The Foundations of Antitrust

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Events, Ideas, and Doctrines

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To my former Antitrust Division colleagues.

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PREFACE

During 42 years in the Antitrust Division of the U.S. Department of Justice, I read perhaps ten thousand court decisions and articles. In addition, I examined many old files within the Antitrust Division as well as records preserved at the Library of Congress and the National Archives. And I amassed a substantial collection of books and other materials on the history of antitrust. In retirement, I wrote the book I wanted to read by drawing on what I had learned over an entire career and what I could learn from all I collected and the extraordinary Internet resources now available.

This is a book for people who practice antitrust and for people who want to learn antitrust. For practitioners, the book supplements a treatise. For students, the book complements a casebook. I go beyond what courts have said and done to probe the ethos, logos, and pathos of antitrust; I present the foundations of antitrust in law, history, and economics. This also could be a book for people who take an interest in antitrust policy. Antitrust law was a populist impulse. After a century during which antitrust has grown ever more technocratic, antitrust is again a matter of public interest.

This book distills a huge amount of material, some excruciating to read, into discrete and digestible portions. The chapters cross reference and reinforce each other, but they do not presume that the reader knows what is in other chapters. Each chapter can be read as a free-standing treatment of a discrete

topic, and the reader is never required to turn to the back of the book for notes or references. Endnotes are totally dispensed with, and the references are placed at the back of the chapters. They include the sources cited, important uncited sources, and some suggestions for further reading.

The parts of this book approach antitrust in three distinct ways. Part I treats antitrust as history. To understand antitrust in the United States, one must know the events of antitrust's formative years from the end of the Civil War to the end of World War I. Part I chronicles the antitrust statutes enacted then, the economics and politics that shaped the statutes, early enforcement, efforts at reform, and the landmark court decisions. A few of the chapters cover familiar subjects, but no chapter is a rehash of prior antitrust literature, and several chapters recount events that almost were forgotten.

Chapter 1 is a short history of John D. Rockefeller and Standard Oil. They provided much of the motivation for an antitrust law and gave this area of law its name. Chapters 2 and 3 outline the "Trust Problem," how it was perceived by the public, and how it became a political issue. The "trust," from which antitrust got its name, began as a specific legal entity, but within a few years, a "trust" was anything in the business world that engendered concern. Chapters 4–5 review the legislative history of the Sherman Act and explore the intended meaning of the Act's prohibitions.

Chapters 6–7 detail what became of Standard Oil and similar "trusts proper" after passage of the Sherman Act, and review the disappointing record of the Sherman Act's first decade. Chapter 8 chronicles an antitrust movement that began in 1899, and Chapter 9 presents the antitrust policy of Theodore Roosevelt, who was called the "trust buster" but was less a friend than a foe to the Sherman Act.

Chapters 10–11 discuss the *Standard Oil* and *American Tobacco* cases decided by the Supreme Court in 1911. These cases seemed to fulfill the promise of the Sherman Act by breaking-up two giant companies, but they did little to clarify the law, and the American people were highly dissatisfied. Chapter 12 explains the antitrust debate in the 1912 election, and how the result was the 1914 Clayton Act and Federal Trade Commission Act. Both are closer to what Roosevelt campaigned for in 1912 than to what Wilson campaigned for. Chapter 13 concerns the 1920 *Chicago Board of Trade* decision, which gave content to the rule of reason announced in *Standard Oil*.

Part I has multiple overarching themes. One concerns what the Sherman Act was meant to accomplish. The history that led to the Sherman Act paints a reasonably clear picture of what it was meant to prohibit. Another overarching theme is that the 1914 legislation was the product of politics and impatience with the Sherman Act, and not of actual deficiencies in the Sherman Act. A final theme is that the 1914 legislation approached antitrust in a very different way from the 1890 Sherman Act. The Sherman Act defined *malum in se* offenses and was a law enforced by generalist prosecutors. The 1914 Clayton Act and especially the Federal Trade Commission Act created *malum prohibitum* offenses and introduced economic regulation by experts.

Part II treats antitrust as intellectual history by exploring some of the people and ideas that that shaped antitrust policy. Chapters 14–15 focus on the thinking of economists who were influential early in the 20th Century, and many of their ideas retain currency today. Chapter 16 presents relevant views of Louis D. Brandeis, who was a powerful advocate for many causes, but competition was not among them. Chapter 17 discusses the Chicago School of antitrust, which made its most enduring contributions to the methodology of antitrust analysis. And Chapter 18 deals with the contentious subject of the goals of the Sherman Act.

Part III treats antitrust as legal doctrine. Chapters 19–20 review the common law antecedents to the Sherman Act. The common law was badly described in the 1911 *Standard Oil* opinion and typically is omitted from law school antitrust curricula. Chapters 21–22 discuss the rule of reason and the per se rule, the two fundamental doctrines in antitrust law. Each is more nuanced than generally is appreciated. Nuances in the rule of reason are critical in defining the plaintiff's burden and the scope for justifications. Nuances in the per se rule are critical in defining what comes within the core per se prohibition and in criminal prosecutions conducted by the Antitrust Division.

Chapter 23 concerns the ancillary restraints doctrine which applies to restraints associated with legitimate, productive cooperation in joint ventures. This is the only aspect of antitrust doctrine that survived intact from English common law. Chapter 24 addresses the "Consumer Welfare Standard." The term has multiple meanings, and is the source of much failure to communicate. Chapter 25 discusses aspects of antitrust doctrine applicable in antitrust cases that might be brought against one of the tech

giants that now cause public concerns approaching those that motivated the Sherman Act. Lastly, chapter 26 examines the past, present, and future of legal doctrine on the global reach of U.S. antitrust law.

PRIMER

This book presumes basic knowledge of antitrust and legal institutions. For a reader with substantial knowledge on both subjects, this primer serves primarily to clarify the scope of the book. For readers new to antitrust, this primer provides background on the law and its enforcement to make the rest of the book understandable.

The major substantive provisions of U.S. federal antitrust law are contained in three statutes—the 1890 Sherman Act, the 1914 Clayton Act, and the 1914 Federal Trade Commission Act. This book focuses mainly on the Sherman Act, the first and most important federal antitrust law. Among the topics only touched on by this book are the subjects of substantive amendments to the Clayton Act. Price discrimination was the subject of the 1936 Robinson-Patman Act, and anticompetitive mergers were the subject of 1950 Celler-Kefauver Act.

The most important prohibition in federal antitrust law is that of Section 1 of the Sherman Act. It prohibits every "contract, combination . . ., or conspiracy, in restraint of trade or commerce among the several States or with foreign nations." This language is understood to prohibit every competition-suppressing commercial agreement with the required nexus to U.S. interstate or foreign commerce.

What constitutes, or proves, an agreement can be a complex and contentious topic, and it is not taken up in this book. The basic idea is that two distinct marketplace actors have reached a

mutual understanding on some aspect of how they will act in the marketplace. Critically, the agreement is the offense, so Section 1 can be violated even if no agreed upon action is ever taken.

Types of agreements are categorized based on the marketplace relationship between the parties to the agreement. When the parties are actual or potential competitors, and they agree on some aspect of how they will compete with one another, the agreement is "horizontal." When the parties have a manufacturer–supplier, manufacturer–distributor, or licensor–licensee relationship—so they are not direct competitors, but rather have more of a cooperative relationship—the agreement is "vertical."

Real-world companies can have many parts, and two companies often have both horizontal and vertical relationships. Any agreement they enter into is characterized for antitrust purposes on the basis of the agreement's subject matter. When one company supplies the other with an input, the agreement to do so is vertical even if the companies directly compete in other aspects of their operations.

Horizontal restraints are further categorized based on how the agreement relates to the relationship between the parties. Horizontal agreements are "naked" when the agreement serves no purpose other than to suppress competition. Horizontal agreements are "non-naked" when the parties are engaged in legitimate cooperation and the agreement plausibly facilitates that cooperation.

Under a "per se rule," an agreement is declared unlawful strictly on the basis of its competition-suppressing character, without regard to its actual marketplace impact or justifications based on special circumstances. The Sherman Act's core per se rule prohibits naked horizontal agreements to fix price or output, or to allocate territories or customers.

Agreements within the Sherman Act's core per se rule often are prosecuted as felonies. Criminal enforcement of the Sherman Act is within the exclusive province of the Attorney General, and is carried out by the Antitrust Division of the U.S. Department of Justice. The Antitrust Division prosecutes both companies and individuals, and convicted individuals normally are imprisoned. Relatively few convicted individuals serve more than two years, but sentences of up to five years have been imposed, and sentences of up to ten years are authorized.

The per se rule is a special case of the "rule of reason," which applies in all cases under Section 1 of the Sherman Act. The rule of reason condemns

restraints if they are unreasonably anticompetitive. In cases governed by the per se rule, unreasonableness is categorical. Unreasonableness is not categorical for agreements closely related to legitimate cooperation among competitors, as in research joint ventures, sports leagues, standard setting organizations, and trade associations. Unreasonableness also is not categorical for vertical agreements.

A substantial majority of antitrust suits in the United States are predicated at least in part on Section 1 of the Sherman Act, which most often is enforced through civil litigation. The federal government, state governments, and private parties all bring civil actions under Section 1. Civil actions can seek relief in the form of an injunction or in the form of damages, or both. Most private antitrust suits seek damages. Successful plaintiffs are awarded "treble damages," that is, an amount three times the damages shown to have been sustained.

Section 2 of the Sherman Act states that: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony . . . ." Criminal Section 2 cases were once common, but Section 2 has not been enforced criminally since violations became felonies in 1975. Moreover, no individual has ever been incarcerated upon conviction under just Section 2 of the Sherman Act.

In contrast to Section 1, which prohibits only concerted conduct, Section 2 prohibits unilateral or single-firm conduct. Section 2 prohibits exclusionary conduct, and what is and is not properly deemed exclusionary is a matter of on-going debate. Exclusionary conduct is contrasted with competition on the merits, although the dividing line between the two can be fuzzy and contentious. Section 2 enforcement is taken up by this book in the context of a possible case against one of the tech giants.

The vast majority of Section 2 cases are private. Successful Section 2 cases, public and private, have been infrequent in recent decades because the courts have made it difficult to establish a Section 2 violation. A successful Section 2 case could possibly result in a court-ordered restructuring of the defendant company, but that never happens. The AT&T breakup in 1982 was consensual.

The Federal Trade Commission (FTC) technically does not enforce the Sherman Act, but it does so as a practical matter. The Federal Trade Com-

mission Act prohibits unfair methods of competition, and courts have interpreted that category to include all conduct violating the Sherman Act. The FTC takes enforcement actions both through civil litigation and through its own internal administrative procedures. If the FTC initiates proceedings administratively, the fact-finding and the initial decision are internal to the FTC. Apart from the FTC administrative cases, all civil cases under federal antitrust law are initiated by filing a complaint in federal district court.