v. Staples, Inc.},\footnote{970 F. Supp. 1066 (D.C. Cir. 1997).} the U.S. District Court for the District of Columbia followed a similar path, enjoining the merger between Staples and Office Depot.\footnote{See infra notes 393–96 and accompanying text. See generally Staples, 970 F. Supp. 1066.} It shoehorned the case into the paradigmatic rubric by defining the market as “office supply superstores,” a \textit{market} in which the court could infer the merged firm would have power based on its large share.\footnote{Staples, 970 F. Supp. at 1074–82 (defining the relevant product market as office superstores).} As in \textit{Kodak}, however, this was a curious form of market power. The court recognized that lots of stores sold office supplies and were easily accessible to businesses large and small.\footnote{Id. at 1078.} And like Judge Bork, the court did not simply rely on its structural market analysis. It explained quite carefully how anticompetitive effects would flow from the merger despite the apparently competitive options.\footnote{Id. at 1081–86, 1082 nn.13, 14 (determining that the merger would have anticompetitive effect).}

Once again, the court’s analysis fits more comfortably within the framework of determining the best competitive makeup. In the office supply industry, the court held, short-run rivalry should govern the realm that included office superstores.\footnote{See id. at 1083–86.} To force that conclusion into the paradigmatic dichotomy is either (1) to deny the reasoning process through which the court actually decided to block the merger, or (2) to strip the market power concept of the attributes that it needs to play the threshold role that the antitrust dichotomy requires it to play.

\begin{footnotes}
\footnote{Id. at 214.}{Id. at 230 n.11 (stating that “[a]ntitrust adjudication has always proceeded through inferences about market power drawn from market shares” without citing a single Supreme Court case in support).}
\footnote{970 F. Supp. 1066 (D.C. Cir. 1997).}{See infra notes 393–96 and accompanying text. See generally Staples, 970 F. Supp. 1066.}
\footnote{Staples, 970 F. Supp. at 1074–82 (defining the relevant product market as office superstores).}{Id. at 1078.}
\footnote{Id. at 1081–86, 1082 nn.13, 14 (determining that the merger would have anticompetitive effect).}{See id. at 1083–86.}
\end{footnotes}
d. Lundbeck

A drug company, Lundbeck, Inc., acquired the only two drug treatments for a potentially life-threatening heart condition afflicting premature infants. First, it acquired Indocin IV, the only drug treatment then on the market and immediately increased the price by 40 percent. Shortly thereafter, it acquired another drug, NeoProfen, that upon Food & Drug Administration (FDA) approval would become the second available treatment. Within days of the second acquisition, the drug company increased Indocin IV’s price 1,278 percent. Four months later, the FDA, as expected, approved NeoProfen and the drug company priced it just a few dollars below Indocin.

The FTC sued, alleging that the defendant violated the antitrust laws by acquiring the second drug. The structural evidence of market power was overwhelming. The defendant owned the only two drug treatments, both of which were effective 75–90 percent of the time. The FDA explicitly rejected labeling that would have allowed NeoProfen to claim superiority to Indocin, thus recognizing the two were interchangeable. Also, if there were any doubt, the defendant’s internal documents confirmed the drugs were substitutes. Lundbeck purchased NeoProfen so it

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394 Id. at *6.
395 Id. at *5.
396 This transaction was too small to require mandatory reporting to the antitrust enforcement agencies. Minnesota v. Ovation Pharms., Inc., 2008 WL 5347144 ¶ 22 (D. Minn.) (Complaint) (“The size of the NeoProfen transaction fell below the regulatory threshold for reporting acquisitions to the federal antitrust agencies.”).
398 Id. at *2–3.
399 Id. at *8–9.
400 Id. at *1; Complaint ¶ 6–7, Minnesota v. Ovation Pharms., Inc., No. 08CV06379, 2008 WL 5347143 (D. Minn. Dec. 16, 2008) (No. 08-06381).
402 Id. at *3.
403 Lundbeck, 2010 WL 3810015, at *10–11 (finding the defendant’s internal documents showed that the company believed that “NeoProfen will capture a significant portion of the pharmaceutical PDA market at the expense of Indocin IV” and “base case Indocin IV forecast assumed volume and sales loss due to new competition (generic entry and NeoProfen). Based on NeoProfen diligence completed to date and associated analysis, we have confirmed our deal model sales projections and the expected sales loss.”) (emphasis added).
could “cannibalize [its] Indocin IV sales in a controlled manner” and “re-
alize a more stable revenue stream for both products.” 404 Finally, the de-
fendant trained its sales staff to convince hospitals to switch from Indocin,
which was about to face generic competition, to NeoProfen, which had con-
tinued patent protection. 405 To assist its sales staff in this effort, the de-
fendant set NeoProfen’s price at a percentage discount below Indocin
IV to, internal documents stated, take “away potential pharmacoeconomic
debate” and allow sales representatives to focus on product differentiation
without “spending time with the pharmacy director on price.” 406

A trial court implementing the standard antitrust dichotomy would see
an easy decision: the relevant market consisted of drugs treating heart
defects in premature infants, and the defendant had market power because
it owned the only two. As if that were not enough, the defendant had in-
creased the price more than ten-fold only after acquiring the second drug.
A relevant market containing both drugs would have seemed obvious.

The district court, however, did not implement the antitrust dichotomy.
It considered the value of competition within particular realms of the drug
industry. 407 At trial, the parties offered conflicting testimony as to whether
doctors considered price in choosing between the two drugs. 408 The district
court, however, did not implement the antitrust dichotomy. It considered
the value of competition within particular realms of the drug industry. 409 At
trial, the parties offered conflicting testimony as to whether doctors consid-
ered price in choosing between the two drugs. 410 Latching onto that testi-
mony, the court “found” doctors would not consider price and thus (1) the
two drugs were in separate markets and thus (2) the acquisition of the se-
cond drug did not create market power. 411 Viewed through the standard
paradigm, the decision appears inexplicable. Even if doctors were the sole

404 Id. at *11, *13 (referring to market shares based on a PDA market).
405 Id. at *12–13.
406 Id. at *11.
407 Id. at *19–22.
408 Id. at *14–19 (for example Dr. Mark Mammel, a neonatologist in St. Paul Minne-
sota testified that he “would feel comfortable treating the vast majority of his patients
with either NeoProfen or Indocin IV,” but “[w]hen deciding between two possible treat-
ments, [he] chooses the one that is safer, if he is persuaded that one is indeed safer. He
makes that decision without regard to cost”); id. at *21 (the court also cited evidence that
Bedford Laboratories—which had obtained FDA approval for a generic version of Indo-
cin—did not forecast any impact of generic Indocin IV on NeoProfen).
409 Id. at *29–30.
410 Id. at *20–21.
411 Id. at *21.
decision-makers—which they were not—those doctors would be influenced by the quality of the two drugs, a basis of competition as legitimate as price.

One can understand—if not agree with—the court’s decision under the best competitive makeup approach. In its answer to the FTC’s complaint, the defendant characterized the competitive makeup of the market in the following way:

The group of patients for whom the drugs even theoretically may be acceptable clinical substitutes is small, such that a profit maximizing supplier of either drug would not alter prices across all sales in competitive response to a price change by the other. Further, that already small theoretical population will decline as more doctors turn to the safer drug and migrate to NeoProfen, and those doctors who want to use indomethacin, for whatever clinical reason, have the option of a generic indomethacin.412

The court apparently agreed the drug industry did not require rivalry on price.413 Doctors prescribe drugs, the court believed, in the best interests of the patient’s health.414 The short-run benefit of price rivalry was thus small. Competition had much more value in regulating longer-run competition to invent new and improved drug treatments, and rivalry in the innovation realm would be stimulated by permitting drug makers to extract significant profit from their sale of approved drugs, as the defendant had done.415

The district court thus appears to have determined the best competitive makeup of the industry did not require rivalry on price or short-run quality.416 Whether the court correctly decided this case is a complicated question that should have been open to de novo review. By ostensibly resting its decision on stage one of the dichotomy, however, the court effectively isolated that decision from meaningful appellate review. This is the real problem to which this Article now turns.

412 Answer of Defendant Ovation Pharm., Inc., FTC v. Lundbeck, Civil No. 08-6379 (JNE/JJG), 08-6381 (JNE/JJG), 2009 WL 407279 (D. Minn. Jan. 13, 2009) (No. 08-06379 (JNE/JJG)).
413 See FTC v. Lundbeck, Inc., Civil Nos. 08-6379 (JNE/JJG), 08-6381 (JNE/JJG), 2010 WL 3810015 (D. Minn. Aug. 31, 2010).
414 Id. at *14.
416 See generally Lundbeck, 2010 WL 3810015.
VI. DE NOVO REVIEW OF ALL ANTITRUST ISSUES

In developing definitions of a market, courts do not assess market power directly by observing real world facts. They instead engage in a creative process to determine the best competitive makeup of the relevant industry. After conducting this analysis, however, the trial judge translates its results into the antitrust dichotomy’s terms, arbitrarily framing it as either: (1) a stage one market power determination limiting appellate review or (2) a stage two competitive effects assessment subject to plenary review. A trial judge should be able to think creatively about how competition operates in the industry before it, as the judge did in FTC v. Lundbeck. Given the importance of antitrust cases to the economy, however, a district court should not have the power to dictate the level of appellate scrutiny that its decision will receive as a result of its classification within the antitrust dichotomy.

If the Lundbeck court had held that the effect of the defendant’s acquisitions and pricing decisions did not harm consumers because longer-run innovation competition is more beneficial than short-run price or quality competition, that decision would have been reviewable de novo. Because the judge held the two drugs were in different markets, however, the decision could be stricken down only if it were clearly erroneous. Since there is no meaningful difference in the reasoning process that a trial court would use to reach either of these decisions, an appellate court should apply the same level of scrutiny in both cases. Additionally, because antitrust cases are both complex and important to wide segments of society, that review should be plenary.

Using a de novo standard to review all antitrust questions would be consistent with the federal courts’ existing practice of rigorously scrutinizing on appeal fact intensive issues with widespread social and economic impact. This Part first illustrates the harm caused by deferential review

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417 See supra notes 170–71 and accompanying text.
419 Similarly, if the trial court had ruled Alcoa lacked market power because recycled aluminum was in the market and thus Alcoa’s share was too small, appellate review would have been limited by the clearly erroneous standard. If instead, the trial court decided that the effect of Alcoa’s conduct with respect to virgin ingot harmed consumers, an appellate court would conduct de novo review. See generally Alcoa, 148 F.2d 416 (2d Cir. 1945).
of market structure questions under current antitrust law. It then reviews numerous constitutional and statutory questions that the courts review de novo despite the significant fact-finding that underlies the trial court’s decision. Finally, this Part shows antitrust liability questions are similar to those that the Court has chosen to scrutinize carefully.

A. Lundbeck as an Illustration of the Danger of Clearly Erroneous Review

The FTC appealed the Lundbeck case to the Eighth Circuit, arguing that the district court applied an incorrect legal standard.\(^{421}\) By looking to doctors, rather than hospitals or patients, and by ignoring marginal consumers and internal business strategy documents showing that the defendant itself viewed the two drugs as direct competitors, the Commission contended, the trial court erred in holding at stage one of the dichotomy that the two drugs were not in the same market.\(^{422}\)

The Eighth Circuit panel acknowledged the persuasiveness of the FTC’s argument, but found itself constrained by the clearly erroneous standard.\(^{423}\) The defendant’s strategy to promote NeoProfen over Indocin IV, the court reasoned, could “be interpreted to mean that while Indocin IV was vulnerable to generics, NeoProfen was not, and thus the products are not interchangeable.”\(^{424}\) Where two interpretations of the evidence are plausible, the court held, “the factfinder’s choice between them is not clearly erroneous.”\(^{425}\)

The evidence showed some level of substitutability between the drugs, and thus the conclusion that they were in different markets was a discretionary one turning on the trial judge’s view of the best competitive makeup of the drug industry. The panel signaled that it might have decided the case differently were it open to plenary review.\(^{426}\) Judge Kopf, a district judge sitting by designation, wrote a concurrence describing the lower court’s heavy reliance on the doctors’ testimony as “perplexing.”\(^{427}\) Doctors, Judge Kopf recognized, had no incentive to rely on the economic factors that drive antitrust analysis.\(^{428}\) “That oddity seems especially strange,” he explained,

\(^{421}\) FTC v. Lundbeck, Inc., 650 F.3d 1236, 1239 (8th Cir. 2011).
\(^{422}\) Id.
\(^{423}\) Id. at 1242–43.
\(^{424}\) Id. at 1242.
\(^{425}\) Id.
\(^{426}\) Id. at 1243 (“Whether this court would come to the same conclusion is irrelevant.”).
\(^{427}\) Id. (Kopf, J., concurring).
\(^{428}\) Id.
“where, as here, there is no real dispute that (1) both drugs are effective when used to treat the illness about which the doctors testified and (2) internal records from the defendant raise an odor of predation.” He concurred in the panel opinion, however, because “the standard of review carries the day in this case as it does in so many others.”

B. Policy Drives the Standard of Review

Outside the antitrust context, the federal courts decide whether to treat a finding as one of fact, subject to deferential review, or one of law, subject to plenary review, by examining the role of appellate review in the substantive area of law, rather than the inherent nature of the question. Many issues bearing all of the earmarks of findings of fact are reviewed by appellate courts de novo. At common law, for example, the issue of whether probable cause existed to prosecute a case was a question of law, even though it clearly required the court to make findings about the information available to the entity filing the case. Under modern law, the Supreme Court has adopted a de novo standard for factual questions in cases dealing with key clauses of the First, Fourth, Fifth, Sixth, Eighth, and Fourteenth

429 Id.
430 Id. (emphasis added). Appellate courts have upheld trial court decisions as not clearly erroneous despite apparent doubt about the result. See, e.g., California v. Am. Stores Co., 872 F.2d 837, 841 (9th Cir. 1989) (“Were we to evaluate independently the evidence of the relevant product market, we might reach a different conclusion.”); SmithKline Corp. v. Eli Lilly & Co., 575 F.2d 1056, 1065 (3d Cir. 1978) (rejecting defendant’s attempt to show that district court finding of sub-market in certain types of antibiotics was clearly erroneous).
431 Some commentators have argued the distinction between questions of law and fact is incoherent. See John Dickinson, Administrative Justice and the Supremacy of Law in the United States 55 (1927); Leon Green, Judge and Jury 270 (1930); Louis L. Jaffe, Judicial Control of Administrative Action 546–48 (1965).
433 See infra Parts VI.B.1.a–VI.B.1.b.
434 See infra Part VI.B.1.c.
437 See infra Part VI.B.1.c.
Amendments. And some federal appellate courts have similarly reviewed factual questions de novo under important statutory schemes.

This subsection describes the issues appellate courts review de novo and compares them to the market definition and market power questions in antitrust cases. It concludes that nothing compels the courts to use a deferential standard to review market definition findings under stage one of the antitrust dichotomy. On the contrary, many of the issues appellate courts now review de novo require judges to implement intensely factual, vaguely worded standards designed to safeguard important social values. The Free Speech Clause of the First Amendment and the Unreasonable Search Clause of the Fourth are two examples. The high stakes in antitrust cases, in terms of both the availability of treble damages and attorney’s fees, the impact on the broader economy, and the need for creativity in determining the best competitive makeup of an industry, make the case for de novo review of all antitrust issues, if anything, stronger.

1. Constitutional Issues

The following sub-sections review areas of constitutional law in which the Supreme Court requires de novo review of fact findings.

a. Obscenity

In the late 1950s, the Court held speech that (1) appeals to a prurient interest, (2) is patently offensive, and (3) lacks social value, is obscene and may thus be suppressed. The Court noted the importance of the role of

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Constitutional issues on which appellate courts are not required to conduct an independent review of key fact findings are those in which the trial judge has unique access to evidence necessary to make critical credibility determinations. See, e.g., Patton v. Yount, 467 U.S. 1025, 1036 (1984) (juror impartiality); Maggio v. Fulford, 462 U.S. 111, 117 (1983) (per curiam) (competency to stand trial). Trial judges in antitrust cases do not have unique access to the information needed to assess the competitive makeup of an industry. They obviously rely on evidence provided by the parties and the testimony of experts.

439 See infra Part VI.B.2.


441 Roth v. United States, 354 U.S. 476, 481-87 (1957). The Court later refined the test in Miller v. California, declaring that:

The basic guidelines for the trier of fact must be: (a) whether ‘the average person, applying contemporary community standards’ would find that the work, taken as a whole, appeals to the prurient interest; (b)
the jury in these proceedings, thus deemphasizing the role of appellate courts. If the trial court followed the correct procedure, the finder of fact would have the last word, subject to deferential sufficiency of the evidence review.

Justice Harlan wrote a separate opinion, criticizing this approach. The constitutional issue, he wrote was “not really an issue of fact but a question of constitutional judgment of the most sensitive and delicate kind.” Every case involving the suppression of speech “has an individuality and ‘value’ of its own.” But that uniqueness, Harlan reasoned, weighed in favor of heightened review, not deference: “a reviewing court must determine for itself whether the attacked expression is suppressible within constitutional standards. Since those standards do not readily lend themselves to generalized definitions, the constitutional problem in the last analysis becomes one of particularized judgments which appellate courts must make for themselves.

Within a few years, the Court came to agree with Justice Harlan that appellate courts could not rely “on a ‘sufficient evidence’ standard of review,” but must instead review the decision de novo. Even after reformulating the test to reference local community standards, the Court reiterated that appellate courts were required to conduct probing review. Requiring a trier of fact to decide an obscenity case in accordance with its own understanding of the tolerance of the average person in their community, the Court explained, “does not mean ... that obscenity convictions

whether the work depicts or describes, in a patently offensive way, sexual conduct specifically defined by the applicable state law; and (c) whether the work, taken as a whole, lacks serious literary, artistic, political, or scientific value.

Miller v. California, 413 U.S. 15, 24 (1973) (internal citations omitted).

Roth, 354 U.S. at 489–91; see also Miller, 413 U.S. at 33–34 (“As the Court made clear in Mishkin v. New York, the primary concern with requiring a jury to apply the standard of ‘the average person, applying contemporary community standards’ is to be certain that, so far as material is not aimed at a deviant group, it will be judged by its impact on an average person, rather than a particularly susceptible or sensitive person—or indeed a totally insensitive one.” (citations omitted)).

Roth, 354 U.S. at 476.

Id. at 498 (Harlan, J., concurring in result and dissenting).

Id. at 497.

Id.

See Jacobellis v. Ohio, 378 U.S. 184, 190 n.6 (1964) (per Brennan, J.) (“[T]his Court cannot avoid making an independent constitutional judgment on the facts of the case as to whether the material involved is constitutionally protected.”).


Id. at 305.
will be virtually unreviewable.” On the contrary, the Court held that “[t]he type of conduct depicted must fall within the substantive limitations suggested” by the Court, and appellate courts had a responsibility to ensure the preservation of constitutional values.

b. Libel

In *New York Times Co. v. Sullivan*, the Court again adopted an imprecise standard that asked the judge or jury to find facts based on an understanding of human nature. The Free Speech Clause was held to require that a public figure in a libel case prove the defendant acted with actual malice, *i.e.*, purposely published a false statement or exhibited a reckless disregard for the truth. As in the obscenity cases, the Court imposed a duty on appellate courts to independently examine the record.

The Court’s reasoning mirrored that in the obscenity cases. It held this “rule of independent review assigns to judges a constitutional responsibility that cannot be delegated to the trier of fact.” This rule, the Court explained, “reflects a deeply held conviction that judges ... must exercise such review in order to preserve the precious liberties established and ordained by the Constitution.” Also, this is particularly true where the substantive standard is “not readily captured in ‘one infallible definition.’”

c. Probable Cause and Reasonable Suspicion

Before police officers may stop and frisk an individual, the Fourth Amendment requires that they must have a reasonable, articulable suspicion

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450 Id. (“[Applying] community standards does not mean, however, that juror discretion in this area is to go unchecked.”).
451 Id. For example, in *Jenkins v. Georgia*, the Court unanimously rejected the argument that, under *Miller*, once the jury resolved the obscenity question, the job of the appellate court was merely to determine whether there was sufficient evidence to support it. *Jenkins v. Georgia*, 418 U.S. 153, 159–60 (1974). Justice Rehnquist, writing for the Court, explained that appellate courts retained “the ultimate power ... to conduct an independent review of constitutional claims when necessary” to preserve First Amendment values. *Id.* at 160. *See also* *Pope v. Illinois*, 481 U.S. 497, 503 (1987); *Hamling v. United States*, 418 U.S. 87, 124 (1974).
453 *Id.* at 279–80.
454 *Id.* at 284–85 (citing *Edwards v. South Carolina*, 372 U.S. 229, 235 (1963)).
456 *Bose Corp.*, 466 U.S. at 510–11.
457 *Harte-Hanks Commc’ns, Inc.*, 491 U.S. at 686.
that crime is afoot.\footnote{458} In order to conduct a full-scale search, the officer must have probable cause to believe evidence of criminal activity will be found in the place to be searched.\footnote{459} In considering the appropriate standard of review, the Court explained that “[a]rticulating precisely what ‘reasonable suspicion’ and ‘probable cause’ mean is not possible. They are commonsense, nontechnical conceptions that deal with ‘the factual and practical considerations of everyday life on which reasonable and prudent men, not legal technicians, act.’\footnote{460}

The Court distinguished these sorts of legal standards from more precise concepts such as \textit{proof beyond a reasonable doubt} where greater deference is appropriate.\footnote{461} “[F]luid concepts” like probable cause, the Court explained, “take their substantive content from the particular contexts in which the standards are being assessed,”\footnote{462} and as a result, one case will seldom serve as precedent for another.\footnote{463} An appellate court must therefore review the trial judge’s decision de novo in order to protect Fourth Amendment values.\footnote{464}

d. Excessive Fines

The Constitution prohibits a government-imposed fine that is “grossly disproportional to the gravity of [a defendant’s] offense.”\footnote{465} This standard is similar in its lack of precision and its reference to communal values to the standards applied in other constitutional cases.\footnote{466} Not surprisingly, the Court required de novo appellate review.\footnote{467}

e. Punitive Damages

Historically, civil juries had unfettered discretion to impose punitive damages. In the early 1990s, however, the Court held that the Due Process Clause limited their use.\footnote{468} Punitive damages, the Court held, could not be

\footnotesize{\begin{itemize}
\item \footnote{458} Terry v. Ohio, 392 U.S. 1, 27 (1968).
\item \footnote{460} Ornelas v. United States, 517 U.S. 690, 695 (1996).
\item \footnote{461} \textit{Id.} at 696.
\item \footnote{462} \textit{Id.}
\item \footnote{463} \textit{Id.} at 698.
\item \footnote{464} \textit{Id.} at 691.
\item \footnote{466} \textit{Id.} at 336 (describing standard as “inherently imprecise”).
\item \footnote{467} \textit{Id.} at 336 n.10, 337–44.
\end{itemize}}
grossly excessive with respect to the defendant’s conduct,\textsuperscript{469} and it re-
quired de novo review of that fact-intensive question.\textsuperscript{470}

2. Statutory Issues

Lower courts have also applied de novo review to discretionary fact-
intensive questions under important statutory schemes that, like the antitrust
laws, have significant economic impact.\textsuperscript{471} For example, the economic
substance doctrine holds a transaction formally satisfying a provision of
the tax code may nonetheless be deemed improper if it has no economic
substance separate from tax avoidance.\textsuperscript{472} Also, in trademark infringement
cases, liability turns on whether an unauthorized use of the mark in com-
merce creates a likelihood of confusion.\textsuperscript{473} Although both of these issues
are fact intensive, at least three circuits—and perhaps as many as seven—
review economic substance questions de novo\textsuperscript{474} and several circuits simi-
larly apply plenary review to the likelihood of confusion issue.\textsuperscript{475}

\textsuperscript{469} BMW of N. Am., Inc. v. Gore, 517 U.S. 559, 562 (1996); TXO Prod. Corp. v. Al-

\textsuperscript{470} Cooper Indus., Inc. v. Leatherman Tool Grp., 532 U.S. 424, 431 (2001).

\textsuperscript{471} See Am. Elec. Power Co. v. United States, 326 F.3d 737, 741 (6th Cir. 2003).


\textsuperscript{474} See, e.g., Coltec Indus., Inc. v. United States, 454 F.3d 1340, 1357 (Fed. Cir. 2006)
(holding that “[t]he ultimate conclusion as to business purpose is a legal conclusion, which
we review without deference”); Dow Chem. Co. v. United States, 435 F.3d 594, 599 (6th
Cir. 2006) (same); James v. Comm’r, 899 F.2d 905, 909 (10th Cir. 1990) (same). Four
circuits have decisions going both ways or appear undecided. \textit{Compare} Estate of Strangi v.
Comm’r, 293 F.3d 279, 281 (5th Cir. 2002) (reviewing under “clear error” standard), Har-
bror Bancorp & Subsidiaries v. Comm’r, 115 F.3d 722, 727 (9th Cir. 1997) (same), Karr v.
Comm’r, 924 F.2d 1018, 1023 (11th Cir. 1991) (same), and Massengill v. Comm’r, 876
F.2d 616, 619 (8th Cir. 1989) (same), \textit{with} Compaq Computer Corp. & Subsidiaries v.
Comm’r, 277 F.3d 778, 780–81 (5th Cir. 2001) (reviewed de novo), IES Indus., Inc. v.
United States, 253 F.3d 350, 351 (8th Cir. 2001) (same), United Parcel Serv. of Am., Inc. v.
Comm’r, 254 F.3d 1014, 1017 (11th Cir. 2001), \textit{and} Sacks v. Comm’r, 69 F.3d 982, 986
(9th Cir. 1995) (same). Five other circuits have applied deferential review. Black & Decker
Corp. v. United States, 436 F.3d 431, 441 (4th Cir. 2006); Nicole Rose Corp. v. Comm’r,
320 F.3d 282, 284 (2d Cir. 2002); ASA Investerings P’ship v. Comm’r, 201 F.3d 505, 511
Serv. Co. v. Comm’r, 115 F.3d 506, 510 (7th Cir. 1997).

\textsuperscript{475} McMonagle v. Ne. Women’s Ctr., Inc., 493 U.S. 901, 904 (1989) (White, J., dis-
senting from denial of certiorari); Elby’s Big Boy of Steubenville, Inc. v. Frisch’s Rests.,
Inc., 459 U.S. 916, 917 (1982) (White, J., dissenting from denial of certiorari) (citing
Ninth and Second Circuit cases applying de novo review).
C. Comparing Antitrust Issues to Those That Courts Review De Novo

The line of cases described above contains two common elements. First, each involves an issue of significant public importance. Some deal with fundamental rights, such as free speech, others involve important economic issues, including punitive damages, excessive fines, and the likelihood of confusion in trademark cases.

Second, in these cases, the appellate courts have been unable to devise clear rules that would definitively resolve most disputes. Instead, the court must apply situation-specific standards that are imbued with meaning by the way courts apply them, rather than by the terms used to describe them. “The content of the rule,” the Court has explained, “is not revealed simply by its literal text, but rather is given meaning through the evolutionary process of common-law adjudication.” The concepts in these cases are “fluid” and “cannot be articulated with precision,” and independent appellate review ensures the appellate courts “maintain control of, and are able to clarify, the legal principles.” At its root, probing appellate review of important fact intensive issues “assure[s] the uniform general treatment of similarly situated persons that is the essence of law itself.”

These rationales for heightened review apply with full force to antitrust cases. To be sure, competition is not a fundamental right. The Supreme Court, however, has recognized the antitrust laws’ pseudo-constitutional status, describing them as “the Magna Carta of free enterprise[,] as important to the preservation of economic freedom and our free-enterprise

476 See supra Parts VI.B.1.a–VI.B.1.b.
477 See supra Part VI.B.1.e.
478 See supra Part VI.B.1.d.
479 See supra Part VI.B.2.
483 Cooper Indus., 532 U.S. at 436 (quoting Gore, 517 U.S. at 587 (Breyer, J., concurring)). The Court has echoed Justice Harlan’s more general concern expressed in an early obscenity case that “the constitutional values protected ... make it imperative that judges ... make sure that it is correctly applied.” Bose Corp., 466 U.S. at 502; see Harte-Hanks Commc’ns, 491 U.S. at 686 (“[O]nly through the course of case-by-case adjudication can we give content to these otherwise elusive constitutional standards.”).
484 See, e.g., W. Coast Hotel Co. v. Parrish, 300 U.S. 379 (1937).
Antitrust issues and those to which the courts now apply de novo review are thus indistinguishable.

CONCLUSION

Nothing approaching antitrust’s dichotomous analytic paradigm is true. Market definition is creative, not observational, and the ostensibly separate inquiries into market power and competitive effects are really a single endeavor designed to determine conceptually the industry’s best competitive makeup. Although that term of art is foreign to the antitrust vocabulary, it captures actual antitrust practice in the courts. Everybody knows pure competition is a fiction; all industries involve an amalgam of competitive and cooperative realms. Antitrust requires competition in

486 Clayton Act, 15 U.S.C.A. § 15 (West 2014) (providing that “any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue ... and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney’s fee”).
those realms where it serves consumer interests, and the case law supports the conclusion that courts use the best competitive makeup approach to determine when the law requires rivalry.

Antitrust thus has an artificial heart. The paradigm supposedly guiding it is false. As Kaplow illustrates, the rhetoric of market definition is a sham in the sense that courts do not observe consumer behavior and discover markets. But so is the rhetoric of market power. Knowing that a defendant has the ability to raise price profitably is just a small piece of the potentially relevant information necessary to resolve an antitrust case.

Where Kaplow’s project was unabashedly “destructive,” the goal here is revelatory. That is, to show that courts decide antitrust cases through a process of determining the best competitive makeup of an industry. Grappling with the interactions between competitive realms, cooperative realms, and those isolated from competition is a challenging task. One might question whether courts are capable of handling it. It would certainly be conceivable to imagine an antitrust regime governed by bright-line, prophylactic rules. That regime, however, would differ from the one we have, and Austrian economics provides a theoretical justification for concluding that thoughtful judges can do a better job of resolving antitrust issues than would mindless, automaton courts applying necessarily over- and under-inclusive bright-line, prophylactic rules.

More important, the Supreme Court has to date, including its most recent 2013 decision, demanded that federal district judges engage theory and make thoughtful antitrust decisions. To be sure, courts ostensibly continue to recite the rhetoric of the antitrust dichotomy. That process, however, may enable them to determine an industry’s best competitive makeup more effectively than a “just look at everything” approach would.

Although much of this Article is interpretive, attempting to explain what courts actually do when they say they are defining markets, the final Part offers a specific prescriptive proposal. Appellate courts should abandon the clearly erroneous standard of review with regard to market definition. The Supreme Court requires independent appellate scrutiny of fact-findings controlling important issues of public policy that are indistinguishable from the antitrust laws. It would thus be a small, but important, step to require de novo review of all antitrust issues.

488 Kaplow, supra note 9, at 466.
489 Id.
490 See Douglas Lichtman, Property Rights in Emerging Platform Technologies, 29 J. LEGAL STUD. 615, 641 (2000) (“The prominence of the rule of reason ... reflects a gradual consensus within the judiciary and also the academy that, when it comes to analyzing market structure, courts can be trusted with at least some degree of discretion.”).